Feedback Statement

Financial Reporting Council

February 2014

AS TM1: Statutory Money Purchase Illustrations

Analysis of responses to the November 2013 exposure draft

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries; and oversee the regulatory activities of the accountancy and actuarial professional bodies.

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Analysis of responses to the November 2013 consultation

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Consultation and respondents

1.1 Members of certain money purchase pension arrangements must be given annual Statutory Money Purchase Illustrations (SMPIs). The Financial Reporting Council (FRC) sets the actuarial methods and assumptions to be used in SMPIs through its Actuarial Standard Technical Memorandum 1: Statutory Money Purchase Illustrations (AS TM1).

1.2 On 15 November 2013, the FRC published an exposure draft[1] of version 4.0 of AS TM1. The consultation on the exposure draft closed on 13 December 2013.

1.3 We received 20 responses to the consultation, one of which was confidential. A list of respondents is included in the appendix.

Changes to the Disclosure Regulations

1.4 The FRC's exposure draft of AS TM1 followed the publication of the *Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013*[2] *("the revised regulations")* by the DWP on 31 October 2013.

1.5 *The revised regulations* come into effect on 6 April 2014 and do not alter the requirement to provide an SMPI but they change some aspects of the illustration. In particular, the revised regulations permit the personalisation of SMPIs to reflect the form of pension the member will choose at retirement. The revised regulations remove the requirement for the statutory illustrations to show an annually increasing pension with a 50% dependant's pension payable on the member's death.

1.6 In its consultation paper on the revised Disclosure Regulations[3] the DWP clarified that a cash lump sum may also be included in the SMPI.

1.7 *The revised regulations* continue to require that statutory illustrations are produced in accordance with the assumptions and methodology set out in AS TM1.

Exposure draft proposals

1.8 In the exposure draft we consulted on the following amendments to AS TM1 reflecting the changes made in *the revised regulations*:

- a change to the calculation methodology to allow for a cash lump sum;
- a change in the wording on dependant's pension to allow varying percentages of dependant's pension; and
- an annuity rate assumption for a pension that does not increase annually.

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[1] https://www.frc.org.uk/Our-Work/Publications/Actuarial-Policy-Team/Exposure-Draft-AS-TM1-Statutory-Money-Purchase-Ill-File.pdf

[2] SI 2013/2734

[3] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/221411/occupational-personal-pension-schemes-disclosure-information-regulations-2013.pdf

1.9 We proposed that version 4.0 of AS TM1 be implemented for statutory illustrations issued on, or after, 6 April 2014.

Summary of changes effected in version 4.0 of AS TM1

1.10 Section 2 of this paper analyses the responses to the consultation on the exposure draft.

1.11 Respondents were generally supportive of the proposals outlined in the exposure draft. There were two main areas of concern to those who responded to the consultation:

- Several respondents did not like the proposal to use fixed interest gilt yields as the basis for the interest rate used for annuity rates when providers illustrate a non-increasing pension. Respondents did not dispute the rationale for our proposed approach but the insurer respondents in particular were keen for the FRC to adopt an approach to this assumption that was consistent with the FCA's rules.

- Many respondents considered that AS TM1 should make it clear that any allowance for lump sum is disclosed with the SMPI.

1.12 In finalising the text of version 4.0 of TM1 we have taken account of the comments we received in response to the exposure draft, as well as other comments that have been made to us.

1.13 The text of version 4.0 of TM1 is substantially the same as the exposure draft and amends AS TM1 to allow:

- for cash to be taken out prior to the calculation of the illustrated pension;

- varying percentages of dependants' pension to be assumed; and

- different pension increases to be assumed with the specification of the interest rate used in determining the annuity rate for:

  1. non-increasing pensions to be based on fixed interest gilt yields;
  2. index-linked pensions to be based on index-linked gilt yields; and
  3. pensions increasing at other rates to be based on a yield consistent with (1) or (2).

1.14 However, in response to consultation responses we have:

- made it clear that where a provider makes an allowance for a lump sum, the lump sum should be shown in today's (inflation adjusted) terms on alongside the illustrated pension on the SMPI; and

- amended the text to allow providers to use the yield specified for the annuity rate for increasing pensions plus 3.5% as the interest rate for determining the annuity rate for a non-increasing pension.

1.15 Additionally we have amended the text in places to improve clarity.

1.16 Section 3 explains the changes effected in version 4.0 of AS TM1 (when compared to version 3.0). Part II contains the final version of version 4.0 of TM1, marked up to show changes from version 3.0.

Effective date of changes

1.17 Version 4.0 of AS TM1 will be effective for statutory illustrations issued on or after 6 April 2014.

Future reviews of AS TM1

1.18 The FRC regularly reviews AS TM1. Reviews take account of various matters including changes to market conditions and changes to legislation.

1.19 As indicated in the consultation paper, we intend to review all aspects of AS TM1 in 2014.

2 Responses to the exposure draft

Introduction

2.1 In this section, we summarise the comments we received and our reactions to them.

Lump sum at retirement

1	Do respondents agree with the proposed approach to the allowance for cash in the calculation of the statutory illustration (paragraph 3.3)?

2.2 The majority of respondents supported the proposed approach to the allowance for cash in the calculation of the statutory illustration.

