



**The FCA Practitioner Panel**

**and**

**The FCA Smaller Business Practitioner Panel**

**Response to HM Treasury's Freedom and Choice in Pensions  
Consultation**

**June 2014**

## **1. Introduction**

The FCA Practitioner Panel and the FCA Smaller Business Practitioner Panel were established by the Financial Services and Markets Act (as amended) to represent the interests of regulated firms and practitioners from smaller regulated firms respectively and to provide input to the Financial Conduct Authority (FCA). The Panels provide advice to the FCA on its policies and strategic development of financial services regulation.

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We provide below some comments and observations regarding the opportunities and risks arising, for UK financial firms, from the Government's proposed reforms to the pensions system.

## **2. Executive Summary:**

- The Panels support the Government's proposals to create greater choice and flexibility for individuals at retirement, and agrees that an informed, active customer base is key to maintaining an effective market in this area.
- To ensure the provision of high quality, impartial advice, the FCA should establish standards for the provision of pensions guidance, and should be responsible for monitoring and enforcing compliance with these standards.
- Where a robust framework of standards exists, it should be possible for guidance to be provided by pension providers or outsourced to trusted third parties. There will be a challenge in ensuring consistency across providers of guidance.
- If required, guidance should be available to consumers not just at the point of retirement but also during the accumulation phase and as consumers approach retirement.
- The demand for free, face-to-face guidance to all consumers should be properly assessed. Given the anticipated volume of consumers reaching retirement each year, there are likely to be capacity and cost constraints associated with providing such guidance for all at retirement.
- Some consumers may wish to opt out of receiving guidance or prefer to engage in other ways (e.g. through digital channels). The industry will need to deliver solutions to meet this demand.
- There needs to be a clear distinction between any initial guidance and subsequent regulated investment advice, including any additional costs to be borne by the consumer.
- There may be an impact on longer-term investment in the UK economy if there is a shift away from the purchase of annuities at retirement.

Panel response:

**A1 - A new tax framework for retirement**

**Question 1: Should a statutory override be put in place to ensure that pension scheme rules do not prevent individuals from taking advantage of increased flexibility?**

From a practical perspective we believe that HMT should consider a statutory override to ensure pension scheme rules do not prevent individuals from taking advantage of the increased flexibility introduced by these changes. Although it is early days there is evidence of some pension schemes not being willing to embrace the flexibility provided in the Budget and such an override would make it clear that all schemes must embrace the changes. However, HMT should be aware that such rules will have cost implications for pension schemes, and that not all schemes in their current form will be set up to allow the flexibility envisaged in the proposed new tax framework.

**Question 2: How could the government design the new system such that it enables innovation in the retirement income market?**

The Government should be aware that there are already products in existence which will meet the requirements of the new rules. However, the removal of the requirement to purchase an annuity will substantially stimulate innovation in its own right. To encourage such innovation in retirement products, some changes could be made to the restrictions currently in place for annuity and pension products; for example, relaxing the maximum permitted guarantee period beyond the current ten years, and allowing annuities to offer varying income. In addition, rules in respect of aggregating pre-retirement assets should be made simpler and easier. Relaxing and simplifying these rules will encourage innovation and more flexible annuity and pension products for customers to consider. There should also be a desire to deliver greater certainty and longevity in respect of the rules introduced so that firms can plan with certainty.

The Government could also consider some form of 'kite mark' for certain low risk solutions and limitation of liability on the adviser, so that they can be provided without the need for costly financial advice.

**Question 3: Do you agree that the age at which private pension wealth can be accessed should rise alongside the State Pension age?**

and

**Question 4: Should the change in the minimum pension age be applied to all pension schemes which qualify for tax relief?**

and

**Question 5: Should the minimum pension age be increased further, for example so that it is five years below State Pension age?**

To ensure trust in retirement saving, the minimum retirement age in private pension schemes should be fixed and aligned for Defined Contribution and

Defined Benefit Schemes. We believe that this should be at the current level of 55 and should not change in line with the increases in the State Pension Age. There is no link between the age at which someone might want to access their private pension and the age at which the Government might – for various reasons – want to give people access to their state pension. Early access for serious ill-health and certain occupations should also continue. If the retirement age of private sector schemes rises on a regular basis with the State Pension Age, this could act as a serious barrier to those who wish to take retirement planning seriously and save harder to enable an early retirement. The flexibility to plan for a number of different sources of income, available at different stages, is an important feature of responsible retirement planning.

From a conduct risk perspective, it would increase risks to customers if they were unable to access both their private and state pension should they need to.

## ***A2 – Supporting choice***

**The government seeks views on its proposed approach to supporting consumers in making retirement choices including, more specifically, on the additional questions below.**

The Panels support the Government's proposals to create greater choice and flexibility for individuals at retirement and agrees that an informed, active customer base is key to maintaining an effective market in this area. It is, however, essential that the Government's proposals are implemented cost-effectively in practice to avoid detriment to both the individual who is retiring and the wider economy. This will be challenging given the short timescales afforded for implementing the proposals.

**Question 6: Is the prescription of standards enough to ensure the impartiality of guidance delivered by the pension provider? Should pension providers be required to outsource delivery of independent guidance to a trusted third party?**

To ensure the provision of high quality, impartial advice the Panels agree that the FCA (working closely with the Pensions Regulator, the Department of Work and Pensions and other key stakeholders) should establish a framework of standards for the provision of guidance. The FCA should also be responsible for monitoring and enforcing compliance with these standards.

The limitations of guidance should be clearly signposted and the benefits of full regulated advice should be clearly articulated to customers, accepting that in its current form regulated advice will not be available to all.

