



BOARD FOR ACTUARIAL STANDARDS

**TECHNICAL MEMORANDUM TM1: STATUTORY MONEY
PURCHASE ILLUSTRATIONS**

SUPPLEMENTARY INFORMATION

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1 INTRODUCTION

- 1.1.1 The Board for Actuarial Standards (the BAS) is responsible for setting technical actuarial standards in the UK. It is an operating body of the Financial Reporting Council (the FRC).
- 1.1.2 **Legislation** provides that **statutory illustrations**¹ must be produced in accordance with relevant guidance prepared by a prescribed body. The Board for Actuarial Standards is the prescribed body for that purpose. The relevant guidance is *Technical Memorandum TM1: Statutory Money Purchase Illustrations* (TM1).
- 1.1.3 A **statutory illustration** shows the amount of pension that might be payable when a **member** retires in terms of today's prices, assuming that:
- any regular money purchase contributions currently being paid will continue to be paid until the **retirement date**; and
 - the pension at retirement will subsequently increase in line with inflation so that its purchasing power is broadly maintained.
- 1.1.4 **Statutory illustration statements** consist of the **statutory illustration** and accompanying information required by the **legislation** or provided voluntarily.
- 1.1.5 **Providers** issuing **statutory illustration statements** will need to be familiar with the relevant provisions of the **legislation**. The provisions include requirements for **statutory illustrations** to be provided and information that must accompany **statutory illustrations**.

¹ Terms appearing in **bold** in the text are explained in the Glossary in Appendix A.

2 BACKGROUND

2.1 PURPOSE

2.1.1 The purpose of this document is to provide supplementary information for those who are involved in the preparation of **statutory illustration statements** in accordance with TM1. (The content of this document is based on material which was in version 1.4 of TM1 but which did not contribute directly to the calculation of **statutory illustrations**.)

2.2 LIMITATIONS OF STATUTORY ILLUSTRATIONS

2.2.1 **Statutory illustrations** are not tailored to individual circumstances. A **member's** actual pension may differ significantly from the amount illustrated because future experience may differ from the assumptions made and the **member's** individual circumstances may not be reflected in the calculations.

2.2.2 **Statutory illustration statements** are not intended to be individual financial advice or to be used in comparing the merits of particular forms of pension provision (such as comparing benefits from defined benefit and defined contribution arrangements or comparing different investment choices).

2.3 THE APPROACH TO SETTING THE ASSUMPTIONS IN TM1

2.3.1 **Statutory illustrations** are intended to provide **members** with a broad indication of the pension to be expected from their current funds and future contributions. Whatever standard assumptions are chosen for **statutory illustrations**, they are unlikely to be borne out in practice, either in general or for particular individuals.

2.3.2 Stable long-term assumptions are more appropriate for younger **members** than assumptions linked to current market conditions, which would be likely to produce more volatile results from year to year.

2.3.3 A **statutory illustration** for a member close to retirement should be expected to bear some relationship to what the **member** will actually receive on retirement. Although there may still be significant variations between the standard assumptions and what actually occurs, a set of assumptions related to current market conditions would be appropriate for such **members**.

2.3.4 The basis for TM1 combines these two approaches. The assumptions for the period before retirement are long-term assumptions. The assumptions for the cost of purchasing annuities at retirement are based on conditions on a particular date, and can vary significantly from one **illustration date** to the next. For a **member** close to retirement, variations in the rate at which the fund accumulates up to retirement may have less effect than variations in the cost of purchasing an annuity at retirement. This does not mean that a **statutory illustration** for a **member** close to retirement will be more accurate than any earlier **statutory illustrations** provided to the **member**, as there are still likely to be differences between the assumptions made and the actual experience (particularly the cost of purchasing an annuity).

2.4 FSA ILLUSTRATIONS

- 2.4.1 **Members** of personal pension schemes (other than stakeholder pension schemes) will have received point of sale illustrations prepared according to rules issued by the Financial Services Authority (FSA).
- 2.4.2 At the time version 2.0 of TM1 was issued, the FSA required such illustrations to be expressed in projected money terms. Point of sale illustrations are therefore not directly comparable with **statutory illustrations** produced on the basis set out in TM1, which are shown in today's prices.
- 2.4.3 There are additional differences between point of sale projections and **statutory illustrations** which mean that the two illustrations are not directly comparable :
- The FSA requires three separate projections using maximum rates of return of 5%, 7% and 9%pa, unless these rates overstate the investment potential of the product. TM1 requires one projection using an appropriate rate.
 - The FSA allows the projections to be personalised and so assume various percentages of pension for spouses, that the pension will not increase or increase at various rates in retirement and that a cash sum will be taken at retirement.

