Actuarial Society of South Africa

EXAMINATION

20 October 2020

Subject F204 - Pensions and Other Benefits Specialist Applications

Time allowed: Three hours and fifteen minutes

Total marks: 100

INSTRUCTIONS TO THE CANDIDATE

1. *Ensure that you are logged into your ProctorU account before attempting the examination.*

2. *Questions are only available in this ASSA Examination platform and may not be printed.*

3. *You are required to submit all of your answers in the ASSA Examination platform only. No uploads of answers (handwritten or otherwise) to the ASSA Examination platform will be accepted.*

4. *You may not use any other computer program (e.g. Email, MS Word or Excel), files or open any other browsers during the examination.*

5. *You are strongly encouraged to use the first 15 minutes as reading time only, however, you may commence answering the paper whenever you are ready.*

6. *Mark allocations are shown in brackets.*

7. *Attempt all questions.*

8. *Show calculations where this is appropriate. You may use blank paper to carry out rough work calculations. You may use a calculator from the approved list only.*

9. *You may return to your answers to review and amend during the allotted examination time. Once you are happy with your answers you need to* ***Finish all and Submit*** *your work. Once you have submitted you will not be able to make any more changes to your answers.*

10. *It is the candidate's responsibility to ensure that all work is submitted BEFORE the end of the allotted examination time. Take this into account when planning your review and submission. There will be no time announcements.*

Note: Answers will be saved automatically during the examination. However, the Actuarial Society of South Africa will not be held responsible for loss of data where candidates have not followed instructions as set out above.

END OF INSTRUCTIONS

QUESTION 1

You have recently been appointed as the valuator to a large defined contribution pension fund. Pensions for retiring members are currently purchased outside the fund, but this practice has only been in force since 1 January 2015. Pensions for members who retired prior to this date were purchased with an insurer through a bulk pension outsource exercise at the end of 2014.

The fund's most recent set of financial statements at 31 December 2019 shows a positive difference between the fund's total value of assets and the total value of liabilities.

The fund's new auditors have recommended to the trustees that this amount, which is held in the financials as an unallocated amount, be allocated to active members as at the date of the most recent financial year end, and that this is done in the form of a once-off addition to investment returns.

The Chairman of the Board of Trustees is eager to resolve the fund's apparent surplus urgently and at minimal cost. He has asked for your approval of the auditor's proposal.

i. Discuss the professional matters arising that you would need to consider in responding to the Chairman's request. [8]

ii. Explain in detail the checking process you would conduct to investigate the source of the surplus. [12]

Your investigations have shown that the surplus arose during the 2012 financial year. During that year, lower investment returns were allocated to active members than were earned on the fund's investments.

iii. In light of this, outline the steps for the technically correct approach to allocate this surplus amount. [7]

You have also discovered that the outsource of the pensions was partially funded from the surplus amount in the fund. As a result of this, the current surplus in the fund is insufficient to fund the enhancements suggested by the technically appropriate calculations you have done.

iv. Identify the issues you need to highlight to your client as a result of this. [6]

[Total 33]

REMEMBER TO SAVE

QUESTION 2

Company XYZ sponsors a defined contribution retirement fund for all its staff. The Trustees of the Fund are grappling with the default regulations and are not happy with their current investment strategy. They currently maintain a single strategy for all members of the Fund. The current strategy targets a return of inflation + 4% per annum. The Trustees have agreed to consider a life stage investment strategy.

i. Compare a single portfolio investment strategy to a life stage investment strategy with member choice and include the advantages and disadvantages of each. [13]

The member Trustees have concerns around members' understanding of the new strategy and their ability to make full use of the options available. The Chairperson has asked for your assistance in setting an appropriate communication strategy.

ii. Propose an appropriate communication strategy setting out all the considerations that would need to be taken into account in such a strategy. [9]

The Trustees agreed on and communicated the following life stage strategy:

Age band	**Investment portfolio**	**Targeted return**
< 50 years	Aggressive portfolio	CPI + 6%
50 – 55 years	Stable portfolio	CPI + 4%
55 – 60 years	Conservative portfolio	CPI + 2%
60 – 63 years*	Money Market Portfolio	CPI + 1%

* Normal retirement age is 63 years

Following the roll out of the member communication there have been a number of complaints from members, noting that the new strategy will result in lower benefits.

iii. Demonstrate, using a range of sample members and reasonable assumptions, whether or not the members' complaints are valid. State any assumptions that you make. [17]

iv. Taking into account the proposed life stage strategy, and your results above, propose to the Trustees a number of adjustments that might improve the proposed strategy. [10]

[Total 49]

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QUESTION 3

Blue Sky Operations has proudly continued to provide staff retirement benefits through a large well-funded defined benefit pension fund. The company believes that the defined benefit nature of the arrangement provides certainty with regards to the benefits for its long-serving staff members and has therefore continued with this arrangement despite all competitors in its sector having moved to defined contribution type arrangements.

Newly implemented default regulations require that on leaving the employer before retirement all members are to be made paid-up members of the Fund. Members then have the option of leaving these benefits in the Fund or transferring them to their new employer arrangements.

The Trustees cannot decide on whether these paid-up benefits should be managed on a defined benefit or defined contribution basis. You have been requested to advise the Board.

Set out a detailed assessment of the two options:

- explain the methodology for each option;
- identify the advantages and disadvantages and associated risks of each option; and
- recommend one option to Blue Sky with your reasons.

[Total 18]

[Grand Total 100]

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END OF EXAMINATION

