RPC

Pension transfers

April 2018

The FCA tries again to get it right with new rules and a further consultation paper.

The FCA has now produced its revised pension transfer rules following the consultation paper published in June 2017. There are some changes from the initial consultation which appear to result from the FCA's review of pension transfer files. The FCA has also published a further consultation paper looking, in particular, at issues arising when more than one firm is involved in the pension transfer process.

The original proposals

If a consumer wants to transfer their defined benefit pension and/or convert their safeguarded benefits and the value of those benefits is over £30,000, the consumer must obtain advice on the transfer. The advice on the transfer must at least be "checked" by a pension transfer specialist and the firm providing the pension transfer advice must be authorised to provide that advice. The mandatory requirement for consumers to obtain advice on a pension transfer was introduced in the wake of the pension freedoms in April 2015.

In the FCA's June 2017 consultation paper, the FCA proposed:

- replacing the transfer value analysis with a broader analysis of a customer's needs and circumstances
- introducing the Appropriate Pension Transfer Analysis (APTA) including the "Transfer Value Comparator" (TVC) that requires an estimation of the present monetary value needed today to fund an annuity matching the benefits in the ceding scheme at retirement. This moves away from looking at the critical yield/investment return required on the transferring funds to match the benefits in the ceding scheme at retirement
- a rule to require that all advice is provided as a personal recommendation fully reflecting the client's circumstances and providing a recommended course of action
- updating the FCA's guidance on assessing suitability when giving a personal recommendation to convert or transfer safeguarded benefits, including removing the starting assumption that a transfer will be unsuitable
- introducing guidance on the role of a pension transfer specialist and what is required of a pension transfer specialist when "checking" pension transfer advice.

The paper also commented that the "outsourcing" of checking and advice functions of pension transfer specialists was already adequately addressed in the current rules. In particular, if the "checking" of the transfer advice was outsourced the adviser

Any comments or queries?

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giving the overall advice remained responsible for the advice to the client and if the "advice" on the transfer was outsourced both firms had the burden to demonstrate that the advice they provided was suitable.

Events since the June 2017 consultation paper

In October 2017 the FCA published its findings of its supervisory work on pension transfer advice. The FCA found that only 47% of advice on pension transfers was demonstrably suitable. The FCA also found that only 51% of the advice provided to British Steel pension scheme members could be shown to be suitable and that in 16% of files, advice was demonstrably unsuitable. A number of firms have voluntarily varied their permissions so that they can no longer provide pension transfer advice and in December 2017 the FCA sent a formal information request to 45 firms, the responses to which the FCA notes they are currently considering.

New pension transfer rules

The headline from the FCA's announcement of its new pension transfer rules was that it would not proceed with its proposal to remove the starting assumption that a pension transfer should be presumed unsuitable. In relation to the other proposals a majority have been adopted:

- an adviser will have to provide a personal recommendation on whether or not to transfer
- pension transfer specialists are to check the entirety of the advice process and not just the numerical analysis, confirm that the personal recommendation is suitable and inform the firm in writing that they agree with the advice before the report is given to the client.

The intention is to resolve any disagreements between the pension transfer specialist and adviser before the suitability report is provided to the client. The requirement that the pension transfer specialist check the "reasonableness" of the personal recommendation has been dropped.

Adoption of APTA

The FCA is not to provide detailed rules and guidance on the relevant elements to include for each individual for the APTA. Instead it is left to firms to decide whether a critical yield approach remains valid in the circumstances.

The FCA has also added further changes to require advisers to consider the impact of tax and access to state benefits, a rule to clarify that APTA must consider a reasonable period beyond average life expectancy, new guidance on considering the PPF and FSCS so they are covered in a balanced way and new guidance in the event that information is provided on scheme funding or employer covenants.

Adoption of TVC

The TVC is not to be personalised and instead firms are expected to take account of personal circumstances when preparing the APTA. The TVC proposal has changed from the consultation phase. It was originally proposed that the TVC would use an estimate of the value needed to replace a client's defined benefit income assuming investment returns consistent with a client's attitude to risk. The final rules do not propose a personalised approach and instead a prescribed rate of return is to be used based on gilt yields. This is likely to result in fewer TVCs indicating that a transfer is suitable for a customer. Although a generic return arguably removes some risk for firms it also means that advisers have to go further and provide additional comparisons based on personalised assumed growth rates to support a pension transfer recommendation.

New rules on assessing suitability

Revisions to COBS 19 are to require a firm to demonstrate that a transfer is in the best interests of the client including taking into account the intention of the client accessing pension benefits, the client's attitude to and understanding of giving up safeguarded benefits, the client's attitude and understanding to investment risk, the client's realistic retirement income needs including how they can be achieved and the alternative ways to achieve the client's objectives instead of the transfer.

