

INSTITUTE AND FACULTY OF ACTUARIES

Scenario Material

19 April 2024 (am)

Subject CP3 – Communications Practice Core Practices

INSTRUCTIONS FOR CANDIDATES

You are provided with this advance information to enable you to read and understand it in your own time and not under examination conditions. Please note that this is an examination to test your ability to communicate technical information to a non-technical audience. It is not a test of your technical actuarial knowledge or skills. As such, any technical actuarial information or techniques needed to answer the question will be provided to you. You do not need to spend time revising other subjects or researching further detail on the topics covered in the paper.

Everyday Building Design Solutions (EBDS) Limited is located in, and operates entirely in, Country X. EBDS employs architects, and the business started in 2015, at which time the EBDS Employee Benefits Scheme (EBDSEBS) commenced.

The following details are available:

- Extract from the annual government report for Country X for 2023
- Details of the EBDSEBS operated by EBDS
- Membership data for EBDSEBS
- Benefit statements
- Recent trustee discussion at 7 March 2024.

1 Extract of the annual government bulletin for 2023 published January 2024

Economic conditions and outlook

The outlook for Country X remains bleak in the short to medium term. The country has been experiencing cost-push inflation and despite recent fiscal measures inflation remains a key concern. Details of historic rates are contained in the following table.

Actual annual percentage inflation figures for 12 months ending:

<i>Year</i>	<i>March</i>	<i>June</i>	<i>September</i>	<i>December</i>
2019	2.8	2.9	3.1	3.0
2020	3.5	3.8	4.2	4.4
2021	4.8	5.1	5.2	5.5
2022	5.8	6.2	6.4	6.7
2023	6.9	7.3	7.5	8.2

The forecast is for the inflation rate to exceed 10% within the next 6 months.

The situation is caused in part by our high trade deficit. Conflicts not directly involving Country X are creating difficulties in importing goods and there are severe restrictions in our energy supplies. Domestically, recent droughts have led to poor crops, which is exacerbating the cost of food due to lower supplies. Record-breaking summer temperatures have occurred in 2023 and severe winters are predicted. These extremes are attributed by the government to climate change, and we therefore expect them to persist. The government is working hard to find solutions to sustain domestic food production with subsidies being offered to farmers.

The average annual earnings inflation figure at 30 December 2023 was 7% so this means that real disposable income is falling. This is causing increased hardship for some sectors of the population.

Government spending

- Pensions: the state pension will continue to be means tested and only those with total assets of less than \$100,000 will qualify for a pension paid by the state. The current state pension, payable from age 60, is \$100 per week and has been at this level since 2020. We remain committed to the philosophy that individuals should be self-sufficient in retirement, which is consistent with the country's culture of saving for retirement. Participation in an employer pension scheme is therefore compulsory and the self-employed must have a private personal pension saving arrangement.
- Healthcare: despite pressure to widen the provision of state-funded healthcare, only free state emergency hospital care will remain in place. There is an efficient and well-established market supplying private medical insurance to individuals with the option to add broader family cover.

2 EBDSEBS

This is a defined contribution scheme into which employees are automatically enrolled on joining the company.

The scheme has two membership tiers: standard tier and low tier. Members are automatically placed into the standard tier but can request to move to the low tier at any time.

Contributions are made by both the employer and employee and are invested in a choice of two unit-linked funds. Only one fund may be used at any time, with employee and employer contributions going into this fund.

On leaving service before retirement, the pension fund must be transferred elsewhere. This may be to a new employer, or into an appropriate private personal pension arrangement.

Contributions

Contributions vary by tier and are a percentage of basic salary according to the following table:

<i>Contribution made by</i>	<i>Standard (%)</i>	<i>Low (%)</i>
Employee	5	2.5
Employer	7.5	2.5

Investment options and charges

<i>Fund</i>	<i>Annual management charge (%)</i>	<i>Plan fee per month (£)</i>
Balanced ethical fund	2.5	2.75
Adventurous fund	3.25	3.00

All charges and fees are fixed. There are no charges on switching funds or transferring funds elsewhere.

Additional benefits

Additional benefits vary according to membership tier.

- Death in service life cover

This is a multiple of total earnings in the 12 months up to date of death.

<i>Tier</i>	<i>Multiple</i>
Standard	3
Low	1

The cost of this is paid entirely by the employer.

Medical underwriting only applies when a member of the low tier opts to rejoin the standard tier. This means that the member will be required to have some level of medical assessment on rejoining the standard tier. The cost of the assessment will be paid for by the employer.

The level of assessment will vary according to the member's basic salary at the time of the transfer back to the standard tier. Those with a basic salary in excess of \$80,000 will have a physical assessment and those with a basic salary of \$80,000 or lower will require a written medical report based on past medical treatment only. Dependent on the results, death in service cover may remain at the level of a low tier member but pension contributions will be as per the standard tier. The cost of the cover will however still be paid by the employer.