In terms of who provides the guidance due to the complications of customers having many pots from different providers and the issue with regard to "biased" guidance, there are two possible options. The Panels' preferred option would be a referral to an independent provider of guidance such as the Money Advice Service or TPAS. It may be possible for independent guidance to be provided by the pension provider within a robust framework of guidelines, but the provision of such guidance should be kept entirely separate from any sales process, which

could progress as either execution only, guided or fully advised. These are already overseen by the regulator.

On a practical level the use of an independent service or services which already exist is preferable to the creation of a new body, although the issues of capacity, scalability and funding, particularly in the early days, need to be addressed.

The difficulties of providing limited guidance are illustrated in the response. This highlights the importance of advice in this space and the importance of the work that the FCA are doing to enable different forms of advice from simplified/focused advice which can be delivered more efficiently than fully regulated more complex advice.

**Question 7: Should there be any difference between the requirements to offer guidance placed on contract-based pension providers and trust-based pension schemes?**

The Panels do not consider there to be a need to differentiate between the two as consumers in both types of scheme are likely to be seeking similar outcomes.

**Question 8: What more can be done to ensure that guidance is available at key decision points during retirement?**

To ensure that guidance is available at key decision points during retirement, industry stakeholders will need to consider consumers' information needs during the pension accumulation phase, as they approach retirement and at retirement. This might include simplified pension benefits illustrations, introducing the "at retirement" guidance options, and providing clarity around the tools and outcomes the consumer can expect from such guidance.

Given the estimated number of defined contribution scheme members retiring each year, the Panel considers that it would be highly challenging to provide face-to-face guidance to all individuals at retirement, not least due to capacity and cost constraints.

Moreover, it is not clear that all customers would want or need face-to-face guidance. It is therefore important to first understand how customers would want to engage with regard to guidance at retirement, and to deliver solutions that meet these needs – including considering allowing consumers to opt out of receiving guidance as appropriate.

Whilst further work would be required to assess the associated merits and risks, such solutions could, for example, include initial digital engagement through interactive tools (e.g. a decision-tree) with a follow-up conversation with a guidance provider as required (e.g. by telephone, other digital means or face-to-face).

Following the guidance process, customers may need to take further action, such as seeking regulated advice; simplified advice; information from a non-advised broker or comparison service; or an execution-only service. As a result, there needs to be a clear distinction between any initial pensions guidance and any regulated advice that might follow. There also needs to be clarity and

transparency around the cost that consumers will be required to bear for any such guidance and advice.

A further challenge is ensuring consistency across providers of guidance, particularly where there is the potential for this to be delivered by a various industry stakeholders (ranging from the pension provider itself to advisory organisations, such as the Money Advice Service (MAS)). The Panels are supportive of FCA's ongoing work to consider the possible guidance models. They believe the regulator should have a role in information provision to retirees, which providers could distribute on its behalf.

### ***A3 – Defined benefit schemes***

**Question 9: Should the government continue to allow private sector defined benefit to defined contribution transfers and, if so, in which circumstances?**

**And**

**Question 10: How should the government assess the risks associated with allowing private sector defined benefit schemes to transfer to defined contribution under the proposed tax system?**

There will be some people who might benefit from a transfer from a Defined Benefit to a Defined Contribution Scheme. Therefore, to enable freedom and choice we believe that transfers from Defined Benefit to Defined Contribution Schemes should continue in certain prescribed circumstances where it benefits the member of the scheme. There are governance measures in place to which schemes must adhere before a transfer can be made from a defined benefit scheme, but these broadly focus on the prevention of 'Pensions Liberation'. These measures are mainly the responsibility of the transferring scheme, and there is limited focus on whether the transfer is financially suitable to the individual. This could be tightened by making it mandatory that the individual obtains financial guidance from a reputable source before any such transfer is made (in line with response to Q6).

In general the benefits accruing to members from defined benefit schemes exceed benefits that they could purchase from defined contribution schemes, except in specific circumstances, for example ill health. Self-directed transfer should not be allowed.

The government should consider two broad categories of risk. At the macro level, many defined benefit schemes are running deficits; it is unclear how they would fund material demands for transfers without materially reducing the transfer value paid out to members. At the individual consumer level, the presumption should be that lower retirement income will be delivered by an equivalent defined contribution scheme, so there must be a high standard of proof for their financial advisor, for example in the case of impaired lives etc.

#### ***A4 – Financial markets and investment***

##### **The government would welcome views on any potential impact of the Government's proposals on investment and financial markets.**

We believe there could be significant macroeconomic effects of some of the proposals.

The Government's proposals could lead to consumers' moving away from purchasing annuities at the point of retirement and diverting their funds into other types of assets (e.g. savings accounts, property etc.). This could cause a shift over time in the insurance industry's propensity to invest in the UK economy for the longer term, such as in corporate bonds and infrastructure projects.

We broadly agree with the statements made that these proposals could inadvertently lead to a reduction in the insurance industry's appetite to invest in long term UK investments such as gilts, corporate bonds and infrastructure projects.

Additionally, if the proposals were to facilitate transfers out of DB schemes, this would also affect the market for gilts. Over £1 trillion is held in private sector DB schemes<sup>1</sup>. The NAPF<sup>2</sup> has pointed out that pension funds are increasing their allocations to index-linked gilts and corporate bonds once schemes, as is increasingly the case, close either to new members or both to new members and future accrual. Closed schemes now hold 21% in index-linked gilts, compared to 8% for open schemes. The Government may wish to explore granting reserve powers to the FPC to address systemic issues raised by mass transfers out of DB schemes.

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<sup>1</sup>PPF index, February 2013

<sup>2</sup>Trends in defined benefit asset allocation, NAPF, July 2013