



ASSOCIATION OF CONSULTING ACTUARIES

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20 September 2017

Emily Pinkerton and David Berenbaum
Strategy and Competition Division
Financial Conduct Authority
25 North Colonnade
Canary Wharf
London E14 5HS

Dear Emily and David

Advising on Pension Transfers – CP17/16

I am writing on behalf of the Association of Consulting Actuaries in response to the above consultation. As advisers to DB pension schemes we are seeing a very significant increase in requests for transfer values from members and associated costs, and we agree it is very important to ensure the advice framework ensures members receive appropriate information and take appropriate advice.

Schemes give a great deal of information with transfer values, which is then added to by advisers' materials, creating overwhelming amounts of information. There is a risk of members not seeing the wood for the trees and relying on the 'personal recommendation'.

Separately, we would encourage the FCA to liaise with the DWP and the Pensions Regulator on disclosure requirements to streamline the communications, with encouragement for them to be shorter and in plain English and reconsider whether the statutory timescales are sufficient for advice to be provided and informed decisions to be taken.

Our comments on the specific questions raised in the consultation are set out in the Appendix. In summary:

- We support the move to a more neutral position on whether a transfer is likely to be suitable, but suggest that this should go further and a neutral tone should be reflected throughout the guidance.
- We support the introduction of the appropriate pension transfer analysis, but only for those not considering retirement in the near future, although the assumption that the member would not commute scheme pension to take a tax free lump sum undermines the accuracy of the transfer value comparison, given most members would take up this option.
- For those members considering retirement in the near future (not just those near the scheme retirement age) the analysis should reflect their actual plans for retirement and the transfer analysis may not be appropriate.

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- We have concerns that the personal recommendation may cause additional difficulties for individuals wishing to transfer overseas for legitimate reasons.

In addition, where schemes offer partial DB transfers to allow members more flexibility in managing their risks the FCA should state that the principles involved should apply equally.

We hope that you find the contents of this letter of assistance. We would be happy to discuss them further if that is helpful. Please contact me on 020 7432 6635 (david.everett@lcp.uk.com), or my colleague Peter Williams who prepared this response on 01372 733 763 (peter.williams@aonhewitt.com).

Yours sincerely

A handwritten signature in black ink that reads "David Everett". The signature is written in a cursive, flowing style.

David Everett

Chairman, Pension Schemes Committee

On behalf of the Association of Consulting Actuaries Limited

Sent by e-mail to: cp17-16@fca.org.uk

Advising on Pension Transfers

Chapter 3: Giving advice and assessing suitability

1. Do you agree with our proposal to require all advice on the conversion or transfer of safeguarded benefits to be a personal recommendation? Please provide the reasons for your response.

Yes. This appears to be the best approach from our perspective. As stated in the document, the FCA estimates that at most 5% of advice transactions are carried out without a personal recommendation (page 35, para 41). As such, making this mandatory will not impact greatly on the delivery of advice but will make it more robust and remove any ambiguity for the client.

2. Do you agree with our proposals for new guidance on assessing suitability? If not, what guidance do you think would be helpful?

The proposals for new guidance on assessing suitability are sensible. In particular, we welcome the move towards neutrality from the previous starting assumption that a transfer will be unsuitable. This seems to reflect the current reality, in particular following the introduction of the April 2015 flexibilities.

However, our view is that the changes should go further. We are not convinced that 19.1.9 of the handbook should suggest that for a majority of people retaining safeguarded benefits will likely be in their best interests and that advisers should have regard to this. Although we welcome the fact that the revised wording will not require an assumption to be made by the adviser, we think there is a strong case for the tone of the guidance to remain neutral throughout.

As a further example of text that does not appear to achieve neutrality, paragraph 10 in Annex 2 of the consultation document explains that the TVC “is likely to enhance the perception of potential losses arising from transfers...[causing]... an emotional reaction countering the attraction of receiving a lump sum”.

3. Do you agree with our proposals to add guidance to the Handbook to clarify what a pension transfer specialist is expected to do when checking advice on transfers or conversion of safeguarded benefits?

Yes, we support the addition of extra clarity on expectations for transfer specialists.

4. What are your views on how the current qualification requirements for pension transfer specialists operate in practice?

The current qualification requirements are adequate and reasonable to ensure a transfer specialist has demonstrated a sufficient level of knowledge by passing a specific qualification in accordance with the FCA training & competency requirements. However, the lack of a requirement to hold any specific investment qualification means that, in practice, transfer

advice can be delivered as a “standalone” recommendation without investment considerations.

