1 December 2023

The Director of Actuarial Policy
Financial Reporting Council
8th Floor, 125 London Wall
London
EC2Y 5AS

Dear Sir or Madam

Consultation on AS TM1 v 5.1

We have prepared this response on behalf of WTW's Retirement, Employee Experience and Defined Contribution consulting businesses. WTW is a global firm with a substantial presence in UK pensions, providing consultancy, communication, administration services and governance solutions to trustees and sponsors of work-based pension schemes. In addition, the firm provides services to a multi-employer master trust, 'LifeSight', which has over 300,000 members and is growing rapidly.

We trust that our comments are clear and helpful. If you wish to discuss them further, please do not hesitate to contact us.

Yours faithfully

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QUESTION 1 - Do you agree with the proposed change to accumulation rate for volatility group 1 (from 1% p.a. to 2% p.a.)? If not, what alternative accumulation rate do you think would be appropriate for this group? Please provide supporting evidence for any alternative view.

We do not have an issue with the proposal to increase the accumulation return assumption for group 1 given the significant changes in interest rates over the relevant period.

QUESTION 2 Do you agree with not amending the accumulation rate for volatility group 4? If not, what alternative accumulation rate do you think would be appropriate for this group? Please provide supporting evidence for any alternative view.

We do not have an issue with the proposal for the accumulation rate for group 4 to remain unchanged for this review.

QUESTION 3 Do you have any other comments on the proposed accumulation rates as set out above?

While we would normally look for stability in the accumulation rate assumptions from year to year, we do not have an issue with the proposal to increase the accumulation return assumption for volatility groups 2 and 3 given changes in asset yields, in particular bond yields. However, in our view the volatility methodology and volatility group band ranges are showing some anomalous effects that are difficult to explain to members and are likely to be at odds with conventional risk/return descriptions and ratings in investment guides. In our research, longer term fixed interest gilt and index-linked gilts will fall into group 4 and most passive equity, property and many diversified funds into groups 2 and 3. This is in reverse to commonly accepted views that equities carry more investment risks than bonds. This will undermine consistency of messaging to members on investment risk, which is a key risk the Disclosure Regulations require providers to notify members of. We think the actual results are showing up the weaknesses of the volatility approach raised previously.

This can be partly addressed this year by changing the volatility group ranges. For example, if the group 3 boundaries are changed to be 10% - 17%, this would include the longer dated gilts funds and those funds would be in group 3. This would not be a long-term solution but a pragmatic change under the current system. Longer term the FRC may wish to reconsider an asset-class based approach to accumulation rates for common asset classes perhaps combined with the volatility approach for other funds.

QUESTION 4 Do you agree with the proposed effective date of 6 April 2024?

We agree with this proposal on the proviso that the date the calculation is performed, referred to for this purpose and in draft AS TM1 v5.1 C2.8, is the Illustration Date. The FRC should make this clear, in line with our previous correspondence on this point.