2.3 Many respondents noted that nearly all individuals elect to take a cash lump sum entitlement at retirement. Therefore, allowing the illustration to take account of cash will mean that the SMPI will more closely reflect the expected benefit outcomes for the majority of recipients.

2.4 Making an allowance for the cash lump sum is optional for providers. Some respondents suggested that the wording in the exposure draft may imply that the allowance for the cash lump sum is mandatory. We have amended the wording to clarify that the allowance is optional.

2	What are respondents' views on the proposed approach to the cash assumption (paragraphs 3.6 to 3.8)?

2.5 The majority of respondents supported the proposed approach to the cash assumption.

2.6 The text in the exposure draft stated that the lump sum assumed to be paid at retirement should not normally exceed the amount permitted by the scheme rules or legislation. Respondents suggested that we clarify that our intention in referring to legislation was to limit the amount of lump sum assumed to the maximum tax-free amount. It was noted that legislation does not prevent the payment of lump sums as unauthorised (taxable) benefits under the Finance Act 2004.

2.7 It was our intention that the lump sum should not usually exceed the maximum tax-free lump sum and we have amended the text in AS TM1 accordingly.

2.8 The exposure draft also stated that where the provider has assumed a lump sum greater than 25% of the nominal accumulated fund or greater than permitted by the scheme rules or legislation, the provider should document the rationale for doing so.

2.9 There was a suggestion that the rationale should be provided with the SMPI or by signposting to the information. We have not included this suggested provision in AS TM1 but providers may wish to consider how best they can explain the assumptions made in the calculations of the statutory illustration and the lump sum to members.

2.10 Concerns were expressed in answer to question 1 and question 2 about the lack of clear guidance on the disclosure of any allowance for a lump sum alongside the illustrated pension on statements. Several respondents suggested that AS TM1 should make it clear that where a provider makes an allowance for a lump sum, that lump sum should be shown on alongside the illustrated pension on the SMPI.

2.11 There was also comment that AS TM1 should clarify whether the lump sum should be illustrated in real or nominal terms. In line with *the revised regulations*, the lump sum illustrated should be shown in real terms.

2.12 We have added text to clarify both these points.

Spouse's or civil partner's pension

3	Do respondents agree with the proposed approach to the spouse's or civil partner's pension (paragraphs 3.10 to 3.12)?

2.13 The majority of respondents supported the proposed approach to the spouse's or civil partner's pension. However, there was a suggestion that the flexibility in the provision be more clearly articulated. We have amended the wording in AS TM1 accordingly.

Interest rates to be used in calculating annuity rates

Annuity rates for non-increasing pensions

4	Do respondents agree with the proposed approach for the interest rate used for annuity rates when providers illustrate a non-increasing pension (paragraph 3.19 to 3.23)?

2.14 In the consultation paper that accompanied the exposure draft we noted that we had considered two approaches for setting the interest rate for determining the annuity rate for a non-increasing pension:

- the yield specified for increasing pensions plus 3.5%; or
- the yield on the FTSE Actuaries' Government 15 year Fixed Interest Index.

2.15 The former is based on index-linked gilt yields and is the interest rate specified by the FCA in its rules for projections where a non-increasing pension in payment is assumed. The latter is based on fixed interest gilt yields.

2.16 In the consultation, we noted that feedback from providers and others indicates that an interest rate based on fixed interest gilts is a better proxy than index-linked gilts for the pricing bases used by insurers for non-increasing annuities. Therefore, in the exposure draft, we proposed the use of an unadjusted fixed interest gilt yield for determining the annuity rate for a non-increasing pension

2.17 The majority of respondents agreed with the rationale behind our proposal to use fixed interest gilt yields. However, many respondents, particularly insurers who have to provide both illustrations in line with AS TM1 and also illustrations under the FCA's rules, expressed a preference for an approach that is consistent with the FCA's approach.

2.18 It was noted that in current market conditions the difference between the two approaches is relatively small but nonetheless the difference in the approaches may require additional explanation for members receiving FCA projections and annual SMPIs. It was noted that differences in approaches by the FRC and the FCA could lead to increased costs and delivery issues for providers who have to provide statements under both regimes.

2.19 We have considered respondents' views and decided that providers may use the FCA basis for the interest rate in a non-increasing pension – ie the index-linked yield specified for the annuity rate for increasing pensions plus 3.5% pa.

2.20 We have clarified the text on the fixed interest gilt yield that should be used.

2.21 The exposure draft consultation was confined to changes required as a result of the revised regulations; we did not review the interest rate used in the annuity rate calculation used for pensions increasing with inflation. However, we intend to review the actuarial assumptions in AS TM1 in 2014. We will consider both the interest rate used for pensions increasing with inflation and the interest rate used for non-increasing pensions and consistency with the FCA's rules as part of that review.

2.22 In the 2014 review, we will also consider other suggestions made by respondents in response to this question, for example:

- that providers might be allowed to use alternative evidence-based assumptions for members close to retirement; and
- that it should be permissible for providers to illustrate using guaranteed annuity rates[4] if they apply to the form of annuity shown and provided an appropriate explanation is included.

Annuity rates for pensions increasing at other rates

5	Do respondents agree with the proposed approach for the interest rate used for annuity rates when providers illustrate a pension that increases at other rates (paragraph 3.25)?

