

INSTITUTE OF ACTUARIES OF INDIA

EXAMINATIONS

12th May 2008

Subject SA4 – Pensions and Other Employee Benefits

Time allowed: Three Hours (09:45* – 13.00 Hours)

INSTRUCTIONS TO THE CANDIDATE

- 1. Do not write your name anywhere on the answer sheet/s. You have to write only your Candidate Number on every answer sheet/s.*
- 2. *You have 15 minutes at 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 have then three hours to complete the paper.*
- 3. Mark allocations are shown in brackets.*
- 4. You must not start writing your answers in the answer papers until instructed to do so by the Supervisor.*
- 5. Attempt all questions, beginning your answer to each question on a separate sheet.*
- 6. Fasten your answer sheets together in the numerical order of the questions.*
- 7. The answers are expected to be India Specific application for the syllabus and corresponding core reading. However, substantially the core reading material is still taken from material supplied by Actuarial Education Company which are meant for UK Fellowship examination. The core reading also contains some material which is India Specific, mostly the IRDA regulation. In view of this, it should be noted that focal point of answers is expected to be India Specific application. However if application specific to any other country is quoted in the answer the same should answer the question with reference to Indian environment.*
- 8. In addition to this paper you should have available Actuarial Tables and your own calculator.*

Professional Conduct:

“It is brought to your notice that in accordance with provisions contained in the Professional Conduct Standards, if any candidate is found copying or involved in any other form of malpractice, during or in connection with the examination, disciplinary action will be taken against the candidate which may include expulsion or suspension from the membership of IAI.”

Candidates are advised that a reasonable standard of handwriting legibility is expected by the examiners and that candidates may be penalized if undue effort is required by the examiners to interpret scripts.

AT THE END OF THE EXAMINATION

Hand in BOTH your answer script and this question paper to the supervisor separately.

- Q. 1)** Employer sponsored retirement benefits in India, as they exist today, are covered under different legislative provisions for different retirement schemes. There has been a suggestion that all retirement benefit arrangements may be brought under proper regulation to cover every aspect of the arrangements. You are an Actuary and have been appointed by the Government to submit report covering wide range of issues. Please describe the points that you will include in your report on the following;
- a) Various issues involved in and possible methods of enhancing security of retirement benefits of members/ beneficiaries (32)
 - b) The funds of EPS '95 are mainly invested, at present, in government bonds. The yield on fund is low as against what could be obtained by investing in wider "variety of instruments. There is a suggestion to diversify the assets of EPS with a proportion to be invested in equities:
 - i). **Discuss** the asset sectors that might feature in the investment portfolio and summarize the main characteristics of each of them. (10)
 - ii). **Comment** on the view that "equities are a good match for salary-related liabilities". (8)
- [50]**
- Q. 2)** A Large Multinational company (company A) having a Defined Benefit Schemes and also a Defined Contribution Scheme in the UK has a wholly owned subsidiary in India and wishes to acquire another Company in India (company B). It has been talking to the company B for some time and has obtained a due diligence report. Arising out of this report certain matters have been referred to the Company B for comments/clarifications and seeking further information. You as a Benefit Consulting Actuary in India have been engaged by the company B to assist it in understanding certain aspects of the issues raised and preparing the responses. You have not worked with the company B in any capacity earlier. In this context please reply to the following:
- a) **List** the information that you will seek from the Indian Company so as to enable you to draft your response. (3)
 - b) The Company A has referred to the statutory requirement of UK for benefit value illustrations on regular basis under Defined Contribution schemes and has enquired of company B if there are such requirements in India and in cases it wanted to provide such illustration post-company B purchase, the Indian actuarial profession's guidance note that exists for the same for an Actuary to work on. **Draft** a response for the company B to consider. (5)

- c) The company A has enquired about Fringe Benefit Tax (FBT) in respect of Superannuation Benefits in India and has wanted to understand it with implications on whether to continue the scheme in case the company B was having one. **List** the points that would explain the nature of FBT and also the implications that company A is concerned about. (10)
- d) The company A due diligence report refers briefly to the subject matter of implied guarantee of interest rates under certain types of Provident Fund provisions in India and has requested more information/clarification on the subject from Company B. **Draft** a reply for the company B to consider which it can then send to the company A covering in particular the following points, amongst others;
- i. Background to the issue and professional framework requiring reporting in financial statements. (3)
 - ii. List the steps involved in applying Stochastic Model approach for valuing the interest rate guarantee. (3)
- e) The due diligence report of company A refers to the subject matter of Sponsor Covenant concept as applicable in the UK and company B has required of you to assist in understanding the same. In this context prepare reply to the following;
- i. What is the background to and definition of sponsor covenant? (1)
 - ii. How the sponsor covenant can be measured? (1)
 - iii. Describe the analogy of sponsor covenant with that of credit risk. (1)
 - iv. Discuss the circumstances when sponsor covenant should be considered. (3)
- f) The Trustees of the company B have insisted to appoint an actuary to advise them independent of the actuary that may be appointed by the management of the company B. The Management is concerned and would want to know as to why the Trustees should require this. List out possible reasons for the same. (3)
- g) The company A is of the initial view that they should not be providing for retirement benefits for the future service to the extent legally possible for the employees of company B. The management of the company B has wanted you to assist them in advocating in favour of such a provision. List the potential key objectives of an employer in providing retirement benefits. (4)

- h) The Due diligence report refers to the Accounting Standard 15 (rev.2005) issued by the Institute of Chartered Accountants of India and has raised number of questions seeking assistance of company B to gain better understanding of the various provisions contained therein. Draft response to the following questions in this context;
- i). What are the kinds of employees covered under AS 15 (rev.2005) and whether a formal employer-employee contract is necessary for the employee benefits liabilities to be covered under the Accounting Standard? (2)
 - ii). Whether an entitlement to earned leave which can be carried forward to future periods is a short-term or a long-term employee benefit? (3)
 - iii). What is the nature of a gratuity benefit scheme covered under a Group Gratuity Scheme with a life insurer? Whether it is a defined benefit plan or a defined contribution plan and whether or not the assets and liabilities of the scheme held by the insurer are required to be disclosed in the financial statements of the concerned enterprise. (3)
 - iv). In case an enterprise has created a separate Trust to administer a defined benefit plan, whether or not the assets and liabilities of the trust would appear in the financial statements of the enterprise. (1.5)
 - v). What is the meaning of the phrase “market yield at the balance sheet date on government bonds” used in paragraph 78 of AS 15 (rev.2005) in the context of the discount rate? (1.5)
 - vi). Is the application of the AS 15 (rev.2005) a change in accounting policy and what would be the disclosures required? (2)
- [50]**
