Dear Sir / Madam

Please find below our response to

About interactive investor

interactive investor (ii) has been supporting retail investors for over 25 years, providing impartial information and tools investors need to make confident and informed investment decisions. Today ii is the UK's second largest direct to consumer (D2C) investment platform with over 400,000 customers and administering over £50bn of assets (including £9bn in SIPPs) on their behalf.

In 2019, ii became a pension scheme operator (prior to this, the 'ii SIPP' scheme operator was a third party) and has grown its Self-Invested Personal Pension (SIPP) activity significantly since then. The scheme now has almost 50,000 members.

The ii SIPP is not a 'full' SIPP and is broadly similar to those offered by investment platforms such as Hargreaves Lansdown, Fidelity, and AJ Bell. Such 'lite' SIPPs offer a diverse range of 'mass market' investment options, but do not offer direct ownership of assets such as property, offshore funds, or unquoted shares.

As an 'execution only' investment platform, ii does not offer advice but provides a range of services for the engaged, self-directed retail investor. Customers can invest in a market leading range of investment products (including shares, investment trusts, funds, ETFs, and bonds) using several different account types (General Investment Account, ISA, Junior ISA, and SIPP).

To support research and investment decision-making, customers can also access a range of research resources, analytical tools, and investment ideas, such as the ii 'Super 60' and 'ACE 40' rated investments, the ii model portfolios and the ii 'Quick Start Funds'.

Customers have continuous access to view their investment portfolios via ii's website and mobile app, and can trade securely using the website, via the app or by telephone. The service proposition is underpinned by simple, fair, and competitive pricing to provide a high quality, value for money investing experience.

Key observations

Alignment of AS TM1 and COBS 13 requirements

We note FRC's comments regarding the scope of this consultation, and in particular the comment at Paragraph 1.7 advising respondents not to include comments related to either point of sale or to subsequent ad hoc projections (i.e. FCA's COBS 13 requirements).

However, we feel it is necessary to question the somewhat 'siloed' approach being taken to updating the requirements for producing illustrations.

In our view, the DWP should follow through on its commitment to "identify the most appropriate ownership of the assumptions going forward" and ensure the revisions to AS TM1 and COBS 13 is a coordinated, single policy development.

The FCA is currently consulting on the incoming 'Consumer Duty'. A key element of the Consumer Duty is the 'Retail Customer Outcome on Consumer Understanding'.

The high-level requirement is that a firm must

a) communicate in a way that is reasonably likely to be understood and that facilitates decision-making, and
b) take proportionate steps to review, and where appropriate, test communications to show the firm has taken reasonable steps to ensure they are reasonably likely to be understood and facilitate customers' decision-making

It stands to reason those equivalent standards should apply to prescriptive disclosure requirements. However, we are concerned that the inconsistency that will continue to exist will mean that firms cannot readily say they have complied with the Consumer Duty with respect to the illustrations they provide.

By taking this disjointed approach, we will, in effect, have three illustration standards: AS TM1 and two 'versions' of COBS 13 (those being personalised and generic illustrations).

Notwithstanding the issue of consistency, consideration also needs to be given to the cost of taking a disjointed approach to revising and aligning AS TM1 and COBS 13.

If FRC works on updates to AS TM1 now and FCA picks up similar updates "in due course", providers will need to initiate two separate projects for essentially the same piece of work (we have commented on the approximate cost of this approach in our response to Q13).

Prescribing Accumulation Rates using Volatility Groups

Whilst we broadly support the aim to improve the consistency of SMPIs through a more prescriptive approach to accumulation rates, we have concerns with the proposed approach. We have provided a detailed description of our concerns in our response to Q3, but in summary we are concerned that:

- A new volatility categorisation will cause confusion, given the existence of a different, standardised 'risk measure' (the Synthetic Risk and Reward Indicator (SRRI)) used by UCITS funds. Customers are inundated with disclosure documents and adding a further inconsistency between these documents seems misguided. We would like to see a joined-up disclosure regime.
- Notwithstanding the comment above, should FRC proceed with the proposed methodology, alongside placing requirements on pension schemes, there must be a concurrent requirement for investment product manufacturers (e.g. fund managers) to provide the volatility banding data in a systematic way. This could be done by way of a simple change to the FCA's existing PROD rules.

Responses to consultation questions

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?

We fully support all efforts to drive consistency and clarity in any customer disclosure. However, please see our response to Q13, in which we question the lack of a joined-up approach to revisions to, and alignment of, AS TM1 and COBS 13.

With regards to consistency, in the context of COBS 13, given the wealth of published forecasts from market participants available, we can't see a justification to preserve independent judgment by individual firms on projections that are ultimately for the customer rather than the firm's benefit.

