Response by TISA to:

Proposed revision to AS TM1: Statutory Money Purchase Illustrations

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About TISA

The Investing and Saving Alliance (TISA) is a unique, rapidly growing membership organisation for UK financial services.

Our ambition is to improve the financial wellbeing of all UK consumers. We do this by focusing the convening the power of our broad industry membership base around the key issues to deliver practical solutions and devise innovative, evidence-based strategic proposals for government, policy makers and regulators that address major consumer issues.

TISA membership is representative of **all sectors of the financial services industry.** We have **over 240 member firms involved in the supply and distribution of savings, investment products and associated services**, including the UK's major investment managers, retail banks, online platforms, insurance companies, pension providers, distributors, building societies, wealth managers, third party administrators, Fintech businesses, financial consultants, financial advisers, industry infrastructure providers and stockbrokers.

As consumers, the financial services industry and the economy react to and recover from the effects of the pandemic, the importance of the three key pillars of work that TISA prioritises has never been more apparent:

- **Strategic policy initiatives** regarding the financial wellbeing of UK consumers & thereby enhancing the environment within which the industry operates in the key areas of **consumer guidance, retirement planning, later lifetime lending, vulnerable customers, financial education, savings and investments**.
- TISA is recognised for the **expert technical support provided to members** on a range of operational and regulatory issues targeted at improving infrastructure and processes, establishing standards of good practice and the interpretation and implementation of new rules and regulations covering **MiFID II, CASS, ESG/RSI, operational resilience, Cyber Risk, SM&CR** and a range of other areas.
- **Digital transformation initiatives** that are driving ground-breaking innovation and the development of industry infrastructure for greater operational effectiveness and revenue promoting opportunity for firms. TISA has become a major industry delivery organisation for consumer focused, digital industry infrastructure initiatives – **TISAtech** (a digital marketplace that brings together financial institutions and FinTechs for greater collaboration and innovation) and **TURN** (TISA Universal Reporting Network – a digital platform providing a secure data exchange for financial services using blockchain technology) – alongside projects **Digital ID** and **Open Savings & Investment**. This reflects TISA's commitment to open standards and independent governance.

Executive Summary

TISA welcomes the opportunity to respond to the FRC consultation - Proposed revision to AS TM1: Statutory Money Purchase Illustrations.

It is clear from research that consumers highly value information relating to an Estimated Retirement Income and therefore important that the calculation limitations and assumptions are clearly and simply displayed alongside the calculated values.

The governance framework in place today places a degree of prescription on the calculation and schemes are required to set reasonable growth rates based on the underlying investment mix. Although Pension Dashboards will provide a consolidated view of all entitlements in scope, we do not believe this should trigger a change to existing rules. Illustrations are, at best, an educated guess but the complexity involved with the existing proposals create a false perception of accuracy and are disproportionate to the outcome.

We need to be mindful that this is an illustration and no more than an indicative value of what might be received in retirement. Schemes should have the ability to determine the most appropriate growth rate rather than following a rigid set of rules, which not all funds will comply to.

Although not wanting to undervalue an ERI, it remains crucial that the wording which accompanies an ERI on the Dashboard makes it clear that it is only a projection and provides no more than an indication of what the individual may receive based on financial assumptions and they will receive more or less than this. It would be bordering on the impossible to describe the calculation method of the existing proposals in a way which a typical consumer would understand.

We do agree that the annuity basis should be consistent and include inflation proofing, as a level basis creates misleading outcomes due to the loss of purchasing power year on year. This is not likely to be fully understood by the typical consumer. Given that pensions are now typically accessed through drawdown or UFPLS, it is important that the annual income quoted is a broad indicator of a sustainable income level, irrespective of the method of access.

Lastly, the pandemic has had an impact on life expectancy with a drop seen in 2020 according to ONS – it is important that the mortality tables used reflect accurate rates - series ‘16’ would now appear out of date.

Question responses

Q1. How supportive are you of the approach to prescribe the accumulation rate and form of annuitisation more precisely, in order to improve consistency across projections from different providers? In particular, do you have any concerns arising from the loss of independence and judgement allowed to providers to set these terms?

Inconsistencies which serve no purpose should be addressed and we agree that the income basis should be prescribed to ensure consistency. However, growth rates are at best an educated guess and the existing governance framework enables firms to project these to the best of their ability, based on reasonable assumptions and their knowledge of the funds available within their propositions.

The fiendishly complicated proposals relating to the annual calculation of growth rates creates a false perception of accuracy. The amount of work involved in producing an estimate is disproportionate and likely to overwhelm certain smaller schemes. They also do not appropriately factor in the government's desire for greater investment into illiquid assets.

If the existing governance and rules in place for SMPIs are perceived to be inappropriate, we would question why it takes the introduction of the Pensions Dashboard to acknowledge this and propose changes.

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Q2. What are your views on the proposed effective date of 1 October 2023?

This does largely depend on the final proposals and the level of complexity that is attached. Given the current scale of regulatory change firms are dealing with, the proposed date is challenging irrespective of the final proposals. Given the SMPI update schedule is normally aligned to the tax year and there remains no certainty as to when the Pensions Dashboard will be available to consumers, we would suggest any changes are implemented no earlier than April 2024.

Q3. What are your views on the proposed volatility-based approach for determining the accumulation rate?

We are not convinced that volatility is an appropriate measure. For instance, the highest grouping has a proposed growth rate of 7%, however the higher the group, the greater potential there is for the associated growth rate to be consistently inaccurate. Where a fund has insufficient history to calculate the volatility, the option to pick a 'similar fund' is too vague and needs to be expanded on.