2.23 In the exposure draft we did not set a basis for determining the interest rate for annuity rates when providers illustrate a pension that increases at other rates as there are many different levels of pension increase which might be illustrated.

2.24 Many respondents agreed with our proposed approach for when providers illustrate a pension that increases at other rates - that the interest rate used should be consistent with the interest rates for non-increasing and increasing pensions set out in AS TM1.

2.25 However, some respondents suggested that achieving consistency with both the interest rates for non-increasing and increasing pensions would be difficult. Recognising this, we have amended the wording in AS TM1 so that the interest rate for annuity rates when providers illustrate a pension that increases at other rates should be consistent with the interest rates for non-increasing or increasing pensions.

Inflation-adjusted projections and rates

6	Should AS TM1 suggest that providers should disclose the accumulation rate used net of inflation (paragraphs 3.28 to 3.29 and 3.36)?

2.26 There were mixed views on whether AS TM1 should suggest providers disclose the accumulation rate net of inflation.

2.27 We have not included such a provision in AS TM1 but would encourage individual providers to consider whether the disclosure of the accumulation rate used net of inflation would aid members' understanding.

[4] AS TM1 states "No account should be taken of a guarantee of annuity terms which produces a higher amount of initial pension as at the **retirement date**, or a higher amount of pension in a subsequent year, than would be produced using the assumptions in AS TM1".

Rates of inflation

Price inflation

7	Do respondents agree with our proposal not to amend the price inflation assumption (paragraph 3.32)?

2.28 The majority of respondents supported the proposal not to amend the price assumption in AS TM1.

2.29 Some respondents called for greater clarity in AS TM1 on what measure of inflation is assumed in AS TM1. Several respondents suggested that the inflation assumption be considered as part of the 2014 review of AS TM1.

Earnings inflation

8	Do respondents agree with our proposal not to amend the earnings inflation assumption (paragraphs 3.33 to 3.34)?

2.30 The majority of respondents supported the proposal not to amend the earnings assumption in AS TM1.

2.31 Two respondents did not agree. One respondent noted that from 6 April 2014 FCA illustrations will also be expressed in real terms and the calculations for FCA illustrations will have to support an earnings inflation rate that is different from price inflation.

2.32 The inconsistency with FCA rules was noted by some and we will consider this issue (in particular in relation to the inflation of charges at C.2.9 of AS TM1) as part of our review in 2014.

2014 review of AS TM1

9	What other aspects of AS TM1 do respondents suggest should be considered in our review of AS TM1 next year?

2.33 The most common theme amongst the responses to this question was the desire for the FRC to consider ways in which there could be greater consistency with the FCA's rules.

2.34 Respondents suggested the following particular aspects of AS TM1 for consideration in our review of AS TM1 later this year:

- rates of inflation;
- mortality;
- expenses; and
- risk and uncertainty.

2.35 One respondent noted that 2014 was a significant year with automatic enrolment and that any changes should have a flexible and realistic timescale; another suggested that members' interests (in terms of consistency) and providers' interests (in terms of costs) might be best served by a period of minimal changes.

2.36 We will consider these aspects and the detailed comments made by respondents as part of our review in 2014.

Timing of changes to AS TM1

10	Do respondents agree that the changes to AS TM1 should be effective for statutory illustrations issued on or after 6 April 2014?

2.37 Almost all respondents agreed that the changes to AS TM1 should be effective for statutory illustrations issued on or after 6 April 2014. It was felt important that the effective date of version 4.0 ties in with the effective date of *the revised regulations* and the FCA changes which are also effective from the same date.

2.38 One respondent questioned whether there are any transitional arrangements.

2.39 We have discussed this issue with the DWP. It confirmed that there are no transitional provisions in the revised Disclosure regulations; a scheme must comply with the law as it exists on a given day. If an SMPI is issued before 6 April 2014, then it must comply with the legislation on the date of issue; if an SMPI is issued on or after 6 April 2014, then it must comply with the revised regulations.

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3 Changes to AS TM1 (version 3.0 to version 4.0)

Introduction

3.1 In this section, we describe the changes we have made to AS TM1 from version 3.0. These changes are illustrated in the tracked changes version shown in Part II.

Effective date

3.2 In the rubric, the text states that version 4.0 is effective for statutory illustrations issued on or after 6 April 2014.

Glossary

3.3 The definition of **legislation** has been updated to reflect the introduction of *the revised regulations* with effect from 6 April 2014. *The revised regulations* revoke some of the legislation previously listed under the definition of legislation.

3.4 A new defined term **lump sum** has been added.

3.5 A new defined term **net nominal accumulated fund** has been added.

3.6 We have amended definition of **real accumulated fund** to **net real accumulated fund** and the definition has been amended to refer to the **net nominal accumulated fund.**

3.7 The definition of **statutory illustration** has been amended to reflect that an allowance for a lump sum can be made.

Section B

3.8 Paragraph B.2.1 has been amended to refer to the net real accumulated fund.

3.9 Paragraph B.3.1 explains how the net real accumulated fund is calculated.

3.10 Paragraph B.3.4 explains how the net nominal accumulated fund is calculated.

3.11 Paragraph B.3.5 clarifies that if the net nominal accumulated fund is less than zero, zero must be used.

3.12 Paragraph B.8.1 has been added to clarify that where a provider assumes a lump sum is paid at retirement then the statutory illustration statement should include a statement of the assumed lump sum in today's (inflation adjusted) terms.

