Department for Work & Pensions

Safeguarded-flexible pension benefits: simplified valuation and introduction of personalised risk warnings

November 2017 – updated February 2018

Information for pension providers, administrators, trustees and scheme managers

Contents

Introduction

About this guidance

This guidance relates to the valuation that must be undertaken and information that must be provided as a result of the Pension Schemes Act 2015 (Transitional Provisions and Appropriate Independent Advice) (Amendment) Regulations 2017 ('the 'Risk Warning Regulations' – SI 2017/717) and the Pension Schemes Act 2015 (Transitional Provisions and Appropriate Independent Advice) (Amendment No.2) Regulations 2017 ('the Valuation Regulations' – SI 2017/1272).

These Regulations amend the Pension Schemes Act 2015 (Transitional Provisions and Appropriate Independent Advice) Regulations 2015 ('the Advice Regulations' – SI 2015/742) and respectively require trustees and scheme managers to carry out the following activities when members seek to transfer, convert or flexibly access their savings:

- send tailored communications ('personalised risk warnings') to members with safeguarded-flexible benefits
- use the 'transfer value' of members'[1] safeguarded benefits, when assessing whether the value of their pension pots is above the threshold at which they are required to receive appropriate independent advice
- make transitional arrangements to inform members with safeguarded benefits who are affected by the change in valuation methodology.

This non-statutory guidance further explains the information requirements where members hold rights to safeguarded-flexible benefits and suggests best practice for those charged with delivering them. Subject to Parliamentary approval, the regulations will come into force on 6 April 2018. It also explains the impact of the change in valuation methodology on certain schemes offering safeguarded non-flexible benefits.

For additional details on the background, rationale and purpose of the regulations see the accompanying consultation and consultation response at GOV.UK[2].

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[1] Within this guidance document the term 'members' also covers survivors, who inherit safeguarded flexible benefits.

[2] https://www.gov.uk/government/consultations/valuing-pensions-for-the-advice-requirement-and-introducing-new-consumer-protections

This guidance is produced for the assistance of providers, trustees, managers and their advisers. It does not provide a definitive statement of the law and should be read alongside the legislation. Providers, trustees and managers should take legal advice if they are unclear about the requirements placed on them by the legislation.

Who this guidance applies to

Personal pension providers, trustees and managers of occupational schemes whose members hold safeguarded-flexible benefits and those charged with delivering information requirements on their behalf.

The valuation section of this guidance also applies to trustees and managers of occupational schemes whose members hold safeguarded non-flexible benefits (such as salary-related defined benefit schemes) which calculate Cash Equivalent Transfer Values on a 'higher than best estimate' basis.

Please Note: Hereafter, in relation to safeguarded-flexible benefits, trustees, managers, providers and administrators are collectively referred to using the term 'providers', unless specifically referencing the wording of the legislative requirements in the numbered boxes; However, to be clear, the legislative requirements that are described in each of the boxes should be noted by all parties – providers, administrators, trustees, and managers.

Valuation

Box 1

What the Regulations say –

For the purposes of determining whether a member is required to seek financial advice, providers must value the member's safeguarded benefits in accordance with the relevant provisions of the Pension Schemes Act 1993 and the applicable regulations made under it, whether or not the individual has a statutory right to transfer. The relevant regulations are as follows:

- (in the case of an occupational scheme) with the Occupational Pension Schemes (Transfer Values) Regulations 1996 (SI 1996/1847);
- (in the case of a personal scheme) with the Personal Pension Schemes (Transfer Values) Regulations 1987 (SI 1987/1112);
- (where the member has pension credit rights) with The Pension Sharing (Pension Credit Benefit) Regulations 2000 (SI 2000/1054);

disregarding any effects from underfunding (regulation 7D) and 'higher than best-estimate' valuations (regulation 7E).

