

The Director
Board for Actuarial Standards
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Sent by Email

3 June 2010

Dear Sir

**TM1: Statutory Illustrations of Money Purchase Benefits
Consultation Response**

This letter sets out Thomson Dickson Consulting's response to the consultation on possible changes to the rules on how calculations should be carried out for pension projections in statutory annual statements.

Thomson Dickson Consulting provides a full range of actuarial advice, pension consultancy and pensions administration services. Our clients are primarily small and medium sized occupational pension schemes and employers, most of them operating within Scotland.

Our comments are as follows, with reference to the questions listed in section 11.1 of the consultation paper:

1. We believe that TM1 should be revised to apply a "principles based" approach which provides a framework for providers to follow to produce SMPs. Less prescription is desired and more flexibility should be available to encourage providers to produce illustrations that are more bespoke for the user of the illustration.
2. The significant uncertainty of the pre-retirement investment return can be addressed by using two rates of return to illustrate the different possible outcomes. See section 16. below.
6. We agree with the proposal to have reduced detail in TM1. The parameters of the projection should be defined in principle, but flexibility to incorporate particular features if so desired should be allowed. For example, the projection needs to have a clearly defined start and end date but the pattern of contributions assumed can take various forms (level, escalating at fixed rate, non-contributory for a period followed by increasing payments, etc).
7. We believe that there should be flexibility to illustrate a level or escalating pension in retirement, in order to better reflect the possible intentions of a member or membership if known to the provider of the projection. Obviously, there is a requirement for a note that clarifies the type of pension used in the illustration.
9. As in 7. above, we believe there should be flexibility to illustrate what is likely to be appropriate for a particular member or membership. Accordingly, TM1 should not require a provider to either include or exclude retirement cash sums, but offer the flexibility to choose to illustrate this option. Again, the supporting notes should clarify which method is used.

11. We agree with the suggestion in section 6.16 to allow providers to choose mortality assumptions that are appropriate for a particular member or membership. This approach is consistent with less detail being prescribed in TM1 and a “principles based” framework being established for the assumptions used for SMPIs.

12. Use of market annuity rates arguably implies spurious accuracy, particularly for projections of pension benefits over a long period for the accumulation phase. With a “principles based” framework, the provider will have freedom to use an annuity rate that they deem to be realistic and appropriate for the user of the statement.

15. The 4% allowance is excessive and an across the board allowance of say 2% of fund at retirement is more appropriate. Given the variation stemming from the unknown investment return, there is an argument for the removal of any expense allowance.

16. With regard to the accumulation rate, in order to simply illustrate the possible variation of outcomes, the projection should be performed at two rates of investment return. For terms of 10 years and above, 5.0% and 7.5% per annum should be used. For terms less than 5 years, 2.5% and 5.0% per annum should be used. For durations between 5 and 10 years, a blended approach, with 0.5% steps, should be utilised. No adjustment should be made to these rates of return to account for investment management costs during the accumulation phase.

18. Price inflation and earnings inflation should both remain at 2.5% per annum, irrespective of period of projection.

20. No.

21. A single approach for the accumulation rate, albeit two illustrations at a high and low rate, as described in 16. above, should be used irrespective of the type of investment fund.

22. Yes, one consistent calculation framework should apply for both point of sale and SMPI projections, with personalisation allowed.

23. Until one consistent basis is implemented, a simple warning should be clearly displayed, along the lines of “The method and assumptions used in this illustration of pension benefits could be different from those used in an earlier illustration you have received. Accordingly, the figures in this illustration may not be directly comparable with corresponding figures in earlier illustrations.”

24. We agree with the use of signposting.

25. We believe that the proposed timetable for changes to TM1, if broadly consistent with our views, is appropriate.

26. There should not be a requirement to include an illustration of pension attributable to contributions already made. The projection of the current fund at the start date (which may be zero) should clearly state the assumption used for the pattern of contributions to be paid in the future (if any).

27. Variation of outcome should be addressed as described in section 16. above.²⁸

28. A “principles based” framework provides freedom for different providers to develop their own format for SMPs. A suite of best practice SMPs would be useful to provide assistance to providers.

I trust that these comments are useful.

Yours faithfully

A handwritten signature in black ink, appearing to read 'A. Thomson'.

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