Section C

Lump sum at retirement

3.13 Paragraph C.2.1 has been amended to refer to the new defined term net real accumulated fund.

3.14 Paragraph C.3.1 has been added to state that the lump sum assumed to be paid at retirement should not normally exceed the amount permitted by the scheme rules or legislation.

3.15 Paragraph C.3.1 includes text to state that where the provider has assumed a lump sum greater than 25% of the nominal accumulated fund or greater than the tax-free lump sum permitted by the scheme rules or legislation, the provider should document the rationale for doing so.

Interest rates to be used in calculating annuity rates

3.16 Paragraph C.3.3 has been amended to reflect that providers may choose to assume that the pension illustrated increases in payment or does not increase in payment.

3.17 Paragraph C.3.4 has been added to describe how the interest rate to be used in the calculation of the annuity rate should be calculated where a provider assumes that the pension illustrated does not increase in payment.

3.18 We have also included text in paragraph C.3.7 which is applicable where providers choose to illustrate a pension that increases at a rate other than inflation. In these circumstances, the interest rate used for determining the annuity rate should be consistent with the interest rates for non-increasing or increasing pensions set out in AS TM1.

Spouse's or civil partner's pension

3.19 Paragraph C.3.13 has been amended to state that the assumed amount of any spouse's or civil partner's pension should not usually exceed the amount permitted under the scheme rules or legislation.

Payment frequency and format

3.20 Paragraph C.3.17 has been amended to cover all forms of pension increases.

A List of respondents to the November 2013 consultation

Professional and trade bodies

Association of Consulting Actuaries

The Institute and Faculty of Actuaries

The Pensions Management Institute

The Society of Pension Consultants

Insurers, consultants and actuaries

Aegon

Aviva

AXA Wealth

BC&E

Chambers Townsend Consultancy Ltd

Capita

Legal & General

Hymans Robertson

Mercer

Scottish Life & Royal London Group

Scottish Widows

Towers Watson

Zurich Financial Services Limited

Others

AMND

Steven Wishart

Part II

Tracked changes from version 3.0 of AS TM1: Statutory Money Purchase Illustrations

~~TECHNICAL MEMORANDUM~~ AS TM1:
STATUTORY MONEY PURCHASE ILLUSTRATIONS

VERSION 4.0 ~~3.0~~

AS TM1: STATUTORY ILLUSTRATIONS OF MONEY PURCHASE BENEFITS

Status

Legislation provides that **statutory illustrations** must be produced in accordance with relevant guidance prepared by a prescribed body. The Financial Reporting Council (FRC) has been appointed as the prescribed body for that purpose. *AS~~Technical Memorandum~~ TM1: Statutory Money Purchase Illustrations* is that relevant guidance.

AS TM1 does not replace or amend the **legislation**. If it appears that any matter in AS TM1 conflicts with any provision of the **legislation** then the latter will prevail.

The FRC does not accept any liability to any party for any loss, damage or costs howsoever arising, whether directly or indirectly, whether in contract, tort or otherwise from any action or decision taken (or not taken) as a result of any person relying on or otherwise using this document or arising from any omission from it.

Purpose

The purpose of AS TM1 is to specify the assumptions and methods to be used in the calculation of **statutory illustrations** of money purchase pensions.

Application

AS TM1 applies to the production of any **statutory illustration**.

Effective date

AS TM1 version 4~~3~~.0 is effective for **statutory illustrations** ~~with an **illustration date**~~issued on or after ~~6 April 2013. Providers may comply instead with TM1 version 2.0 for **statutory illustrations** issued before~~ 6 April 2014.

Future changes to AS TM1

The FRC reviews AS TM1 regularly. It is possible that the methods and assumptions used will be amended as a result. It is likely that some of the assumptions in Part C will be changed from time to time, and **providers** are strongly advised to take account of the possibility of such changes when devising systems to produce **statutory illustrations**.

CONTENTS

A INTERPRETATION

A.1 INTERPRETATION OF THE TEXT

A.1.1 This technical memorandum (AS TM1) should be interpreted in the light of the purpose set out in the rubric on page 1.

A.1.2 **Providers** may adopt a different approach from that specified in AS TM1 if it does not materially affect the result of the calculation of the **statutory illustration**. For example, this may apply to the order in which the calculations are carried out.

A.1.3 Any assumptions that are used which are not specified in AS TM1 should be appropriate to the purpose of AS TM1 set out in the rubric on page 1. Such assumptions might include the valuation of property assets or the treatment of contributions if payment records are incomplete.

A.1.4 If a **member**'s **current fund** is invested in a with-profits fund (including with-profits deferred annuity contracts) the **statutory illustration** should be provided in a manner consistent with AS TM1 and with the insurer's bonus policy.