1. For personal pension schemes offering safeguarded benefits, the effect of the regulations is that providers can use the same method to calculate the value of the benefits for the purposes of determining whether the member is required to seek advice as for calculating the cash equivalent for the purposes of the transfer payment.
2. For occupational pension schemes with safeguarded non-flexible benefits – salary-related defined benefit pension schemes – the vast majority of schemes will see no change. However, from 6 April 2018 occupational pension schemes will be required to disregard any increase resulting from a 'higher than best estimate' calculation of the transfer value (under regulation 7E of SI 1996/1847), when determining whether members are required to seek financial advice.
3. This is intended to ensure that members with the same underlying value of benefits are treated in the same way for the purposes of the advice requirement. All such schemes will in future need to use the best estimate calculation for the purpose of assessing whether the appropriate independent advice requirement applies.

Best practice - getting ready for the change

4. Trustees who believe they may be using the higher than best estimate approach should query this with their scheme actuary, who will be able to advise. Their actuary will recommend the best estimate assumptions for the purposes of calculating whether members need to seek advice.

5. Trustees will be aware that the production of best estimates are dependent on the values allocated to a range of factors, including mortality and investment returns. The decision as to whether the transfer value generated can reasonably be considered to constitute a best estimate is ultimately a matter of judgement for the trustees or managers of a scheme, having obtained the advice of the actuary.

6. Trustees will still be free to offer transfer values on a more generous basis than best estimate – but if they do so, they will also still need to determine whether the member is required to seek advice using the (lower) best estimate calculation.

7. The transitional provisions in the next section will also apply to members of occupational schemes who have been informed on or after 1 October 2017 that they need to seek financial advice, based on a higher than best estimate transfer value calculation. Two methods of compliance are available. These are outlined in box 2 below. Note that these requirements do not apply to members whose transfer values will be above £30,000 even on a best estimate basis.

8. Trustees and managers do not need to issue personalised risk warnings, covered in the remainder of this document, in respect of safeguarded non-flexible benefits. Those requirements only apply to pension scheme members with safeguarded-flexible benefits.

Ongoing Best practice

9. Where trustees and managers of occupational schemes continue to use higher than best estimate transfer values they will wish to take care in how they communicate with members.

10. For most members, the transfer value they are being offered (calculated on a higher than best estimate basis) will be of primary interest. Where the member is being offered over £30,000 but is not being required to seek financial advice (because the value on a best estimate basis is £30,000 or below), trustees may believe it is helpful to explain as part of the member communication why they are not being required to seek financial advice.

11. However, there is no legal requirement to communicate the best estimate transfer value, only the transfer value being offered to the member – in this case the higher figure. Where the transfer value is above £30,000 on *both* estimates, trustees may decide that it is potentially confusing to also communicate the best estimate value.

Transitional Provisions

12. When legislation is revised there will often be those caught by the changeover. The revised valuation method for the advice requirement is no exception. There will be members required to take financial advice under the valuation method in force until 5 April 2018, who would not be required to do so, under the revised valuation method used from 6 April 2018 onward.

13. Transitional provisions ensure providers identify and inform those affected by the change in valuation. Box 2 describes providers' options for meeting this requirement.

Options for delivering the transitional provisions

Box 2

Option 1: Members informed after Valuation Regulations come into force

Providers can meet the requirement under Regulation 6(2) and (3), and wait until 6 April 2018 before contacting members. This requires providers to -

a) identify members who were told between 1 October 2017 and 6 April 2018 that they had to receive appropriate independent advice, but are now no longer required to as a result of the change, and have not contacted their provider to show they've taken it.

b) inform these members in writing by 26 April 2018 that they are no longer required to take advice.

Option 2: Informing members prior to Valuation Regulations coming into force

Alternatively, providers can use Regulation 6(4) and take action before 6 April 2018 which will make them exempt from the requirement to provide information after the regulations come into force. In order to do so providers will need to –

a) put in place measures that identify any members who are told between 1 October 2017 and 6 April 2018 that they have to take financial advice, and may, or will, be exempt from 6 April 2018.

b) inform them in writing that they may not be required to take financial advice from 6 April 2018, and that they can contact the scheme for further information from that date. Members informed before 6 April 2018 will not have to be told pro-actively of the change once the regulations come into force.

