KPMG LLP
Pensions
8 Salisbury Square
London EC4Y 8BB
United Kingdom

Tel +44 (0) 20 7694 1736
Fax +44 (0) 20 7311 4936
DX 38050 Blackfriars
james.riley@kpmg.co.uk

The Director of Actuarial Policy
The Financial Reporting Council
5th Floor, Aldwych House
71-91 Aldwych
London
WC2B 4HN

Our ref FRCAug2012

By e-mail: TM1@frc.org.uk

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Dear Sir

Consultation paper: Product projections and transfer value analysis

I am responding to the above consultation on behalf of the Pensions Practice in KPMG.

We would respond to the questions posed in chapter 5 of your consultation paper as follows. We have also included as an appendix our response to the questions in chapter 2 to 4 which we have provided to the FSA.

Q1: Do you agree that the assumptions in AS TM1 should be consistent as far as possible with those specified in COBS 13 Annex 2 of the FSA Handbook?

Yes, from a consumer perspective consistency between projections is appropriate. However, it is important that the projection assumptions are appropriate as well as consistent and we have provided comments to the FSA in relation to its proposed projection rate assumptions (see the appendix to this letter).

Q2: a) Should AS TM1 continue to specify a maximum accumulation rate?

Yes.

b) If AS TM1 continues to specify a maximum accumulation rate, should it be the same as the FSA's intermediate projection rate?

Yes, provided the FSA's intermediate projection rate is appropriate for the purposes of money purchase illustrations. That is, it is based on an appropriate underlying asset mix.

Yours faithfully

James Riley
Director

Appendix

Q1: Do you agree with the new revised mortality basis? If not, please explain what alternative basis you think is more appropriate.

Yes, from a consumer perspective consistency as far as possible between TVA and KFIs is appropriate.

Q4: Do you agree with the assumption for CPI-linked revaluation in deferment? If not, please state the level at which you believe the assumption should be set and why you believe it is more suitable.

Yes.

Q5: Do you agree with the approach and level of the assumptions for pension increases based on CPI? If not, please explain what alternative basis you think is more appropriate.

Yes.

Q8: Do you agree that the proposed changes to these assumptions are appropriate? If not, what changes would you propose? Please explain why you would make other proposals.

No. Ideally, the projection rate used would reflect the asset mix of the specific product to which each projection relates. However, we accept that the practical difficulties of such an approach mean that there must be a compromise.

In light of this, where a single intermediate rate is to be referenced for all products we think that the approach used to determine this rate must be transparent to allow users (e.g. consumers and advisors) to understand the projections. For example, a rate which is set with reference to a specific investment strategy would allow users to determine the appropriateness of projections given the asset mix underlying the product to which they relate.

The need for transparency is particularly important as there are significant differences in the asset mix across the range of products for which projections are made. For example, PwC comment in their report that “the major retail pension funds offered by the larger life insurance companies typically having between 70% and 90% invested in equities” whereas “Insurance products such as with-profits funds now commonly invest anywhere between 50% and 100% in bonds”.

The best estimate rate of 6% set out by PwC is based on a specific asset mix whereas the proposed rate of 5% is not explicitly, and so is not consistent with such a transparent approach.

In addition, whilst we acknowledge that the current intermediate projection rate of 7% is too high, adopting a rate which is outside of the ranges around the best estimate set out by PwC appears contrary to the FSA’s desire to avoid spurious accuracy. We also note that, whilst PwC concluded that there is risk of short term downside to the forecasts set out, we think that there must be a balance between an allowance for this and the long term nature of some of the products for which the rates are used e.g. KFIs for pension products.