3 INFORMATION ACCOMPANYING STATUTORY ILLUSTRATIONS

3.1 INTRODUCTION

- 3.1.1 The **legislation** specifies information which must be provided either alongside the **statutory illustrations** or on a suitably signposted website.
- 3.1.2 This section lists some considerations on the provision of additional information and sets out examples of additional information and additional estimates that **providers** might wish to provide to **members** who receive **statutory illustration statements**. The information required by the **legislation** is not listed in this section.

3.2 CONSIDERATIONS FOR PROVISION OF ADDITIONAL INFORMATION

- 3.2.1 When determining which additional information or estimates are provided, **providers** should note the following:
- **Statutory illustration statements** should be provided in plain English. A long explanation may not be read and the impact of the **illustration statement** might then be lost.
 - **Members** who require more information or technical details can ask the **provider** to supply it. **Providers** might therefore wish to limit the amount of additional information automatically given to **members**.
 - The basis set out in TM1 for the calculation of **statutory illustrations** is not intended to constrain the assumptions or methods that are used to provide other information. Further estimates of pension or other amounts could be provided but it should be made clear to the **member** which is the **statutory illustration**. An explanation of why any further estimate have been produced might need to be given.
 - Additional information could be provided as part of the **statutory illustration statement**, in a separate explanatory document, or on a website.

3.3 INFORMATION WHICH MIGHT BE PROVIDED

- 3.3.1 **Providers** might wish to consider whether to provide **members** receiving **statutory illustrations** with the information or estimates described in the remainder of this section.

Identifying the member and scheme

3.3.2 **Providers** should consider what information is needed to identify the **member** and the **scheme** concerned. Possible items include:

- the **member's** name, National Insurance Number and date of birth;
- the name of the **scheme**; and
- if the **statutory illustration** is shown as a single total amount for more than one fund or contract with the same **retirement date**, sufficient information for the **member** to be able to identify which funds or contracts have been included in the **statutory illustration**.

Warnings

3.3.3 **Providers** should consider providing a statement encouraging the **member** to obtain further information or advice before taking any action on the basis of the **statutory illustration statement**.

3.3.4 **Providers** should consider stating that the **member's** eventual pension may differ significantly from the **statutory illustration**, because it will depend on what actually happens in practice, which may differ significantly from the assumptions that have been used.

Risk and Uncertainty

3.3.5 **Providers** should consider providing additional information about risk and uncertainty (for example, stochastic illustrations).

3.3.6 **Providers** should consider whether a measure of the sensitivity of results to changes in one or more of the assumptions (for example, the effect of a 1% per annum variation on investment return or the interest rate used in calculating the **annuity rate**) would be useful in demonstrating the risk and uncertainty in the **statutory illustration**.

Assumptions

3.3.7 **Providers** should consider stating the assumptions that have been used including:

- how the **member's** pension fund is invested and the investment returns that it will produce;
- the interest rate used in calculating the **annuity rate** used to convert the projected fund into a pension;
- the age of the **member's** spouse or civil partner at the **illustration date**; and
- the allowances made for charges or expenses and **risk benefits**.

Year on year changes

3.3.8 **Providers** should consider giving **members** an explanation of any material changes to their **statutory illustration** from the previous **statutory illustration**. For example, **providers** might wish to explain any changes to the **statutory illustration** arising from the abolition of money purchase contracting-out.

Assets

- 3.3.9 **Providers** should consider stating the value of the **member's current fund** and whether the value is the actual value or has been estimated. If the **current fund** is invested in a with-profits fund or a deferred annuity contract, the **provider** may disclose an amount for the **current fund** which is consistent with information to which the **member** is accustomed to receiving, even if it differs from the asset value used as the basis of the **statutory illustration**. In this case, **providers** should consider giving an explanation or definition of the amount which has been disclosed.
- 3.3.10 If a **member** has a range of investment choices within the arrangement, **providers** should consider explaining the different characteristics (such as risk and return) of alternative future investment strategies.