Again, we acknowledge that the FRC is not consulting on the AS TM1 / COBS 14 inconsistency issue. However, we believe that getting both regimes aligned should be a single piece of work.

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

The implementation timeline is not unreasonable. However, please see our response to Q13. If there is an intention to revise, and align, AS TM1 and COBS 13, this should be carried-out as a single piece of work, with a single implementation date. The disjointed approach being proposed means that schemes will first have to implement a project to make changes to SMPIs and at a later date, implement a new project to make changes to their COBS 13 illustrations. Whilst the methodology behind the changes might be the same, the costs of carrying out these changes as two separate projects will be significant.

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

In very broad terms, we support the aim to improve the consistency of SMPIs through a more prescriptive approach to accumulation rates. Moreover, we broadly support the policy intent that prescribed accumulation rate assumptions should take account of additional returns that can be expected from higher-risk funds, in respect of a fundamental assumption of capital market theory that increased risk should be correlated with increased long term average return.

However, we are concerned that the following guiding principles developed by FRC are not being properly addressed:

- The resulting accumulation rate assumption can be determined consistently for different funds.

Whilst we agree with this being a guiding principle, we would question whether developing four new 'volatility groups' is the correct approach. As noted in the consultation, there is an existing, standardised 'risk measure' (the Synthetic Risk and Reward Indicator (SRRI)) used by UCITS funds. Whilst accepting the point that the SRRI is not perfect, illustrations by their very nature have inbuilt imperfections and are, after all, only meant to be illustrative.

As we noted in our response to HMT's 'Wholesesale Markets Review', the disclosure regime has become problematic and, in an understandable effort to establish minimum standards, regulators have unwittingly created a regime in which the primary aim of product manufacturers is to have met regulatory standards, rather than having provided the customer with pertinent and engaging information.

Customers are inundated with disclosure documents and adding a further inconsistency between these documents seems misguided. We would like to see a joined-up disclosure regime, where customers receive consistent communications about the nature of their investments and the level of return they might expect.

Moreover, if the goal is to help people understand the impact of volatility on the growth of their fund, we would suggest that educational supporting materials for customers on the potential impact of volatility, provided separately, may be of more use to them and less confusing than further illustrations on this document.

- The resulting accumulation rate assumption and the resulting statutory illustration should be easy to describe to savers and to be understood by them.

We are not convinced that the approach being proposed will meet this standard. On a standalone basis, it will be difficult to explain to a standard retail customer and when one adds-in the inconsistency we have noted above, this becomes more problematic.

- The determination of the resulting accumulation rate assumption should not place an undue burden on providers.

As an investment platform, we offer our customers access to 1,000s of retail funds, investment trusts, and exchange traded products. For us to be able to adapt our systems and processes to accommodate these new standards, the volatility band **must** be a standardised data item that can be systematically 'consumed'.

Alongside placing requirements on pension schemes to provide SMPIs using the new methodology, there must be a concurrent requirement for investment product manufacturers (e.g. fund managers) to provide the volatility banding data in a systematic way.

This could be done by way of a simple change to the FCA's PROD rules – for example, amending PROD 3.2.16R by adding a requirement to provide data to distributors sufficient for them to comply with the AS TM1 requirements.

Since investment product distributors are typically using the European MiFID Template (EMT) data to meet their regulatory requirements with respect to cost disclosure, target market etc. it would seem logical that the volatility group becomes a mandatory data item in the EMT. We accept that FRC/FCA cannot compel investment product manufacturers to use the EMT, but the change to PROD noted above would probably bring about this change via industry cooperation.

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?

We would echo AMPS' comment in response to this question: the accumulation rate of 7% for volatility group 4 and allowing for 2.5% inflation (e.g. a nominal rate of 9.5%) is not aligned with the maximum growth rate allowed for under FCA projections (8%). Over the long term such differential will be significant and may cause additional confusion with consumers.

Fundamentally, it seems illogical to have differing maximum thresholds.

In terms of the rates themselves, as we set out in a report 'Is 12% the new 8%?'[1], there are reasons to believe that historic market performance may not be repeated and the consequence of potential 'lower for longer' global equity market growth could be profound for pension holders. They might, for instance, have to contribute more to their pension throughout working life or opt for a higher risk fund than they would do otherwise. In presenting only a status quo view based on past performance, we would suggest there could be a risk that the outcome for consumers of this potentially false hope could be lower pot values on retirement. Given the outcomes-based focus of the FCA's Consumer Duty, we think the presentation of these assumptions requires some context so that pension holders can decide for themselves whether they need to act. Pension holders may themselves begin to question whether the assumptions being used are a useful guide if the figures quoted and the resulting pot size projections change significantly from year to year. Using an assumed long-run CPI rate of 2.5% might also require explanation to consumers, in times of higher inflation such as we are now experiencing.