Confirmation that streamlined advice is unlikely to be suitable for pension transfers

The APTA and TVC are to come into force on 1 October 2018 with the majority of the other changes having come into effect on 1 April 2018.

Further consultation paper

The further consultation paper invites views on the qualifications of pension transfer specialists, but more substantively on introducing guidance on outsourcing models and assessing a clients' attitude to risk for both investments and the transfer itself. In particular, the further consultation paper proposes:

For all pension transfer specialists to obtain the investment advice qualification by October 2020

The rationale is that it is the FCA's firm position that when providing pension transfer advice account must be taken of the investments in which the transferred funds are to be invested. Even though a pension transfer specialist does not have to give the investment advice on the transferring funds, the FCA considers that the pension transfer specialist needs to be able to identify whether a proposed investment solution is consistent with the client's needs and objectives and ultimately to ensure a pension transfer is not recommended if the destination funds are unsuitable, so a pension transfer specialist will need to assess the suitability of the destination funds even if another firm is advising on this.

Amending the definition of pension transfer to remove any ambiguity

The definition is to change so that it is drafted with reference to the movement of safeguarded benefits to flexible benefits.

Handbook guidance to be introduced for outsourcing cases

In its June 2017 consultation paper, the FCA commented on where responsibility sits in cases where pension transfer advice is outsourced. In particular: where the transfer advice is outsourced to be checked by a pension transfer specialist the adviser giving the overall advice remains responsible to the client; and where the pension transfer advice is outsourced to another firm both firms must be able to demonstrate that the advice they provided was suitable.

The paper comments that consideration should be given to a client's attitude to investment risk and, separately, to their attitude to transfer risk and firms utilising outsourcing models should have appropriate processes and arrangements in place so it's clear which role a firm is playing in cases of outsourced advice and which firm has responsibility/liability for a given piece of advice. The FCA is to provide handbook guidance on the issue and the FCA says that it expects all parties to work together to (1) collect information to inform the transfer and investment advice and (2) recognise that investment advice should also take account of the impact of any loss of safeguarded benefits.

Although the paper refers to firms putting in place agreements so it is clear which party has "responsibility/liability" for the advice given, the content of such agreements is unlikely to influence FOS or remove liability to the ultimate client for the party giving the specialist pension transfer advice.

Self-investors

Consumers transferring safeguarded benefits are not required to obtain advice on the ultimate investment of the transferring funds; such investors can obtain advice on the transfer alone and self-select the destination investments. The FCA comments that it does not consider that it needs to change its rules to address this category of consumer; its expectations are that advisers take account of the proposed destination of the funds and if a transfer is in principle suitable but the transfer is unsuitable because of the proposed destination funds the adviser should explain this.

Triage services
Giving customers information on safeguarded and flexible benefits before they decide to obtain transfer advice

The FCA comments that when reviewing triage services some forms of triage were inadvertently crossing the advice boundary. The FCA is to provide new perimeter guidance to clarify that advising in a generic, balanced form on the advantages and disadvantages of a transfer is appropriate but that no comment can be made on whether or not the customer should consider the transfer in their own personal circumstances.

Assessing attitude to both investment and transfer risk
The FCA proposes new guidance whereby firms should take account of risks and benefits of staying and transferring their benefits, the client's attitude to certainty of income throughout retirement, whether the client is likely to access funds in an unplanned way, the client's attitude to any restrictions on their ability to access funds in a safeguarded scheme and the client's attitude and experience when managing their own investments.

Suitability reports must be provided even where the recommendation is not to transfer

The report also raises a number of questions in relation to investor charging as the FCA considers banning contingent charging on pension transfer advice. The responses on this issue are to inform whether or not the FCA revisits the starting assumption that a pension transfer is unsuitable.

What next?

Over 6 million people are eligible to transfer deferred benefits out of defined benefit schemes with the average size of transfer over £250,000. The figures clearly indicate that there are a lot of consumers who could be affected by pension transfer advice.

It is no doubt helpful that the FCA has recognised that more needs to be done to provide guidance on the outsourcing of pension advice. The FCA's work has also uncovered further issues on triage services and self-investors and the identification and proposals on these issues are likely to be helpful. However, it is far from clear whether or not the new APTA and TVC will provide clarity or confusion for consumers; much is likely to depend on how these new requirements are presented to consumers and the flexibility in the new rules arguably brings some risks for advisers. This is perhaps particularly the case in relation to the APTA where the FCA has decided not to provide any guidance.

The further proposals are open for comment until 25 May 2018. By this time the FCA should have completed its review of the responses to the questionnaire sent in December 2017. We anticipate that the FCA's position will be informed by its assessment of responses to the questionnaires alongside the responses to the consultation paper.

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