There is a strong government drive for DC schemes to invest in illiquid assets, based on the assumption these will generate better returns over time. Many of these will be unquoted and if schemes do invest significant proportions of their FUM into these assets, the growth rates will be zero in real terms. This means the projections would fall significantly short of what they are likely to provide and risks creating negative consumer perceptions and disengagement. Growth rates need to be based on reasonable expectations.

If growth rates do become prescribed in nature, then we believe the simplest way to achieve this is based on asset class. Existing market catergorisations could be used to ensure the groupings are appropriate. This achieves the principle of consistency without the complexity of the proposals and still generates a growth rate which is based on reasonable assumptions but ultimately, it will always be no more than an educated guess. This approach would also be easier to describe to the typical consumer.

Q4. Based on an assumed CPI of 2.5% do you find the accumulation rates proposed for the various volatility indicators to be reasonable and suitably prudent?

Notwithstanding our concerns with the proposed approach, the rates do not seem inappropriate.

Q5. What are your views on the proposed approach to reflect derisking when calculating the accumulation rate assumptions?

We need to be mindful that the derisking strategy should be aligned to the expected decumulation option that will be used. Pre pension freedoms, it was fairly typical to derisk into 25% cash and 75% bonds because any drop in annuity rates would be broadly offset by an increase in the bond fund value. There are potentially more aspects to consider than actuarial based calculations in isolation.

Regarding the proposed approach, either method could yield the same result however we are comfortable for the proposed approach to be universally adopted. However, there is no guidance on the calculation required to account for derisking. In the absence of this, we would assume that firms could continue to calculate this in the same way that they do today.

Q6. What are you views on the proposals that the recalculation of volatility indicator should be annually as at 31 December with a 0.5% corridor?

Whilst we understand the reason for the proposed corridor, it highlights the complexity of the proposals and adds yet a further layer to the requirements.

Q7. What are your views on the proposed approach for with-profits fund projections?

We agree with the proposed approach.

Q8. Do you have experience of unquoted assets held in pension portfolios and what are you views of the proposed approach for unquoted assets? In particular do you regard a zero real rate of growth to be acceptable and if not please provide suggested alternatives with evidence to support your views?

There are various initiatives which are being implemented by government, designed to remove the barriers and encourage DC schemes to invest in illiquid assets. The reason being they may achieve better long-term returns and adds another option for diversification. The nature of these assets mean that many will be unquoted and therefore, a zero real rate of growth applied based on existing proposals. Yet applying a zero growth rate is at complete odds with the reason for government promoting this asset class.

For individuals who are members of schemes which fully embrace the government objective, their illustrations will be significantly undervalued and not provide even a remotely indicative value. Projecting such poor or zero performance is likely to result in consumer disappointment, generate negative perceptions and lead to disengagement. This highlights the number of moving parts there currently are in pensions, their competing priorities and the need to have a joined-up approach. It is crucial that these assets are valued on a basis which is more aligned to the long-term performance they are expected to achieve.

Q9. What are your views on the proposed approach to determine the accumulation rate assumption across multiple pooled funds?

This again illustrates the increasing complexity involved to generate an expected growth rate. External events such as the Russia/Ukraine war has resulted in fund suspensions, the creation of 'side pockets' and potentially another layer of complication for the existing proposals.

If returns were based on asset class, then the calculation becomes easier potentially using historic relative volatility for growth assumptions, with a straightforward weighted average calculation as required.

Q10. What are your views on the proposed prescribed form of annuitisation and treatment of lump sum at retirement? In particular, does the recommendation to illustrate a level pension without attaching spouse annuity cause you any concerns in relation to gender equality or anticipated behavioural impacts?

The overarching requirement is that irrespective of the basis used in the calculation of the SMPI, it is clearly displayed and the basis easy to understand.

Whilst there are very few scenarios where a lump sum is not taken, we understand that for most people, it will be needed to supplement retirement income and should not be considered as a windfall or bonus. We therefore understand why the proposal is to assume no tax-free cash is taken, however there should be appropriate wording clearly stating that tax-free cash is available and if selected, would mean the annual income would be reduced.

We do not agree with the current proposal on the annuity basis and believe this should default to inflation linked. Given that annual income may be taken for 20 years or more, it is important that the amount shown is inflation proofed and reflects the real annual value. The typical consumer will not make this adjustment themselves. The annual annuity payable on this basis may then more broadly align to a sustainable income level for drawdown or regular UFPLS.

Given the variables which can exist within the SMPI, it is important that modelling tools are easily accessible to enable consumers to change the basis e.g. add in tax fee cash and/or change the annuity basis.

Q11. What are your views on the proposed approach to determine the discount rate assumption when used to determine the annuity rates for illustration dates which are a) more than two years from retirement date and b) less than two years from retirement date?

We agree with the proposed approach.

Q12. What are your views on the proposed new mortality basis for determining the annuity rates where the illustration date is more than 2 years from the retirement date?

'Series 16' mortality tables relates to 2015-2018 however ONS data shows that the life-expectancy for both males and females in England fell in 2020 to the same level as a decade ago. It is important that the mortality tables used do reflect current trends and are representative of current figures.

Q13. Do you have any other comments on our proposals?

Although FCA illustrations are not strictly in scope, this consultation provides an opportunity to align some inconsistencies which currently exist. COBS states that illustrations must assume 2% inflation, which is in line with the government's long-term target. Given the strong focus on consistency, it would be appropriate to level up this assumption across the board so SMPI, ERI and FCA illustrations are projecting on the same inflation figure. Additionally, it would also be logical for FCA illustrations to adopt usage of the same mortality tables used for SMPIs.

Q14. Do you agree with our impact assessment? Please give reasons for your response.

N/A