A.2 GLOSSARY

A.2.1 Terms appearing in **bold** in the text are used with these meanings:

accumulation rate	The annual rate of return assumed to be earned up to **retirement date** from the **current fund** and **future contributions**.
annuity rate	The value of an annual pension of £1 at **retirement date** calculated using the assumptions specified in AS TM1.
current fund	The relevant assets of the **scheme** in relation to the **member**'s money purchase benefits at the **illustration date.**
future contributions	All money purchase contributions due after the **illustration date** which the **provider** determines to be part of a regular pre-determined series of contributions expected to continue until the **member**'s **retirement date**.
illustration date	The date specified by the **provider** as the date by reference to which amounts are calculated for the purpose of the **statutory illustration**. The **illustration date** will normally be the **specified date.**
inflation factor	The accumulated assumed inflation from the **illustration date** to the **retirement date**.
inflation rate	The assumed annual rate of inflation.

legislation

Legislation governing the provision of statutory illustrations including but not limited to:

a) *the Pension Schemes Act 1993 (c.48) Section 113;*

~~b) *the Personal Pension Schemes (Disclosure of Information) Regulations 1987 (SI 1987/1110);*~~

~~c) *the Occupational Pension Schemes (Disclosure of Information) Regulations 1996 (SI 1996/1655);*~~

b) *the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (SI 2013/2734);*

~~d)~~c) *the Stakeholder Pension Schemes Regulations 2000 (SI 2000/1403)*; and

~~e) *the Occupational and Personal Pension Schemes (Disclosure of Information) Amendment Regulations 2002 (SI 2002/1383)*; and~~

d) *the Occupational, Personal and Stakeholder Pension Schemes (Disclosure of Information) Amendment Regulations 2010 (SI 2010/2659)*.

Northern Ireland has its own body of law relating to pensions with corresponding legislation.

lump sum

The amount of the benefit assumed by the provider to be taken as cash by the **member** at **retirement date**.

member

Any person eligible to receive a **statutory illustration** from a **scheme**.

net nominal accumulated fund

The **nominal accumulated fund** reduced by the **lump sum**, if any.

nominal accumulated fund

The **current fund** and **future contributions** accumulated to the **retirement date** adjusted where relevant for tax relief, charges and expenses.

provider

The trustees or managers of a **scheme**, or any other party preparing a **statutory illustration** on their behalf. Other parties might include advisers, insurance companies or software houses.

net real accumulated fund

The **net nominal accumulated fund** expressed in today's (inflation adjusted) terms.

retirement date	A date which the **member** has specified to the **provider** and which is acceptable to the **provider**; or where no acceptable date has been specified by the **member**, a date specified by the **provider**. A **member** may have more than one **retirement date** for different funds or contracts within a **scheme**.
risk benefits	Benefits payable on death, sickness or critical illness.
scheme	A pension arrangement that is required to provide a **statutory illustration** under the **legislation**.
scheme year	The period specified for the provision of a **statutory illustration**.
specified date	The date the fund is valued for the purpose of the **legislation**. For an occupational pension **scheme**, this is normally the last day of the **scheme**'s administrative year.
statutory illustration	The amount of pension (after allowance for any **lump sum**) calculated in accordance with AS TM1.
statutory illustration statement	The **statutory illustration** and accompanying information.

B DETERMINING THE AMOUNT OF PENSION TO BE ILLUSTRATED

B.1 INTRODUCTION

B.1.1 This Part sets out the method which must be followed for calculating **statutory illustrations**.

B.2 THE AMOUNT OF PENSION TO BE ILLUSTRATED

B.2.1 The **statutory illustration** is the annual amount of pension calculated by dividing the **net real accumulated fund** (see section B.3) by the **annuity rate** (see section B.7).

B.2.2 The **statutory illustration** must be shown in whole pounds, rounded down to 3 significant figures. If the result is under £1,000 and is not an exact multiple of £10, it may be rounded down to the next lower multiple of £10.

B.2.3 Any resulting monthly pension of less than £10 may be shown as "less than £10 each month" or "less than £120 each year".

B.3 ACCUMULATED FUND

B.3.1 The **net real accumulated fund** must be calculated by dividing the **net nominal accumulated fund** by the **inflation factor** (see paragraph B.3.6~~B.3.5~~).

B.3.2 The **nominal accumulated fund** must be calculated as the sum of:

- the accumulated **current fund**, if any;
- the accumulated **future contributions**, if any; and
- the accumulated amount of any tax relief expected to be reclaimed and credited to the **scheme** for the benefit of the **member** in respect of **future contributions**;

reduced by:

- the accumulated amount of the costs of any **risk benefits**; and
- the accumulated amount of charges or expenses, if the terms of the **scheme** require such charges or expenses to be deducted from **future contributions** or the **current fund**.

B.3.3 Each element of the **nominal accumulated fund** must be accumulated from the relevant date to the **retirement date** at the rate of accumulation determined in accordance with paragraphs C.2.3 to C.2.6. The relevant date is:

- for the **current fund**, the **illustration date**;
- for each individual payment of **future contributions** or tax relief, the date on which the payment is due to be received by the **scheme**; and
- for each individual payment of charges or expenses or cost of **risk benefits**, the date on which the payment is due to be paid.

B.3.4 ~~If the **nominal accumulated fund** is less than zero, zero must be used instead.~~The **net nominal accumulated fund** is the **nominal accumulated fund** reduced by the **lump sum**.

~~B.3.4~~B.3.5 If the **net nominal accumulated fund** is less than zero, zero must be used instead.