Contributions

- 3.3.11 **Providers** should consider stating the amounts paid in the **scheme year** by the Government as tax relief, with any explanation needed, such as explaining that the amount of tax relief shown might omit any higher rate relief received direct by the **member**.
- 3.3.12 If contributions are fixed in nominal terms, **providers** should consider explaining that this represents a reducing real rate of contribution in relation to the assumption made about future inflation.
- 3.3.13 If appropriate, **providers** should consider explaining that the **statutory illustration** includes tax relief in respect of **future contributions** which is expected to be reclaimed and credited to the **scheme** for the benefit of the **member**.
- 3.3.14 If appropriate, **providers** should consider stating that they do not intend to provide subsequent **statutory illustrations** unless further payments are received.
- 3.3.15 **Providers** should consider providing an additional estimate to show the effect of making additional contributions.

Data

- 3.3.16 **Providers** should consider stating whether the details of the spouse or civil partner have been assumed by the **provider**, have been taken from the **provider's** records or have been specified by the **member**.

Terms of the arrangements

- 3.3.17 **Providers** should consider providing a description of any guarantees which may apply, such as guaranteed annuity rates.
- 3.3.18 If benefits are underpinned by an amount under the Guaranteed Minimum Pension (GMP) provisions of the State pension arrangements, **providers** should consider including an explanation of the GMP underpin or an accompanying estimate of the amount of pension in respect of the GMP.
- 3.3.19 **Providers** should consider providing details of death benefits before retirement and any death benefits after retirement not taken into account in the calculation of the **statutory illustration**.

- 3.3.20 **Providers** should consider including an explanation of any allowance for a benefit on death of the **member** after retirement, other than a spouse's or civil partner's pension, included in the **statutory illustration**.
- 3.3.21 If a **scheme** does not provide for a pension which increases in line with inflation, **providers** should consider stating this, or providing an indication of how the **member** could use the fund to purchase an inflation-linked pension.
- 3.3.22 **Providers** might wish to consider providing additional information or additional estimates to:
- reflect more closely the **member's** actual circumstances (for example, the **member's** intended date of retirement if it differs from the **retirement date**);
 - show a lump sum on retirement together with a reduced pension amount;
 - show a non-increasing pension; or
 - show a pension for the **member** with no pension payable to a spouse or civil partner on the death of a **member**.

Transfers and divorce

- 3.3.23 If a transfer of part or all of a **member's** benefits was in hand at the **illustration date** or a transfer value has been received in the year preceding the **illustration date**, **providers** should consider warning the **member** about possible double-counting or omissions if **statutory illustrations** from different arrangements produced on different dates are added together.
- 3.3.24 Where relevant, **providers** should consider stating that the benefits are subject to a pensions debit or earmarking order.

A GLOSSARY

A.1 Terms used in TM1 are set out below with their meanings. Not all of these terms appear in this document.

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 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: <ul style="list-style-type: none"> a) <i>the Pension Schemes Act 1993 (c.48) Section 113;</i> b) <i>the Personal Pension Schemes (Disclosure of Information) Regulations 1987 (SI 1987/1110);</i> c) <i>the Occupational Pension Schemes (Disclosure of Information) Regulations 1996 (SI 1996/1655);</i> d) <i>the Stakeholder Pension Schemes Regulations 2000 (SI 2000/1403);</i> e) <i>the Occupational and Personal Pension Schemes (Disclosure of Information) Amendment Regulations 2002 (SI 2002/1383);</i> and f) <i>the Occupational, Personal and Stakeholder Pension Schemes (Disclosure of Information) Amendment Regulations 2010 (SI 2010/2659).</i> <p>Northern Ireland has its own body of law relating to pensions with corresponding legislation.</p>

member	Any person eligible to receive a statutory illustration from a scheme .
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.
real accumulated fund	The 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 calculated in accordance with TM1.
statutory illustration statement	The statutory illustration and accompanying information.



FINANCIAL REPORTING COUNCIL
5TH FLOOR
ALDWYCH HOUSE
71-91 ALDWYCH
LONDON WC2B 4HN
TEL: +44 (0)20 7492 2300
FAX: +44 (0)20 7492 2301
WEBSITE: www.frc.org.uk

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Registered Office: 5th Floor, Aldwych House, 71-91 Aldwych, London WC2B 4HN.