Best practice

14. It is each provider's own decision how they explain the introduction of the new valuation method and its affects to their members. However, best practice would expect providers to highlight where there might be other considerations or consequences which could inform a member's decisions to pause an existing request. Some examples of best practice would be for providers to –

    - make members aware that a request to transfer at a later date could result in a different transfer value next time, which could be lower or higher than the existing one;
    - explain any scenarios where scheme rules, or members' contractual terms, do not allow the member to make a further request for a transfer within 12 months or where such a request would incur a fee.

15. Whilst the Valuation Regulations allow for providers to meet the transitional provisions once they have come into force (under option 1), there are some obvious advantages for members being informed at the earliest opportunity as it allows more time for members, who have not yet taken advice, to come to their own conclusions about whether they wish to proceed with their original request. Providers can achieve this outcome (in the case of option 2) by amending the existing communications that they already required to send members about the need to take financial advice, in accordance with regulation 6 of the Advice Regulations.

Personalised Risk Warnings

Circumstances where personalised risk warnings are required?

Box 3

What the Regulations say –

● A member with safeguarded-flexible benefits (irrespective of their pot size) must be sent a personalised risk warning if any of a list of specified 'triggers' relating to a relevant transaction occur. A summary of these triggers is provided in Box 4.

● Personalised risk warnings must be sent by the ceding provider.

What ceding schemes must determine –

● Whether the event – for example an enquiry by the member 'triggers' a risk warning.

● When the risk warning should be sent relative to other disclosure requirements.

16. This section relates to the following legislative requirements -

- Regulation 8A(2) of the Advice Regulations, as amended by the Risk Warning Regulations.
- Regulation 8(2) of the Advice Regulations.

17. Providers should first establish whether an event constitutes a 'trigger event' that requires a personalised risk warning be sent.

What triggers a personalised risk warning?

Box 4

In general four types of action trigger a risk warning –

● the member makes a written enquiry about carrying out a relevant transaction - either a transfer payment, conversion of benefits or payment of an Uncrystallised Funds Pension Lump Sum (UFPLS) from their pension scheme) – or makes a written enquiry about applying for a 'transfer quotation'[3];

[3] We use 'transfer quotation' in this context to mean statement of entitlement or a written statement of the cash equivalent – as defined in Regulation 1 of the Appropriate Independent Advice Regulations 2015. It is used here because this terminology is understood to be common used amongst contract based pension providers, and it is not intended to cover other forms of valuation.

● the member applies to obtain a ‘transfer quotation’ - a valuation used for the purpose of responding to enquiries about transferring or accessing their pension benefits;

● the provider gives a ‘transfer quotation’, or otherwise communicates their intention, agreement or offer to carry out a relevant transaction; or

● the member makes a written request for a valuation.

18. The following activities, amongst others, therefore trigger a risk warning.

    i. The member requests a transfer to another scheme or seeks a ‘transfer quotation’.
    ii. The member asks to convert their benefits into money purchase benefits for the purpose of accessing flexi-access drawdown with their existing provider
    iii. The member asks to withdraw a part, or all, of their pension savings through an UFPLS.

19. Providers should note that the regulations require a personalised risk warning to be sent when the member makes a **written request for a valuation**. This means that:

    - an emailed request for a valuation will tend to trigger a personalised risk warning (see Box 5 for a scenario where the member would not be sent a risk warning).
    - On its own, a valuation given by telephone does not trigger a personalised risk warning.
    - logging on to a website and navigating to the valuation of a pension pot would not generally constitute a request for a valuation.Providers will however wish to seek their own legal advice.

Member requests a valuation - no risk warning is required?

Box 5

A member calls their pension provider to find out the value of pension savings. They are told it over the telephone and later check this is correct by signing into their online account via the firm’s website. Unbeknown to the provider, the member then uses the valuation of their pot to shop-around for a retirement income product.

Even though the valuation provided may be used to inform a later relevant transaction that triggers a risk warning, providers are not required to send a personalised risk warning when the valuation is provided by telephone or at the point it is checked online.