On death in service, the member's pension fund will also be available to the spouse or other member nominated as a financially dependent relative.

- Healthcare

Private medical insurance is paid for by the employer for members of the standard tier only. This benefit ceases if the member opts to transfer to the low tier. On first joining the standard tier there is no medical underwriting regardless of the earnings of the member. An excess of \$50 applies to each claim.

Members who rejoin the standard tier from the low tier are subject to medical underwriting which will be a medical examination paid for by the employer. The level of excess will increase to \$100 of each claim and any pre-existing medical conditions highlighted in the examination will be excluded from the cover. The premium will still be paid by the employer.

Retirement options

Members can retire from age 60. The latest possible retirement age is 70.

At retirement, the members enter a drawdown arrangement that gives the member the freedom to take any amount at any time from their accumulated fund until the pot is exhausted.

3 Membership data for EBDSEBS

The following data is taken from the scheme valuation at 31 December 2023. There are 3,571 members and the age distribution is not expected to change significantly in the future.

The actual distribution by category is as follows:

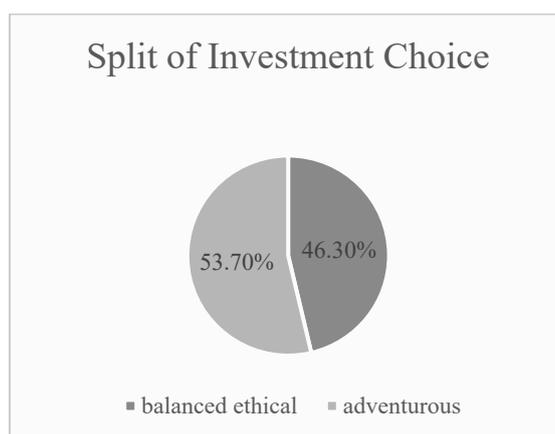
<i>Age band</i>	<i>Standard tier</i>	<i>Standard tier</i>	<i>Low tier</i>
	<i>Death in service multiple 1</i>	<i>Death in service multiple 3</i>	<i>Death on service multiple 1</i>
18–25	3	285	18
26–35	15	613	27
36–45	241	1,562	113
46–55	123	494	52
56–60	3	18	4

The first request to move to the lower tier was actioned in 2019 and the number of requests has been increasing sharply.

The average length of time in the low tier is currently 13 months. A survey of members in the low tier was conducted in October 2022, asking how long they expected to remain in this tier, and 71.3% do not expect to change before they retire or leave service.

Choice of investment and overall fund split

The following shows the investment split between funds based on number of members:



Of the overall fund size by value, 51.75% is invested in the balanced ethical fund.

4 Benefit statements

Every year on 1 March, members receive a statement that contains their personal details and relevant salary and earnings data. It shows their current investment choice, the amount currently in their pension fund and then a projected amount of their pension fund at retirement age 60 only.

This is a deterministic projection that allows for future salary growth and all charges. It assumes no change in membership tier or change of investment fund. Economic assumptions are reviewed annually. The projected funds are shown rounded down to thousands when included in the benefit statement.

It also contains their level of death in service life cover but has no reference to their health benefits.

The economic assumptions for 2024 benefit statements are:

- Basic salary growth rate: 7% p.a.
- Fund growth:
 - Balanced ethical fund: 5% p.a.
 - Adventurous fund: 6% p.a.

5 Recent trustee discussion: 7 March 2024

Trustees met following the publication of the annual benefit statements.

The Human Resources Director who is also Chairman of the Board of Trustees noted that the number of employees requesting a transfer to the low tier was the highest it had ever been. Transfers are actioned immediately on receipt of the request.

The trustees requested their advising actuary to perform some additional calculations to allow the trustees to understand the impact on the average member of moving between tiers. The examples show the impact on the projected retirement fund of the member if they:

- switch immediately into the low tier for a period of 12 months.
- switch immediately into the low tier and remain there until retirement.

The projections assume a salary of \$25,000 and an existing fund value of \$10,000. All other assumptions to be as per the 2024 basis and use the same method.

The results are tabulated below:

Fund value (in \$) at normal retirement age 60 for a member investing in the balanced ethical fund

<i>Number of future years in low tier</i>	<i>Current age</i>			
	<i>40</i>	<i>45</i>	<i>50</i>	<i>55</i>
0	176,478.56	108,575.91	62,141.53	30,791.75
1	173,389.91	105,833.66	59,706.81	28,630.08
All	79,740.65	51,646.77	32,244.80	18,969.56

Fund value (in \$) at normal retirement age 60 for a member investing in the adventurous fund

<i>Number of future years in low tier</i>	<i>Current age</i>			
	<i>40</i>	<i>45</i>	<i>50</i>	<i>55</i>
0	179,807.43	110,216.05	62,820.88	30,982.61
1	176,597.06	107,393.78	60,339.79	28,801.46
All	81,404.02	52,522.53	32,645.85	19,102.98

END OF SCENARIO MATERIAL