Inflation factor

~~B.3.5~~B.3.6 The **inflation factor** must be calculated by compounding the **inflation rate** specified in paragraph C.2.7 from the **illustration date** to the **retirement date**.

B.4 CURRENT FUND

B.4.1 The **current fund** is the value of the relevant assets of the **scheme** in relation to the **member**'s money purchase benefits at the **illustration date**. The **current fund** must be based on a realistic asset value such as:

a) the market value of the assets;

b) the bid value of relevant units;

c) for an insured **scheme**, the policy value on an ongoing basis;

d) for a **scheme** where a **member**'s rights are determined as a share of the **scheme**'s assets, the value of the **member**'s share; or

e) for a with-profits fund or if assets are not readily marketable, a value consistent with the principles of AS TM1 .

B.4.2 The **current fund** includes allowances for any contributions due at the **illustration date** and for the recovery of any tax due to the **illustration date**. It is not necessary to discount these allowances from their expected payment dates. Allowances which are unlikely to change the **statutory illustration** may be omitted.

B.4.3 A **provider** may omit the allowances referred to in paragraph B.4.2 from the **current fund**, provided that if there are **future contributions**, any items due but unpaid which have been omitted from the **current fund** are treated as **future contributions**.

B.4.4 If the **member** is in receipt of income drawdown in respect of part of the assets of the **scheme**, those assets must be omitted from the **current fund**.

B.4.5 Outgoing transfer values which have been agreed but not paid on or before the **illustration date** must not be deducted from the **current fund**.

B.5 FUTURE CONTRIBUTIONS

B.5.1 **Future contributions** are all money purchase contributions due after the **illustration date** which the **provider** determines to be part of a regular pre-determined series of contributions, irrespective of the formal basis on which contributions are determined. They do not include contributions made after the **illustration date** which are not part of a series of pre-determined payments which are expected to continue.

B.5.2 When determining whether a **member** should be treated as paying **future contributions**, **providers** should take into account factors including the **member**'s expectations and the certainty of payment. In the following examples the **member** should normally be treated as paying **future contributions**:

- a **member** of an occupational **scheme** paying a percentage of earnings from time to time (irrespective of whether or not the **member** has an option to change the percentage rate); an exception might be if the **member** is employed on a short-term contract and there is no continuity of employment or of contributions;
- a **member** paying regular contributions into a personal pension or stakeholder pension **scheme** under a direct debit or standing order;
- it is clear from the **provider**'s records that regular payments (such as a particular cash amount or a percentage of earnings) are intended; and
- a **scheme**'s terms describe future money purchase contributions as being single payments, and they form a series of pre-determined payments which are expected to continue until the **member** reaches **retirement date** or State Pension Age.

Initial level of future contributions

B.5.3 The initial level of **future contributions** must be the actual amount of **future contributions** payable for the **scheme year** following the **illustration date** if it is known.

B.5.4 If paragraph B.5.3 does not apply and if the amount of **future contributions** is determined as an amount which increases in line with inflation or as a proportion of the **member**'s earnings, the initial level of **future contributions** must be the latest known amount of contributions increased for the appropriate period at the rate specified in paragraph C.2.7 or C.2.8 respectively.

B.5.5 If neither paragraph B.5.3 nor paragraph B.5.4 applies the initial level of **future contributions** must be the last known annual amount.

B.5.6 If the amount of **future contributions** is related to the **member**'s earnings and if the **provider** does not have detailed information about the **member's** earnings or if earnings are expected to fluctuate significantly from year to year, the initial level of **future contributions** must be estimated.

B.5.7 For many occupational **schemes** the definition of earnings for pension contributions is updated annually, on the first day of the **scheme year**. In such cases the initial level of **future contributions** may be based on the **member**'s earnings on the day after the **illustration date**. **Providers** may ignore any information they have about changes in the **member**'s earnings which occur after the day after the **illustration date.**

Subsequent levels of future contributions

B.5.8 **Future contributions** must be assumed to increase in accordance with **scheme** provisions or with recognised practice. If there are no **scheme** provisions regarding the increase of contributions, or if there is no recognised practice of increasing contributions, **future contributions** must be assumed to remain unchanged until **retirement date**.

B.5.9 **Future contributions** which are determined as a proportion of the **member**'s earnings must be assumed to increase at the rate specified in paragraph C.2.8.

B.5.10 **Future contributions** which increase in line with inflation must be assumed to increase at the rate specified in paragraph C.2.7.

B.5.11 It may be assumed that **future contributions** which relate to the payment of the maximum non-earnings-related amount into a personal or stakeholder pension **scheme** remain fixed or increase at the rate specified in paragraph C.2.7.

B.5.12 If the amounts of contributions payable are subject to a maximum of a fixed monetary amount or a deduction of a fixed monetary amount the **provider** must deal with the situation in an appropriate manner.

B.5.13 A deduction which is specified in such a way that it will, or is expected to, increase broadly in line with State benefits or contribution limits or with earnings must be assumed to increase at the rate specified in paragraph C.2.7 or C.2.8 as appropriate.

B.5.14 Contributions which are age-related or term-related must be dealt with in an appropriate manner.

B.5.15 If the last known amount of contributions does not relate to a period of 12 months the **provider** must deal with the situation in an appropriate manner.

Transferred benefits

B.5.16 Incoming transfer values which have been agreed but are outstanding at the **illustration date** must not be included in **future contributions**.