What is the timing for sending risk warnings?

Box 6

What the Regulations say -

Following a trigger, personalised risk warnings must be sent:

● within a month of the event that triggers the requirements (such as the member's request for a transfer quotation); and

● at the same time as, or in advance of, the member's transfer quotation (or the written confirmation of the provider's agreement, intention or offer to carry out the relevant transactions); and

● no later than two weeks before the relevant transaction (such as the transfer to another scheme) completes.

20. This section relates to the following legislative requirements -

- Regulation 8A(3) of the Risk Warning Regulations
- Regulation 6 and 8 of the Advice Regulations
- Regulation 6 of The Occupational Pension Schemes (Transfer Values) Regulations 1996

21. Three separate sets of communications for members with safeguarded-flexible benefits can be triggered by the same event. The respective timings of these disclosure requirements for providers with members who both a) seek transfers and b) have safeguarded-flexible benefits are summarised in Box 7 below. A timeline illustrating the interaction of these communications is available in the Annex.

When various communications to members must be sent

Box 7

(a) Personalised Risk Warnings –within one month of the initial 'trigger' action (or where relevant at the same time as the 'transfer quotation', if provided sooner).

(b) Notification of need to take financial advice – within one month of initial 'trigger action' (or where relevant at the same time as the 'transfer quotation', if provided sooner. This is only sent to members whose benefits under the scheme exceed £30,000.

(c) 'Transfer Quotation'– within 3 months and 10 days of 'trigger' action (that is, a written application or request for a valuation in order to transfer).

22. Whilst it is not a requirement to send these separately, the new Regulations require the ‘transfer quotation’ cannot be sent ahead of personalised risk warnings.

Best practice

23. It is good practice for providers to consider how the three communications can be sequenced, both to ensure sufficient time for members to consider them and to ensure they best support members’ decisions.

24. To maximise the impact of the messages received by the member, providers should consider either –

   - **send both (and where applicable all three) communications at the same time** - the member can make a decision as to what they should do with all relevant information; or where this is not possible…
   - send personalised risk warning and (where relevant) notification to take financial advice well in advance of the ‘transfer quotation’ – this ensures the member has time to consider their guarantees in advance of any decision to surrender them being made.

25. Providers should seek to review and amend their processes in preparation for capturing all circumstances that require administrative changes to meet the new ‘Risk Warning’ requirements. Box 8 below illustrates the legal requirements and best practice for providers for the situation where the request to transfer is received not by the ceding scheme but by the receiving scheme.

Amendments to processes when transfer requests arrive through the receiving scheme

Box 8

Scenario: The member ‘shops-around’ and finds their preferred retirement income product and asks the receiving provider to accept their transfer. The receiving provider contacts the ceding provider on the member’s behalf to arrange the transfer.

Transfers between many schemes are often completed in less than 1 month, the timescale for issuing a risk warning. Therefore we have introduced a requirement that schemes must issue the risk warning no later than 2 weeks before proceeding with the transfer.

The requirement: The ceding provider must ensure that any transfer (or other relevant transaction) in relation to the member’s safeguarded-flexible benefits is **not completed for at least two weeks after the issue of the risk warning**, and inform the member within the risk warning if the transaction will automatically proceed in the absence of further contact by the member.

Best practice

26. Providers seeking further assurance that members make a well-informed decision can take additional measures to confirm with the member that they have read the risk warning and/or still wishes to proceed with their original transfer request.

What must personalised risk warnings include?

Box 9

What the Regulations say -

Personalised risk warnings must include a written ‘narrative section’ which:

- informs the member that their pension contains one or more potentially valuable guarantees, details their features, and how they can access them;
- highlights that proceeding with their proposed relevant transaction will result in losing those guarantees, detailing any other circumstances in which they will be lost;
- explains how the guarantees can be taken and any material restrictions that apply.

The narrative section must be *‘clear and intelligible’*.

The warning to the member that they risk losing guarantees must be ‘prominent’.

