Advising on pension transfers

Financial Conduct Authority (FCA)

RPC rating: validated

Description of proposal

The FCA has rules which govern advice given to consumers when they transfer between different types of pensions. The FCA's new rules[1] were published in March 2018.

One of the rules relating to advising on pension transfers came into force in April 2018 requiring all advice on pension transfers to take the form of a personal recommendation specific to the consumer's circumstances. Following an initial review notice, the RPC validated an equivalent annual net direct cost to business for this rule of £6.8m on 3 September 2018[2]. Within its opinion, the RPC stated that the FCA had agreed to submit a separate assessment covering the remaining rules when they came into force, as they form part of an overall package of regulation on pension transfers. The remaining rules are:

a) clarifying the role of a pension transfer specialist (PTS);
b) applying a consistent approach for pension opt-outs where there are potential safeguarded benefits; and
c) replacing the current transfer value analysis (TVA) requirement with a requirement to undertake an 'appropriate pension transfer analysis' (APTA) of a client's options and a prescribed transfer value comparator (TVC) indicating the value of the benefits being given up and the cost of purchasing the same income in a defined contribution environment.

The FCA argues that the costs associated with clarifying the role of a PTS through guidance will be negligible as firms were already complying prior to the rules coming into effect. Further, as stated in CP17/16[3], the FCA does not expect firms to incur any costs associated with a consistent approach for pension opt-outs as this

[1] https://www.fca.org.uk/publications/policy-statements/ps18-6-advising-pension-transfers
[2] https://www.gov.uk/government/publications/advising-on-pension-transfers-cp1716-and-ps186-rpc-opinion
[3] https://www.fca.org.uk/publication/consultation/cp17-16.pdf

represents a clarification of existing rules. Therefore, the assessment provided by the regulator addresses the impact of changes to the current transfer analysis requirement (point c).

At present, when advising on the conversion or transfer of safeguarded benefits, advisers are required to make a comparison, known as TVA. The analysis calculates the rate of return (critical yield) that is necessary to reproduce the safeguarded benefits being given up. The FCA argues that the existing methodology used in TVA is no longer fit for purpose and consumers may not be getting the appropriate information in an easily understandable format. It therefore outlines new rules for what is required as a minimum for APTA and specifies that a TVC[4] must be included in the APTA.

Impacts of proposal

The majority of advice firms use third-party software to perform the required analysis. Therefore, the costs of system changes would initially fall on software providers before being passed on to advice firms through higher fees. The one-off cost estimates were provided by industry and amount to £50,000 per software system for an overall cost of £600,000. The estimates include all aspects of changes, including familiarisation costs.

Based on consultation responses from advice firms, the FCA does not expect any additional ongoing costs once the new processes and software are in place.

Quality of submission

The regulator has consulted with the affected firms and has based its estimates on information provided by industry. Although the rules confirmed in the FCA's Policy Statement 18/6 Advising on Pension Transfers (PS18/6) come into effect in different BIT reporting years, all of these rules are considered as part of a package of measures in this case and, therefore, qualify as a single regulatory provision. The FCA is in the process of implementing a package of related measures confirmed in the FCA's Policy Statement PS18/20 'Improving the quality of pension transfer advice'. The RPC will expect to see impact assessments for all qualifying parts of the new rules.

[4] A TVC requires the firm to make a calculation involving a projection of the ceding scheme benefits to normal retirement age, the estimated cost of purchasing those benefits using an annuity; and the present value needed today to fund the annuity.

The RPC considers this assessment sufficient to validate an EANDCB of £0.1m[5], giving a total EANDCB of £6.9 m for the rules in PS18/6 relating to advising on pension transfers.

The BIT assessment would further benefit from addressing the points below.

Providing clearer cross-referencing to the consultation document and policy statement. The BIT assessment provides only a minimum level of detail and requires the reader to refer to two additional documents. To improve clarity, the IA would benefit from more clearly cross-referencing the related sections from the cost benefit analysis in CP17/6 and final rules in PS18/6, or including more information from the two supporting documents in the assessment itself.

Costs to advice firms. The estimates provided by industry appear to include only the cost of familiarisation incurred by software providers. The regulator does note that, based on discussions with advice firms, it does not expect any ongoing costs to advice firms once software systems are in place; however, it is possible that advice firms would incur one-off costs of familiarising themselves with the new rules and the new software. Furthermore, under the FCA's outsourcing rules, firms are not able to fully outsource compliance with rules and they are, therefore, obliged to be familiar with all rules that apply to their respective business, ensure staff are trained and integrate them into their compliance and risk frameworks. Given the scale of the expected impact, the RPC considers this approach reasonable; however, the IA would greatly benefit from including these costs or providing evidence that they would negligible.

Costs related to updating the assumptions made about future inflationary increases. The FCA considers these costs to be minimal and claim they would only require minor software changes. The RPC accepts that these costs would be small in comparison to the more significant changes required to comply with rules on APTA and TVC. However, if proportionate, the FCA should have consulted explicitly on these costs with the affected firms.

Support for assumption relating to the number of software systems. The FCA assume that there are between 10 and 12 software systems that will require updates. Although this assumption was included in the consultation with industry, the FCA does not provide any evidence in support and further, it is unclear whether there were any objections raised by consultees. The RPC has taken a proportionate view in this case given the likely minimal effect on the validated EANDCB; however,

[5] For reporting purposes, the RPC validates EANDCB and BIT score figures to the nearest £100,000.

in future, the FCA must provide evidence for all assumptions or, if not possible, clearly describe consultee support for the estimates.

Clarity around packages of measures It was not initially clear whether all the impacts related to the broad range of rules under PS18/6 had been appraised either in this impact assessment or in the one submitted to the RPC in 2018. The FCA has subsequently provided sufficient information that this is the case; however, in future, the FCA should set out clearly which costs relate to which rules, especially when they span two BIT reporting years.

Departmental assessment

Classification	Qualifying regulatory provision (all rules related to advising on pension transfers are considered as part of a package and, therefore, in scope of the BIT)
Equivalent annual net direct cost to business (EANDCB)	£0.1m (£6.9m for all rules relating to advising on pension transfers)
Business net present value	- £0.6m
Overall net present value	- £0.6m

RPC assessment

Classification	Qualifying regulatory provision (all rules related to advising on pension transfers are considered as part of a package and, therefore, in scope of the BIT)
EANDCB – RPC validated[6]	£0.1m (£6.9m for all rules relating to advising on pension transfers)
Business Impact Target (BIT) Score	£0.5m (£34.5m for all rules relating to advising on pension transfers)

[6] For reporting purposes, the RPC validates EANDCB and BIT score figures to the nearest £100,000.