5. Do you have any comments on our explanation of the responsibilities of advice firms and pension transfer specialists?

We do have some concerns over the potential impact of outsourcing pension transfer specialist checking. It would seem appropriate for the pension transfer specialist to be responsible directly to the individual for the advice provided, as their work will form an important part of the advice.

6. Do you have any comments on our explanation of the responsibilities of advice firms and independent pension transfer firms?

Paragraph 3.26 details the process used by some firms without the necessary permissions to provide specialist advice pertaining to transfers. As this states, in this scenario the transfer element of the advice is passed to an adviser with the appropriate permissions; however, the destination of the funds following transfer is handled by the original firm that does not have the ability to advise on the transfer. So, in essence, one firm provides a recommendation as to whether to transfer and a separate organisation recommends the product/plan it will go into and the investment funds within that product.

We do not see how this works for the benefit and protection of the individual client. This process seems to allow the adviser whom the client engaged to deflect any future issues by not accepting responsibility for aspects of the advice. We would expect any advice pertaining to a recommendation of a DB transfer to include suitability and a product and investment recommendation relevant to the client based upon objectives and needs.

Chapter 4: Analysis to support advice

7. Do you agree with our proposals on the introduction of an appropriate pension transfer analysis? If not, how could we amend it?

We support the change in focus away from the critical yield towards a quantification and pictorial illustration of the immediate capital value loss that the individual could well incur through transferring. Although this is doing no more than looking at the issue in a different way and so is neither a weakening nor strengthening of the current approach, we can see how it will be of greater assistance to the individual. Instead of getting hung up on whether investment returns are likely to exceed the critical yield, the advice process can focus on whether the likely loss in capital value is more than compensated for by the greater flexibility provided in the receiving scheme (which may in turn lead to a greater capital value for the individual).

In principle, the analysis should reflect the individual’s personal circumstances and plans for the future. We have a significant concern over the detailed proposals for the Transfer Value Comparison.

A key issue is whether the member would take a cash lump sum at retirement. The proposed new requirement that the comparator should allow for 100% of benefits to be taken as income introduces additional prescription and fails to reflect that in a large majority of cases members commute pension for cash if they remain in the scheme. You note that the majority of people will take a lump sum in paragraph 4.21 of the consultation document but justify

ignoring this important fact on the basis that “in the majority of cases, the CETV will not allow for options that will reduce it”. We do not believe that this is a logical reason for failing to reflect what members are likely to do if they remain in the scheme in the pension transfer analysis. The fact that a CETV assumes a member will not take a lump sum (and hence allows the member to access a higher transfer value) when in practice the member is likely to take a lump sum if they remain in the scheme is a highly relevant factor and may make the difference between a transfer being financially attractive or otherwise. The transfer value comparison should reflect reality – members generally take the lump sum if they remain in the scheme, but the transfer value is generally based on the (more valuable) full pension if they transfer out.

In principle, the transfer value comparison should compare the transfer value available with an appropriate valuation of the benefits that the member would be likely to take if they remained in the scheme. The way in which legislation requires the transfer value to be calculated is not directly relevant to this consideration. In addition to a realistic allowance for the PCLS likely to be taken by a member, this would also point to carrying out the comparison based on current financial conditions rather than conditions at the date the transfer value happened to be calculated. In practical terms, if financial conditions have changed significantly since the transfer value was calculated, given the amount is guaranteed this could be a highly significant factor in considering whether a transfer should take place, which should therefore be reflected in the transfer value comparison.

We acknowledge that obtaining cash commutation factors would involve additional data collection, and that the factors may change in future. However, we do not think that either of these points is a valid reason to prescribe an unrealistic assumption – that members will not commute any pension for PCLS if they remain in the scheme.

For many members tax on payment of benefits and the position on death would also be very relevant factors.

The guidance takes a very light touch to tax, as one of the miscellaneous items that an adviser should have a mind to in personal circumstances (3.13) and later in 4.12 when it is acknowledged that this could be an inherent part of the consideration of crystallising benefits and accessing funds.

We feel that tax is becoming a really important issue even for the man in the street: for many, the tax free cash element of the package will grow by virtue of the DB to DC change, but conversely:

- the Lifetime Allowance charge is significantly more likely to apply by virtue of changing from DB to DC and
- for those who are crystallising an old DB benefit but are still in a current employer’s scheme, the money purchase annual allowance is taking on new significance for ongoing savings potential.

Given its importance, tax should be an item explicitly mentioned in COBS 19.1.10G that firms should consider. Thought should also be given to whether individuals would be more adequately protected if the COBS listed some examples of the tax issues which might require consideration, whilst being clear that this is not an exhaustive list.

