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The Director of Actuarial Policy

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By email to APT@frc.org.uk

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Dear Sir

Re: Proposed Revision to AS TM1: Statutory Money Purchase Illustrations Consultation Paper

XPS Pensions Group welcomes the opportunity to respond to the above consultation paper.

XPS Pensions Group is the largest pure pensions consultancy in the UK, specialising in actuarial, covenant, investment consulting and administration. The XPS Pensions Group business combines expertise, insight and technology to address the needs of more than 1,500 pension schemes and their sponsoring employers on an ongoing and project basis. We undertake pensions administration for over 948,000 members and provide advisory services to schemes of all sizes including 47 with over £1bn of assets.

We also have a specialist SIPPS and SSAS department. It is in that capacity that we make our response as the impact on individual or very small bespoke pension schemes will be very different from group off the peg schemes.

We set out in the appendix our responses to the questions posed in the consultation paper.

If you have any queries, please do not hesitate to contact me.

Yours sincerely,

Jane Masding

Actuary

Appendix – Responses to questions posed in the consultation

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?

We are supportive of prescription to improve consistency from different providers.

Before 2013 SMPIs were produced on a prescriptive basis with one accumulation rate for all assets and this ensured consistency. It also ensured production of SMPIs in an efficient, cost-effective manner which was of benefit to providers and pension scheme members of both group schemes and bespoke SIPPS alike.

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

The effective date should be such that arrangements for compliance can be put in place for a workable solution to the problem. It would appear that what is suggested is unworkable for bespoke SIPPS, due to the changes required in training, processes, data collection and to update IT systems. It also cannot be overstated how reliant pension providers will be on information from third parties.

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

Any accumulation rate used for the projections will be wrong for any individual set of investments.

A one-size fits all accumulation rate will be wrong, but will allow providers to minimise their fees and maximise their service to the benefit of pension scheme members.

An accumulation rate, calculated from the volatility of potentially hundreds of individual assets in one member's pension scheme, will also be wrong but it will greatly increase the cost of providing each projection and impact the standard of service to the detriment of pension scheme members. There will be no benefit to the pension scheme members in using such a rate.

No doubt large insurance companies, whose pension scheme members can only invest in a limited number of funds within that company, may have all the necessary data and experience of undertaking volatility projections to calculate such accumulation rates.

Providers of bespoke SIPPS will not.

A bespoke SIPPS can invest in any assets allowable by HMRC. One member can have a bank account, an NS&I bond, some unquoted shares, some individual quoted shares, a property, a structured product, a unit trust and investment portfolios (either under a DFM or on a platform) which could hold 50, say, underlying assets. The next member will have a completely different set of varied assets. The proposals talk a lot about funds but are unclear or silent on how other assets should be treated. For example, how should an investment portfolio of individual shares etc be treated?

A bespoke SIPPS will not hold the necessary data; it will need to be requested from all the underlying asset providers, based on experience of dealing with multiple investment providers over many years it could be very difficult or impossible to obtain such information, particularly in a consistent format.. The requirement for very detailed investment charges data to comply with FCA requirements for clients in drawdown has shown how that system is very time-consuming when SIPPS providers have no choice but to ask other companies (for whom it is just extra work) to provide the data.

As a company we have approximately 4,500 SIPPS around half of which require SMPIs. A quick analysis of 50 SIPPS from one month shows that we request or look up information from 28 different places to obtain values of all the assets. Some are single equities but many are investment portfolios. The average number of underlying investments per information request could easily be 20. This would, apparently, mean 0.5x4500x28x20/50=25,200 volatility calculations every year.

An average of 5 volatility calculations (that we have never done before) for every SIPPS every year.

Not only is this unworkable it is also reliant on external firms (for whom there is no regulatory requirement) providing the information in a usable format.

The volatility calculation exercise alone could well take more resources than providing the SMPIs in their present format.

There is no shame in going back to one accumulation rate (or perhaps one for cash and another for the rest) if it is a practicable solution of benefit to pension scheme members and would assist with the consistency of approach across providers.

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

The proposers will be well qualified to have suggested a technically and theoretically sound set of assumptions. The more important questions are whether they are workable in practice or of any benefit to pension scheme members, or do they suggest a degree accuracy that simply is not there in projections.

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

No comment

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

SIPPS do not have a restricted set of funds into which they can invest. The full range of funds and shares permitted by HMRC is available to them, and the members can be invested in many different holdings. Determining which volatility group each individual investment is in will be an enormous task to carry out each year and providers would be reliant on the fund managers/investment community to provide information.

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

No comment

Q8 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?

Many of our members directly hold commercial property investments, with a smaller number having other types of unquoted holdings such as unquoted shares. The return on such investments can be hugely varied.

If there are to be specific accumulation rates then a zero real rate of growth will be wrong in most cases, as would any other, but it is workable and understandable.

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

In 3.51 the proposals say that being obliged to recalculate the volatility group for each policy/ plan at each illustration would place an undue burden on providers and yet, that is exactly what would have to be done for a bespoke SIPPS; except that it would be without any of the data or experience of volatility calculations, making it even more onerous.

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?

Although this may more closely reflect what is done in practice with regard to spouses, there are concerns that not providing for a spouse could be seen as the normal course of action and this could lead to unnecessary hardship in the future.

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?

No comment.

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?

No comment.

Q13 Do you have any other comments on our proposals?

The need to change SMPIs to fit the Pensions Dashboard and achieve consistency is a wonderful opportunity. The opportunity should be taken to achieve consistency with other projections outside the scope of this consultation.

The opportunity should also be taken to make the illustrations as simple and understandable to the pension scheme members as possible, even if that means they are less technically and theoretically correct.

There is no benefit to the member in providing a more complex, more costly, time-delayed projection that is less understandable and will still be wrong.

Before implementing the proposals, we would strongly urge that you look closer at the impact of the requirements for the bespoke SIPP providers to fully understand the burden of work this imposes and the potential costs implication, the latter which will undoubtedly need to be absorbed by the SIPP members.

To be clear, we believe the proposals as stated are unworkable for open-architecture SIPPs, driven by time and complexity in obtaining and interpreting necessary data, and the costs imposed on members from doing so.