B.6 RISK BENEFITS

Initial level of the cost of risk benefits

B.6.1 If the cost of **risk benefits** payable for the **scheme year** following the **illustration date** is known, it should normally be used for the initial level of the cost of **risk benefits**.

B.6.2 If paragraph B.6.1 does not apply and if the cost of **risk benefits** is determined as an amount which increases in line with inflation or as a proportion of the **member**'s earnings, the initial cost of **risk benefits** should be the latest known cost increased for the appropriate period at the rate specified in C.2.7 or C.2.8 respectively.

B.6.3 If neither paragraph B.6.1 nor paragraph B.6.2 applies, the initial cost of **risk benefits** should be the last known annual amount.

B.6.4 If the last known cost of **risk benefits** does not relate to a period of 12 months the **provider** must deal with the situation in an appropriate manner.

Subsequent levels of the cost of risk benefits

B.6.5 If **risk benefits** are determined as a proportion of the **member**'s earnings their cost must be assumed to increase at the rate specified in paragraph C.2.8.

B.6.6 If the cost of **risk benefits** increases in line with inflation it must be assumed to increase at the rate specified in paragraph C.2.7.

B.6.7 If the cost of **risk benefits** increases as the **member** ages then **providers** must deal with the situation in an appropriate manner.

B.6.8 If none of paragraphs B.6.5 to B.6.7 applies, the cost of **risk benefits** must be assumed to increase at the rate specified in paragraph C.2.7.

B.7 ANNUITY RATE

B.7.1 The **annuity rate** is the value of an annual pension of £1 at **retirement date** calculated using the assumptions in Part C.

B.8 GENERAL CONSIDERATIONS

B.8.1 Where a **provider** assumes a **lump sum** will be paid at **retirement date,** that **lump sum** should be disclosed in today's (inflation adjusted) terms in the **statutory illustration statement.**

~~B.8.1~~B.8.2 Appropriate adjustments to the calculations must be made if a **scheme year** is not a period of 12 months. Where annual rates are specified in Part C, the equivalent rates for part of a year should be calculated as the appropriate root of the annual rate, not as an arithmetic proportion. For example, the monthly rate equivalent to 2.5% per annum is approximately 0.00206 (1.025^(1/12)-1) and not 0.00208 (0.025/12).

~~B.8.2~~B.8.3 If it is necessary to calculate the period between two dates, the period must be calculated to an exact number of months or more accurately (for example, to the exact number of days). Similarly, if contributions will continue for part of a year, **statutory illustrations** must include an allowance for such contributions for an exact number of months or more accurately.

~~B.8.3~~B.8.4 The **pension** illustrated may be shown as a weekly, monthly or annual amount.

C ASSUMPTIONS

C.1 INTRODUCTION

C.1.1 This Part sets out the actuarial assumptions which must be used in providing **statutory illustrations**.

C.2 ACCUMULATION

C.2.1 This section specifies the assumptions to be used in determining the **net real accumulated fund.**

Mortality

C.2.2 No allowance is to be made for mortality before retirement (other than in the calculation of the cost of any **risk benefits**).

Accumulation rate

C.2.3 In determining the **accumulation rate** the **provider** must take account of the expected returns from the current and anticipated future investment strategy of the **member**'s funds over the period to the **retirement date**.

C.2.4 The **accumulation rate** must be based on expected returns before the deduction of expenses or charges.

C.2.5 The **accumulation rate** must be justifiable and consistent with the **inflation rate** assumption specified in paragraph C.2.7.

C.2.6 The method used to determine the **accumulation rate** in accordance with paragraphs C.2.3 to C.2.5 should be consistent from year to year, and the rationale used should be documented and made available to members on request.

Rates of increase in inflation and earnings

C.2.7 The **inflation rate** must be 2.5% per annum compound.

C.2.8 Earnings and any earnings-related indices must be assumed to increase at 2.5% per annum compound.

Expenses

C.2.9 If the terms of a **scheme** require future charges or expenses to be deducted from **future contributions** or the **current fund**, then:

- for **schemes** subject to the FC~~S~~A Rules on projections, charges or expenses must be assumed to be an amount not less than those required by the FC~~S~~A Rules;
- for other **schemes**, amounts no less than the actual charges or expenses of the **member**'s arrangement must be assumed. The assumed charges or expenses should include the costs of investment management, but exclude any dealing costs for the underlying portfolio and any routine management and servicing costs of existing property investments.

C.2.10 Future charges or expenses which are related to **future contributions** (such as those which are calculated as a percentage of contributions) must be calculated by reference to the **future contributions**.

C.2.11 Future charges or expenses up to **retirement date** which are related to the **scheme**'s assets must be calculated using a projected fund as at each annual anniversary of the **illustration date** or, more frequently, from the **illustration date** to the **retirement date**. The projected funds must be based on the **current fund** and allow for any **future contributions**, tax relief, the cost of **risk benefits** and relevant charges or expenses.

C.2.12 If future charges or expenses are not known and cannot reasonably be obtained or estimated, the approach set out in paragraph C.2.11 must be used with charges or expenses of 1% per annum of the projected fund at the start of each year.