27. This section relates to the following legislative requirements -

    - Regulation 8C(2) of Risk Warning Regulations

The narrative section

28. Each provider is responsible for interpreting and acting on the terms ‘clear and intelligible’ and ‘prominent’. These words are intended to have their ordinary meaning. However, Box 10 suggests best practice, following which should ensure compliance with the requirements of the regulations.

Box 10

Suggestions for presenting and formatting risk warnings

"A prominent statement" can be interpreted to mean that it -

- Secures readers attention.
- Emphasises it must be read and considered urgently. .
- Raises the spectre of 'risk' to the reader so that they read and consider its content.
- Uses a formatting style that is eye-catching and stands out.
- Be a separate page from any other communications in the mailing – not hidden within other information about the member's pension benefits.

"Clear and intelligible" can be interpreted to mean

- Using language that is simple and accessible to the reader, yet also concise.
- Avoiding jargon and technical terms.
- Providing descriptions of the guarantees in plain English

29. Whilst providers are not restricted in providing additional information alongside the risk warnings, DWP would caution against this in case it detracts from the key messages that must be included in the risk warning. Too much additional information could lead to the requirements around the prominence of the warning, or the clarity and intelligibility of the narrative not being met.

Best practice

30. Where additional information is provided, good practice would dictate that this should only be to highlight where the option of a secure income which is greater than the guarantee being offered by the risk warning is currently available – for example where the provider offers an enhanced annuity and the member is expected to be eligible.

31. Where explaining the different guarantees available good practice would be for a providers to at least highlight the following -

    - Where a guarantee is available at a specific age or for a limited period of time;
    - What guarantees are available to the member but at a later date
    - Where the member has multiple guarantees and their interaction can lead to more or less choice for the member – this should be explained to the reader.

32. In meeting requirements to explain the circumstances in which guarantees are surrendered, providers will wish to highlight where a decision to access part of the pot will result in guarantees then being lost for the whole of the pot.

33. Providers will also wish to highlight the specific actions which result in permanent and irreversible loss of guarantees.

The income illustration

Box 11

What the Regulations say -

Personalised risk warnings must include an income projection illustration showing:

- a first 'guarantee illustration' - this estimates the annual income offered to the member by the guarantee which is available closest to the future retirement date specified by the member.
- a second 'comparison illustration' showing the annual income the same sized pension pot would provide if used to purchase an annuity of the same type using the most recent rate for the open market[4].

34. This section relates to the following legislative requirements -

    - Regulation 8C(2)(d), (3), (4) and (5) of the Risk Warning Regulations
    - Regulations 17 of, and Part 2 of Schedule 6 to, the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 ('the Disclosure Regulations')

35. The illustrations required within the personalised risk warnings communicate the **relative** value of their guarantee. The two illustrations will be comparable as they are produced using all the same key variables - age of the member, date at which pension pot is converted, and size of the future pension pot; the only exception being the rate at which the estimated future pension pot is converted into a projection of future annual income.

[4] The interest rates to be used for calculating annuity rates for the purpose of the open market comparison are determined by gilt rates as of 15 February each year. This is the method used for producing Statutory Money Purchase Illustrations and is set out in C.3.2 and C.3.3 in AS TM1 4.2. CoBs uses the same methodology for calculating annuity rates.

36. As of 13 November 2017, these assumptions were the same as those set by the FCA for use in producing income projections (see COBS 13 Annex 2[5]), except in two specific respects[6]. In those respects, risk warnings can be produced using the alternative assumptions set in COBs, as in force on 13 November 2017.

37. It is a requirement that the retirement date used for the purpose of both illustrations is the future date closest to the member's selected retirement date on which the guarantee can be exercised. This means that where the member seeking a transfer or other relevant transaction has a selected retirement date which is ahead of the date the guaranteed annuity can be exercised, the illustrations must assume a retirement date when the guarantee becomes available.