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

The proposed approach seems reasonable. However the addition of scenarios for: 'De-risked' and 'Not de-risked' would be helpful for people planning for retirement. For instance, the two projections could mean the difference between someone continuing to work for a further five years, or not.

Moreover, we echo AMPS' comment in relation to this question: we would appreciate clarification as to whether you are only proposing this change where the lifestyling is programmatic (presumably in both the lifestyling arrangement itself and in any SMPI functionality).

6. 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?

The proposed approach seems reasonable. However, we would refer you to our response to Q3. For us to be able to adapt our systems and processes to accommodate these new standards, the volatility band **must** be a standardised data item, provided by investment product manufacturers, that can be systematically 'consumed'.

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

As we do not offer these products, we do not have a view on this issue.

8. 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?

Broadly speaking, the unquoted assets we hold in our SIPPs are securities that were previously listed, but the company has subsequently gone into liquidation. Accordingly, for these assets, we would support the 'zero growth' approach.

[1] https://media-prod.ii.co.uk/s3fs-public/pdfs/Is-12percent-the-new-8percent-report.pdf

That said, we would echo AMPS' comments on this matter: assets may be unquoted for several reasons, such as being genuinely unquoted in that they are private companies. Growth of these assets will be specific to the underlying holding but to suggest no growth within a SMPI does not seem appropriate. In effect you would be saying that allowing for inflation these assets are loss making in real terms which would not necessarily be the case. We would instead suggest that a better measure of growth in these circumstances would be a real return equivalent to the prevailing inflation assumption.

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

The proposed approach seems reasonable.

10. 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?

We would echo AMPS' comments here: the concept of annuitisation is outdated now and has been for some time. SIPP customers do not necessarily view their retirement date as a 'line in the sand' where their portfolio will be sold down and 'cashed-in' for an annuity. There is a growing expectation that their fund will continue to benefit from investment growth throughout the decumulation phase.

That said, we also acknowledge the comments FRC has made regarding the complexities associated with incorporating the more flexible arrangements that customers have available, post-Pensions Freedoms. Accordingly, on balance, we agree that a simplified approach is sensible. However, we would like to see the Tax-Free Lump Sum (TFLS) incorporated. In our view, there should be two illustrations, one showing annuity-only and one incorporating the TFLS.

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?

We do not have a view on this question.

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?

The proposed approach seems reasonable.

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

Inconsistency with COBS 13 requirements:

Whilst we acknowledge FRC's comments regarding the scope of this consultation, and in particular the comment at Paragraph 1.7 advising respondents not to include comments related to either point of sale or to subsequent ad hoc projections (i.e. FCA's COBS 13 requirements), we feel it is necessary to question the somewhat 'siloed' approach being taken to updating the requirements for producing illustrations.

In Paragraph 2.4, FRC comments:

"While leaving AS TM1 unchanged would minimise the work required of providers, the resultant ERI projections would not provide the individual saver with consistency in projections from different providers. This would raise concerns about the validity of aggregating resulting ERIs and continue to present significant communication challenges in explaining why the projections are not consistent."

Moreover, in October 2020, the Department for Work & Pensions (DWP) acknowledged (in consultation outcome: 'Simpler annual benefit statements') the need to align the FRC assumptions with FCA's COBS 13 requirements.

Finally, in CP22/3, FCA noted that in due course it will "consider" COBS 13, including whether and how FCA can "adhere to similar principles as the revised AS TM1".

There is clearly a recognition of the need for consistency of the standards that apply to illustrations, and yet the revisions to AS TM1 and COBS 13 are being treated as two separate issues.

In our view, the DWP should follow through on its commitment to "identify the most appropriate ownership of the assumptions going forward" and ensure the revisions to AS TM1 and COBS 13 is a coordinated, single policy development.

Notwithstanding the issue of consistency, consideration also needs to be given to the cost of taking a disjointed approach to revising and aligning AS TM1 and COBS 13.

If FRC works on updates to AS TM1 now and FCA picks up similar updates "in due course", providers will need to initiate two separate projects for essentially the same piece of work. Whilst it is difficult to put a cost figure on this, it is not unreasonable to assume that each project will cost £50,000-£100,000 to implement. Moreover, there is an intangible 'opportunity' cost with running two projects back-to-back, when the same work could be carried out as one piece of work.

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

Please see our response to Q13. Whilst we acknowledge FRC's comment that "providers have been strongly advised to take account of the possibility of changes when devising systems to produce statutory illustrations for SMPIs", and we accept that, over time, revisions to illustration standards are an inevitable cost of being a pension provider, the disjointed approach to revising and aligning AS TM1 and COBS 13 will lead to significant, and largely avoidable, costs.