INSTITUTE OF ACTUARIES OF INDIA

EXAMINATIONS

18th May, 2011

Subject SA4 – Pensions and Other Employee Benefits

Time allowed: Three hours (9.45* - 13.00 Hours)

Total Marks: 100

INSTRUCTIONS TO THE CANDIDATES

1. ***Please read the instructions on the front page of answer booklet and instructions to examinees sent along with hall ticket carefully and follow without exception***

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 then have three hours to complete the paper.***

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

4. ***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.***

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

6. ***Mark allocations are shown in brackets.***

AT THE END OF THE EXAMINATION
Please return your answer book and this question paper to the supervisor separately.

Q. 1) a) A developing country is on the growth trajectory for the past two decades. It has a glorious past when the Joint Family System (JFS) was deep rooted in the society. Over a period of time the JFS has almost disappeared and the State could not introduce a Social Security System due to its limited resources.

The State's role in retirement benefits, at present, is very limited. The direct benefit provision is almost non-existent. There are few mandatory retirement benefits for the organized sector of the country. Further the State is providing some encouragement by way of tax efficient private provision and in the regulation of non-State benefit provision.

The present government of the country is committed to address the old age provision needs of its countrymen and wants to encourage private provision as well. The government also wants to provide adequate regulation in the pension and other employee benefit area. However the government is not interested to increase mandatory benefits and rather wants to enhance the scope of voluntary provision by its people.

You are a consulting actuary and the government has approached you to submit a report covering all the basic aspects regarding Voluntary Contribution Schemes (VCSs) to be set up by the government, as well as Additional Voluntary Contributions (AVCs) by the members of existing private pension schemes. Your report should also cover options for such voluntary contributions (VCs) and the provision of illustrations to the members of such schemes.

Discuss the points, with explanation, you will include in your report. (32)

b) The government also wants to introduce a formal Social Security Scheme in the country from a future date. Distinguish between the Joint Family System and the Social Security Scheme at the national level explaining the similarities the two systems have from pre-requisites point of view. (9)

c) The country has a well organized Actuarial Profession. The professional body of the country has, so far, not issued any guidance to its members covering Social Security Programmes (SSPs). Looking to the developments taking place in the country, the actuarial body has formed a Committee for working on a Guidance Note (GN). You are one of the members of such Committee.

Give your views in respect of the following:

a) The need for such a GN (2)

b) The Social Security Programmes (SSPs), with examples, the GN should cover (3)

c) The principles to be complied with by the actuary in his actuarial work covering an SSP (4)

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Q. 2) You are an actuary in a consultancy in India. Your colleague from the United Kingdom calls you to tell you that one of her clients is embarking on a potential acquisition of a part of a company in India. The UK business does not have any existing presence in India. You are informed that the target company is a diversified company with many divisions. The largest division is a manufacturing business, however, the division under consideration to acquire is a back office division. This particular division was itself acquired by the business 4 years ago and has grown over time from being solely a captive division to now serving its own external clients. It is considered a BPO in its own right.

The basic information you are given so far is that the total business has 7,500 people and is 25 years old and the BPO division up for sale is 9 years old currently with 1,500 people. The structure of the company is that there is only one legal entity in India and divisions are business units.

- The company in India currently has a funded Gratuity scheme which is set up under a self managed Trust. The last available actuarial valuation under AS15 (Revised) was conducted as at 31 March 2010 and the scheme was shown to be 85% funded. The Gratuity benefit is as per the Payment of Gratuity Act 1972, as amended. The main assumptions used were discount rate of 9%, salary growth of 5% per annum, attrition of 2% per annum.

- The company has a leave encashment benefit where employees may accumulate up to 90 days of unused leave which is paid as a lump sum encashment at the time of resignation, retirement or death. The company has not been funding this benefit and there has been no actuarial valuation of this benefit.

- There is a defined benefit pension scheme for 30 key executives of the company, of which 5 are currently part of the BPO division. This scheme is a frozen defined benefit pension plan where accrual was ceased on 31 March 2009 and salary was also frozen as at that date. The scheme has a 10 year service vesting criteria before an executive is entitled to any benefits. Upon retirement at age 60 or earlier the fixed, non-escalating benefit is secured through an annuity from an insurance company. The scheme is funded through a trust through an insurance company and at the last actuarial valuation as per AS15 (revised) the scheme has a surplus as at 31 March 2010 of 30% of liabilities.

You have been asked to prepare a presentation for the Board in the UK. Set out the points you would make in your presentation covering;

a. The broad occupational retirement benefits environment in India (5)

b. Outline the various stakeholders related to the benefit plans and their roles and vested interests that will need to be borne in mind (5)

c. A list of the key clauses that should be included in the Sale & Purchase agreement related to benefit plans (5)

d. Initial observations regarding the benefit plans as applies to the scenario of acquisition, in particular any risks for your client to bear in mind and the further investigations that will be required (15)

e. Describe the options for each schemes that the company needs to consider for the post acquisition implementation, whilst conducting the negotiations (10)

f. In general terms detail the background, requirements, principles and process for conducting an actuarial valuation of the leave accumulation scheme as per AS15 (10)

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