38. Providers should also not assume for the purposes of the illustration that where a contributing member is considering whether to transfer ahead of a guarantee becoming available that the member's contributions will cease from the date of the risk warning or the proposed transfer. Rather, they should provide the illustration on the basis of the assumptions set out in AS-TM1 – Paragraph 8, Schedule 6 of Disclosure Regulations – broadly, that members currently paying regular contributions will continue to do so.

Best practice

39. Whilst it is not a specific legal requirement for both illustrations to be presented next to each other, it would represent good practice for providers to do so, because it permits direct comparison by the reader.

40. The Disclosure Regulations specify the messages that accompany the SMPIs. It is a requirement to follow the assumptions (subject to the flexibility described above in paragraph 36) to produce the income projections themselves. However; for the purposes of the risk warnings, it is not necessary to include the additional disclosures required when providing an SMPI.

41. It is nevertheless good practice to highlight to the reader that certain assumptions have been made in producing the income illustration (essentially, those prescribed by Paragraph 7 of Schedule 6 to the Disclosure Regulations) and explain, where applicable, what these are (those required by paragraph 17 of the Schedule 6). However, this approach could presents difficulties where they undermine the clarity and intelligibility of the risk warning narrative section. Where appropriate, providers are permitted to use alternative messages, or indicate where the assumptions can be found or requested.

42. It is also worth noting that where the member seeks to transfer or access part of their pot, while the illustration is only required for their safeguarded-flexible

[5] https://www.handbook.fca.org.uk/handbook/COBS/13/Annex2.html
[6] See Regulation 8c (4) of the 'Risk Warning' Regulations.

benefits, it must be for the whole pension pot, not just the part that is being transferred or accessed.

43. Providers should additionally consider the following suggestions of best practice:

- **Where a guarantee can be exercised immediately**, this fact should be prominently highlighted to inform the member's decision whether to surrender their potentially valuable benefits or exercise this option.

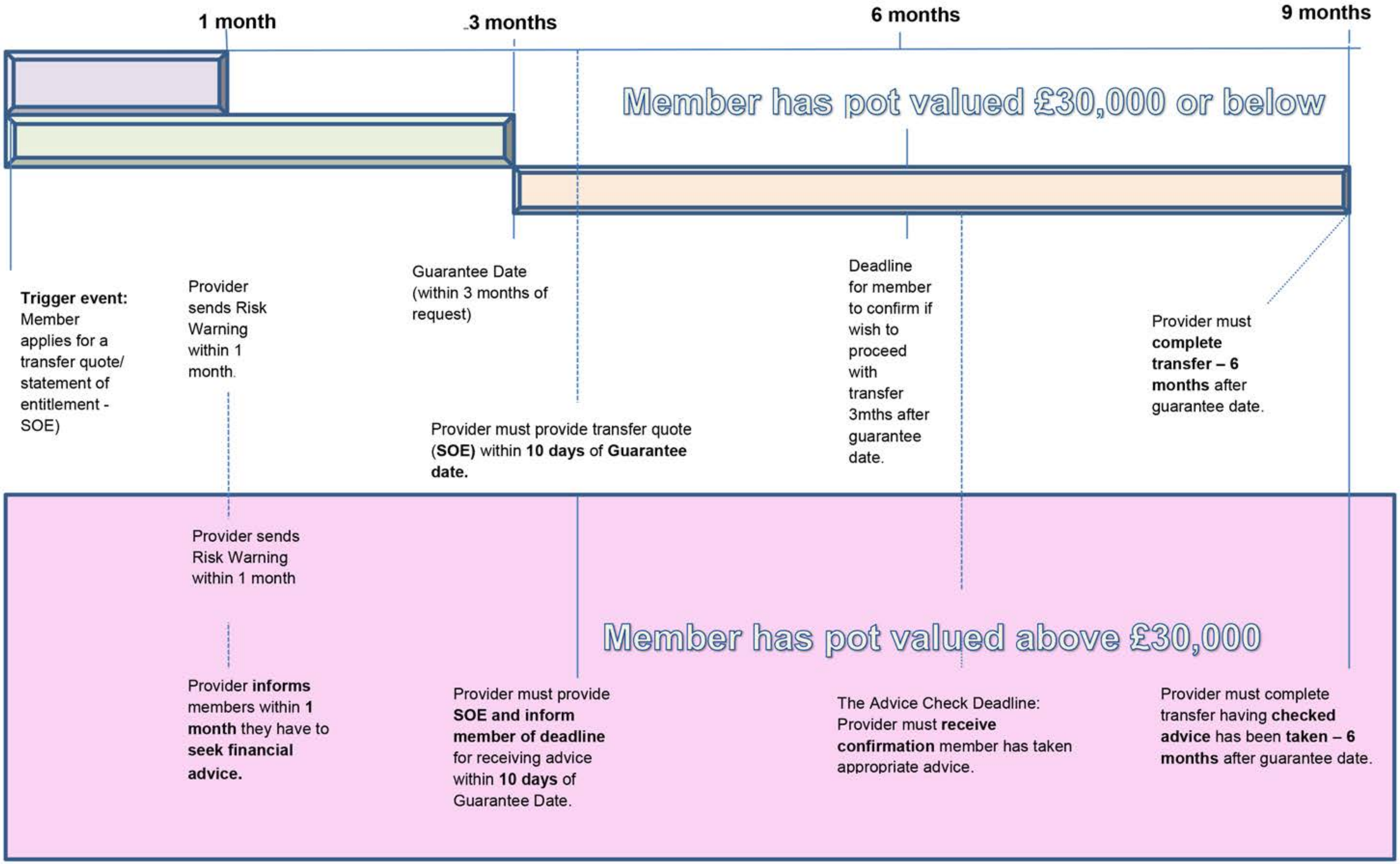
- **Where more than one guarantee is available** to the member, providers still have to produce a 'guarantee' illustration for at least one of the guarantees available.