8. Do you agree with our proposals on preparing and presenting the client with a mandatory transfer value comparator within the appropriate pension analysis? If not, how could we amend it?

Again, in principle the transfer value comparison should reflect the individual's personal circumstances and plans for the future.

We agree that the transfer value comparison is appropriate for individuals who are some way from retirement. However, we do not believe it is an appropriate piece of information for all members – in particular those intending to retire (whether this is at the scheme's retirement date or at an earlier date) in the near future, particularly where they do not intend to purchase an annuity with the transfer value. We would suggest that the threshold for requiring the transfer value comparison be amended so that this is only needed where the member does not intend to retire in the next year (irrespective of the scheme retirement age).

For those close to retirement, it will be more helpful to reflect what the member is likely to do with the transfer value more accurately in providing the advice. For example, if the individual is considering purchasing an annuity with the proceeds in the near future but is still several years away from the scheme retirement age, it may be more helpful to compare the transfer value with the cost of the early retirement pension which the scheme would provide. If the individual is considering commencing flexible drawdown, a comparison of the likely income from flexible drawdown with the likely income from an early retirement pension from the scheme may be appropriate. Providing more guidance on appropriate comparisons for those expecting to retire in the near future would seem a better approach than compelling the transfer value comparison for this group.

9. Do you agree with the proposed changes to the assumptions for the rolling annuity interest rate, non-annuity mortality, the growth rate and the inclusion of charges?

Yes, these appear reasonable as far as they go, if enhanced with disclosures to the client such as that the annuities are based on average mortality rates and take no account of individual health factors etc and that annuity rates are volatile.

10. What are your views on the use of stochastic tools within appropriate pension transfer analysis? How could the outcomes be presented in a way which results in good consumer understanding, given the format and outcomes presented in other mandated documents?

In our experience some individuals find stochastic analysis difficult to understand. We do not think they should form part of the minimum compliant disclosure requirements. Advisers should be left to provide additional information like this if they think it is appropriate in specific cases.

One area in which it might be appropriate to prescribe how advisers allow for future uncertainty is in the allowance for longevity. For example, the transfer value comparison is based on typical mortality. It would be helpful for individuals to understand the impact of longevity which was, say, 5 years shorter and longer than the central estimate.

11. Do you have any comments on our explanation of the responsibilities of advice firms in relation to software?

No.

12. Do you have any views on the assumptions for CPI and for benefits with caps and collars?

We agree that the gap of 0.5% between the CPI and RPI related assumption now appears too narrow. However, there is a strong argument for reviewing all the economic assumptions together, as suggested in paragraph 4.35.

We note that this question has effectively been superseded by proposals set out in Consultation Paper 17/32.

Chapter 5: Other issues

13. Do you agree with our proposal for the application of the additional requirements for pension opt-outs to be restricted to opt-outs where there are potential safeguarded benefits available?

Our understanding is that you are proposing to limit the additional requirements to where the client will lose the benefit of future accrual of safeguarded benefits on opting out. On this basis, your proposal seems reasonable.

14. Do you agree with our proposal that the new TVC analysis should not be required for any pension opt-outs?

We have not considered this point.

15. Do you have any thoughts on the impact of these proposals on overseas transfers?

We are aware that it can be difficult for members with safeguarded benefits to obtain the advice necessary to transfer to an overseas arrangement. A high level of knowledge is required to provide the necessary advice. It appears that the requirement for a personal recommendation may make the process even more difficult for overseas transfers and may even necessitate a two stage process whereby an individual would need to transfer to a DC arrangement within the UK (allowing advice and a personal recommendation which does not need to consider overseas issues) before transferring from the UK DC arrangement to an overseas arrangement, with associated cost implications.

16. Do you have any comments on our expectations for the provision of streamlined advice when advising on safeguarded benefits?

We do not have any specific comments as, in principle, everything that is appropriate for normal advice should also be appropriate for streamlined advice. However, we do note that the proposed changes to advice in general may make the provision of streamlined advice more challenging. In particular, TVAS can currently be carried out in advance and compared with the individual's risk characteristics. As drafted, the TVC would need to be tailored to the individual's risk characteristics and would therefore require the factfind to be completed in advance of the calculation. This is a much more significant issue for streamlined advice for large numbers of members.

17. Do you have any comments on our cost benefit analysis?

No.

About the Association of Consulting Actuaries (ACA)

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and all actuarial advice given is subject to the Actuaries' Code. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes.

The ACA is the representative body for UK consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

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