EXAMINATION

27 April 2009 (pm)

Subject SA4 — Pensions and other Benefits Specialist Applications

Time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *Enter all the candidate and examination details as requested on the front of your answer booklet.*

2. *You have 15 minutes before the start of the examination in which to read the questions. You are strongly encouraged to use this time for reading only, but notes may be made. You then have three hours to complete the paper.*

3. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*

4. *Mark allocations are shown in brackets.*

5. *Attempt all three questions, beginning your answer to each question on a separate sheet.*

6. *Candidates should show calculations where this is appropriate.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet, with any additional sheets firmly attached, and this question paper.

In addition to this paper you should have available the 2002 edition of the Formulae and Tables and your own electronic calculator from the approved list.

1 (i) Explain how the cost of the Pension Protection Fund (PPF) is met. [8]

(ii) Comment on the risks affecting the PPF and ways in which these can be managed. [10]

(iii) Describe how Trustees and sponsoring employers can reduce their PPF levy. [2]

[Total 20]

2 A sponsoring employer of a defined benefit pension scheme wishes to remove the liabilities from its pension scheme by offering deferred pensioners an enhancement to their cash equivalent transfer value. The enhancement above the Scheme's standard transfer value will be paid directly by the employer to the member's chosen pension arrangement.

The Scheme's normal retirement age is 65. The Trustees have the power to set the transfer value basis on advice from the Scheme Actuary. The discount rates for the Scheme's current transfer value basis are:

pre-retirement	gilt yield + 3.5%
post-retirement	gilt yield + 1.5%

(i) Discuss the main issues to be addressed by the employer when considering a suitable level of enhancement to offer to members. [8]

The employer decides to offer enhanced transfer values calculated using the following discount rates:

pre-retirement	gilt yield + 3.75%
post-retirement	gilt yield + 0.25%

All other assumptions will be the same as those used for the standard transfer value basis.

(ii) Assuming a standard transfer value of £10,000, estimate the enhancement in respect of a deferred pensioner who is:

(a) currently aged 30
(b) currently aged 55 [3]

(iii) Comment on the suitability of the basis that will be used to calculate the enhanced transfer values. [5]

Unaware of the enhancement exercise, the Trustees of the Scheme independently decide they are to review the Scheme's standard transfer value basis.

(iv) Set out the issues the Scheme Actuary will discuss with the Trustees in relation to setting the transfer value basis. [7]

After receiving the advice of the Scheme Actuary, the Trustees' decide to change the discount rates to:

pre-retirement	gilt yield + 3.1%
post-retirement	gilt yield + 1.0%

All other assumptions remain unchanged from the Trustees' previous standard transfer value basis.

(v) Determine the impact and discuss how the employer might alter its proposals in response to this new basis. [12]

[Total 35]

3 The Scheme Actuary to a defined benefit pension scheme also provides occasional advice to the sponsoring employer. The latest valuation is underway, the basis having been agreed with the Trustees.

The Finance Director (FD) of the sponsoring employer contacts the Actuary to ask for some advice. The Company is considering selling a large division of its business and is proposing that a bulk transfer will take place in respect of the pension benefits for the active members. The FD would like advice on determining an appropriate actuarial basis for the bulk transfer value.

(i) Outline how pension issues are usually addressed in a sale and purchase agreement. [8]

(ii) Discuss the main potential conflicts for the Actuary in providing advice to the FD. [10]

The FD has chosen to seek separate advice from another actuary. The Scheme Actuary has been provided with the following brief extract from this advice, and is preparing to discuss the proposed bulk transfer with the Trustees.

Assumption	*Funding Basis*	*Bulk Transfer Basis*
Discount Rate (pre-retirement)	5.75% p.a.	6.75% p.a.
Discount Rate (post-retirement)	4.50% p.a.	5.00% p.a.
Inflation	3.75% p.a.	3.50% p.a.
Salary increases	4.75% p.a.	4.00% p.a.
Pension increases (5% LPI)	3.25% p.a.	3.00% p.a.

(iii) Suggest how the difference between the valuation basis and bulk transfer basis might be justified for each assumption. You should assume that market conditions have not changed since the effective date of the funding valuation. [8]

(iv) Estimate the impact on the Scheme's funding liabilities of the transfer taking place using the following information and stating any further assumptions made. [4]

	All active members	*Active members of division to be sold*
Number	1600	1000
Total pensionable salary	£54.4m	£28.8m
Average age (liability weighted)	48	43
Average service (weighted)	12	10
Estimated accrued liability (actives)	£210m	Not known

You should assume that the Scheme retirement age is 65 and that all members accrue the same benefits for all pensionable service.

(v) Discuss why the Trustees of the Scheme might wish to pay a different amount to that determined using the sale and purchase agreement. [4]

(vi) Discuss the impact of this transfer on the financing of the pension scheme by considering the sponsor covenant, funding strategy and investment strategy. [11]

[Total 45]

END OF PAPER