  However, if there are too many options illustrated (typically more than three), this risks confusing the member. It is therefore better practice to prominently inform the member about these guarantees and offer instructions as to where they can find out more information, if interested.

  Providers should use a combination of what they know about the member, combined with the relative popularity of each guarantee, to choose which guarantee they use to produce a 'guarantee illustration'.

- **Where a member's guarantee offers an annuity rate that differs from a typical single life flat rate annuity**, it is a legal requirement that this 'shape' should be reflected in the calculation of the comparison illustration. However, should there be rare instances where it is not technically possible to reflect the features of the guarantee within the comparison illustration, best practice would suggest providers make it clear where and how the guarantee and comparison illustrations differ.

Annex – Timeline for safeguarded-flexible benefits



Text version: Timeline for safeguarded-flexible benefits

Action to be taken and by when, if a member applies for a statement of entitlement (SOE); referred to here as a ‘transfer quotation’.

Periods of time refer to time elapsed since the application was made.

Pot valued £30,000 or below

- 1 month – deadline for sending risk warning.
- Guarantee date (by reference to which provider calculates cash equivalent) must be within 3 months after the application
- Within 10 working days after guarantee date –‘transfer quotation’ must be provided.
- Within 3 months after the guarantee date– deadline for member to confirm if they wish to proceed with the transfer (6 months maximum from date of application).
- 6 months after the guarantee date – deadline for completing transfer (maximum 9 months after the date of the application).

Pot valued above £30,000

- 1 month – deadline for sending risk warning.
- 1 month – (if transfer quotation provided later) deadline for telling member they are required to seek financial advice and informing member of deadline for confirming they have received advice
- Within 10 days of guarantee date – ‘transfer quotation’ must be provided – and, if within 1 month after application, member informed that they are required to seek financial advice and informed of deadline for them to confirm they have received financial advice.
- 3 months after member is told they are required to take financial advice – the advice check deadline; provider must have received confirmation the member has taken financial advice.
- Within 3 months after the guarantee date– deadline for member to confirm if they wish to proceed with the transfer (6 months maximum from date of application).

- Within 6 months after the guarantee date – provider must complete member’s transfer, having checked the member has received appropriate financial advice (9 months maximum from application).