CURTIS BANKS

PROPOSED REVISION TO - AS TM1: SMPI
CONSULTATION RESPONSE

APRIL 2022

1. 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?

The headline intention to align SMPI assumptions is in theory a logical one, on the grounds that, if done well, it will allow individuals to compare the projections they see on the dashboard from their various different providers, which in turn would drive better customer outcomes.

However, as a provider of open-architecture self-invested personal pensions (SIPPs), there are numerous and significant concerns with the approach detailed in this consultation paper. It is likely that the proposals will lead to situations where illustrations are not aligned between providers (which is the opposite outcome compared to the intention of the new regulations), based on concerns with lack of pricing information, volume of investment data required and the use of a 0.5% corridor. These are outlined in greater detail in responses to the appropriate questions below.

The highest accumulation rate as set out in the consultation paper is 7%. However, the FCA's Conduct of Business Sourcebook (COBS 13 Annex 2) states that a mid growth rate of no greater than 5% is to be used in projections. The two are directly at odds with each other.

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

Given that this consultation closes on 6 May 2022, meaning final rules will not be published until after that date, there will be a maximum of 17 months to develop, test and launch by 1 October 2023. The proposed new rules are extremely onerous for open-architecture SIPP providers. This, alongside all of the development required to connect to the pensions dashboards ahead of the staging dates in 2023, in addition to all of the other regulatory changes being introduced by the FCA and HMRC such as Consumer Duty, Operational Resilience, Vulnerable Customers, and changes to the normal minimum pension age, mean that these timescales are challenging for providers.

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

The premise is based on the availability of price volatility data for the previous 5 years. This will very likely be problematic for open-architecture SIPP providers who do not operate an investment platform

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and who do not manufacture or operate any investments, especially given that there has been no regulatory requirement or other purpose for SIPP providers to retain historic price volatility data. Depending on the level of historic data held by SIPP providers, or the length of time that assets have been held with that SIPP provider, this data may not be available to them, and would require significant external input and incur administrational costs each year going forwards. This is even assuming that the information is readily available to providers – often it may not be, for example, SIPPs often invest in assets that are infrequently priced or not priced at all.

The suggestion that similar investments or shorter term data can be used instead of the full 5 year data may lead to inconsistencies between providers, who may choose different investments to benchmark against. Alternatively the short term data may skew the accumulation growth banding. This appears to fly directly in the face of the overarching aim of achieving consistency between providers.

A further issue is that fund distributions do not appear to have been taken into account. For example, many funds have both income and accumulation units available. If an investment was made into income units, and the income reinvested, one would theoretically end up with the same returns as with accumulation funds, however this point is ignored by focusing only on pricing data. The result would be that accumulation funds would be projected with higher growth than income funds.

4. 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?

The price inflation assumption should be aligned to the rate prescribed by COBS 13 Annex 2 (currently 2.00%), or vice versa, COBS 13 should reflect the assumption in AS TM1. It is confusing as to why SMPIs are required to use a differing rate of inflation, which may be difficult for customers to understand. If the overarching aim is consistency for the pension member, then this assumption seems to fly directly in the face of that.

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

n/a

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

This is likely to lead to further inconsistencies. The corridor allows different providers to make different choices as to whether to reclassify assets into different accumulation bands, which could lead to customer confusion.

It also adds inconsistency between providers who have held the assets for different lengths of time. Consider the example of two providers with the same asset, which is within the corridor for downward reclassification. Provider 1 has held the asset for years, and does not reclassify down due to the corridor. Provider 2 is purchasing the asset for the first time, and looks only at the current measure of volatility. Using the accumulation rate table in the proposal, it must classify the asset at the lower level. This means that a customer currently with provider 1 but shopping around for a better deal, will

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be incorrectly told that provider 1 will provide better returns for their pension than provider 2, which is incorrect and very clearly a poor customer outcome.

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

Whilst there are no specific concerns with the approach to pricing for with-profits funds, it needs to be borne in mind that in our experience most with-profits providers are less likely to provide automated data feeds to third party pension providers, which further emphasises the difficulties that providers will have in obtaining up-to-date prices in order to ascertain the accumulation rate.

8. Do you have experience of unquoted assets held in pension portfolios and what are your 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?

As an open-architecture SIPP provider we have significant experience of unquoted assets, in different forms.

Being able to invest in commercial property is a major advantage of SIPPs which offer full functionality. Of course commercial property is not regularly priced, and would therefore fall into the bracket of 'unquoted assets'. Being required to project zero real growth would be unacceptable – it paints a completely misleading picture of the investment opportunity. This can best be illustrated by looking at the price changes in the commercial property market, for example, there are commercially available indices for the UK commercial property market and the sectors within it. Whilst this market is currently affected by the peaks and troughs caused by the changes in behaviours brought about by the pandemic, generally it can be seen that it is not appropriate to use a value of zero growth in real terms.

This approach also presents issues for assets that are priced less frequently than monthly, for example quarterly-priced assets. The model would need to fit these assets too, as it is misleading to treat these assets as attracting zero growth merely on the grounds of price frequency.

Zero real growth may well be appropriate for other unquoted assets, such as unlisted company shares. However there are further questions raised by the existence of further unquoted assets such as fixed term bank accounts. Based on how price volatility is defined, fixed term bank accounts may need to be shown as zero real growth, which may be correct at this moment in time where cash returns are lower than 2.5%, but we would not necessarily expect this to always be the case.

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

n/a

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10. What are your views on the proposed prescribed form of annuitisation and treatment of lump sum at retirement?

This is concerning because in our experience as a pension provider, the vast majority of clients choose to take their tax-free cash (TFC) lump sum. To project the retirement income without taking TFC into account risks painting too optimistic a picture for the client, as the taking of TFC would obviously reduce the level of income available to the client, which could be seen as misleading. Therefore if this approach is to be followed, then it must be made abundantly clear to the client that this is the scenario.

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?

Similar to the first part of Q10 above, the primary concern is that this may not reflect real life situations for clients. A better way might be to introduce a range of 'what if?' scenarios on the dashboard, such as wanting to inflation-proof retirement income, or wanting to provide for a spouse upon the first death, so that clients can easily paint their own retirement picture that most accurately reflects their own personal situation.

11. 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?

n/a

12. 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?

n/a

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

These proposed rules will only apply to SMPIs, and not FCA-mandated illustrations (key features illustrations). This means that key features illustrations have the potential to differ significantly from SMPIs, both in terms of growth rates (above the FCA's mandated 5% ceiling) and differing inflation rates, which could lead to significantly different projected retirement values, which could obviously lead to customer confusion and poor outcomes.

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

As mentioned above, the delivery timescale itself is challenging. In addition, the requirement to measure price volatility, every year, for each and every asset in which any of our almost 80,000 clients are invested, is potentially enormous for an open-architecture pension provider which does not operate or manufacture any of its own investment funds. We will be reliant upon third party investment providers to supply us with the required information, the provision of which is neither legislated nor regulated, meaning that the supply of this information is not guaranteed.