C.2.13 Future charges or expenses which relate to the **member**'s arrangement and which are not deducted from **future contributions** or from the underlying assets must be ignored for the production of the **statutory illustration**.

Tax relief on contributions

C.2.14 Tax relief must be assumed to be at the rate at which it is expected to be reclaimed. The expected rate should allow for any known future changes.

C.3 ANNUITY

Lump sum at retirement

C.3.1 ~~No allowance may be made for the payment of a **lump sum** at retirement.~~The **lump sum** assumed to be paid at retirement date should not normally exceed the amount permitted by the **scheme** rules or legislation. Where the **lump sum** assumed is greater than 25% of the **nominal accumulated fund** or is greater than the tax-free lump sum permitted by the **scheme** rules or legislation, the **provider** should document the rationale for doing so.

Interest rates to be used in calculating annuity rates

~~C.3.1~~C.3.2 The rate of interest must be determined as at each 15 February. This rate must be used for all **statutory illustrations** with **illustration dates** occurring in the following financial year (6 April to 5 April). If the information on which the rate of interest is to be based is not published for 15 February, **providers** must use the relevant information for the previous business day for which such information is published.

~~C.3.2~~C.3.3 When it is assumed that the **statutory illustration** increases in payment at a rate linked to inflation, t~~T~~he **annuity rate** must be calculated using annual interest equal to 50% of the sum of the FTSE Actuaries' Government Securities Index-Linked Real Yields over 5 years assuming:

- 5% inflation; and
- 0% inflation

minus 0.5%.

C.3.4 When it is assumed that the **statutory illustration** does not increase in payment, the **annuity rate** must be calculated using the FTSE Actuaries' Government 15 year Fixed Interest Yield Index except that at the **provider**'s discretion the annuity rate may be calculated using the yield set out in paragraph C.3.3 plus 3.5%.

~~C.3.3~~C.3.5 The interest rate must be rounded to the nearest multiple of 0.2%. Intermediate exact multiples of 0.1% should be rounded down.

C.3.6 Published interest rates must be used without any adjustments (such as to convert the published rate from a convertible half-yearly rate to an annual rate).

C.3.7 When it is assumed that the **statutory illustration** increases in payment at a rate other than those described in C.3.3 and C.3.4, the **annuity rate** must be determined using an approach consistent with C.3.3 or C.3.4.

Expenses

~~C.3.4~~C.3.8 An allowance of 4% of the value of the annuity at retirement must be made for expenses.

Mortality

C.3.9 The mortality of the **member** and the **member**'s spouse or civil partner must be based on the year of birth rate derived from the Institute and Faculty of Actuaries' Continuous Mortality Investigation tables PCFA00 and PCMA00 and including mortality improvements derived from each of the male and female annual mortality projection models, in equal parts.

~~C.3.5~~C.3.10 For **statutory illustrations** produced with **illustration dates** in the range 6 April 20YY to 5 April (20YY+1), mortality improvements must be derived from the CMI mortality projection models[1] CMI_(20YY-1)_F[1.25%] and CMI_(20YY-1)_M[1.25%].

~~C.3.6~~C.3.11 For example, **statutory illustrations** produced with an **illustration date** of 6 April 2014 the mortality assumptions must be based on

50% of PCMA00 including improvements based on CMI_(2013)_M[1.25%] +

50% of PCFA00 including improvements based on CMI_(2013)_F[1.25%].

~~C.3.7~~C.3.12 These rates of mortality improvement apply to both the **member** and the **member**'s spouse or civil partner.

Spouse's or civil partner's pension

~~C.3.8~~C.3.13 ~~**Legislation** specifies the assumption to be used for the amount of pension to be provided to the spouse or civil partner on the death of the member.~~ Where illustrated, the amount of any spouse's or civil partner's pension should not exceed the amount permitted under the **scheme** rules or legislation.

Age difference between member and spouse or civil partner

~~C.3.9~~C.3.14 It must be assumed that a husband is three years older than his wife and that those in a civil partnership are the same age as each other, except that:

- at the **provider**'s discretion the **member** may specify the spouse's or civil partner's age to be used;
- the spouse's or civil partner's age shown in the **provider**'s records may be used.

Guaranteed annuity terms

~~C.3.10~~C.3.15 No account should be taken of a guarantee of annuity terms which produces a higher amount of initial pension as at the **retirement date**, or a higher amount of pension in a subsequent year, than would be produced using the assumptions in AS TM1.

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[1] The model can be found at: http://www.actuaries.org.uk/knowledge/cmi
CMI_20NN_x [a%] refers to the model published by the CMI where:

- 20NN is the version number of the model reflecting the year of its publication;
- x is the gender and is either M (male) or F (female); and
- a% is the long-term rate of mortality improvement.

Payment frequency and format

~~C.3.11~~C.3.16 When calculating the **annuity rate, providers** may allow for benefits, other than a spouse's or civil partner's pension, payable on the death of the **member** after the pension commences (such as the payment of the balance of five years' payments on death within five years after retirement).

~~C.3.12~~C.3.17 The pension illustrated must be assumed to be payable monthly in advance ~~and increase annually in payment in line with inflation~~ and when it is assumed that the statutory illustration increases in payment, those increases are assumed to apply annually. Pension increases in payment in line with inflation are implicitly allowed for in the rate of interest specified in paragraph C.3.3.

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