Financial Conduct Authority

Consultation Paper CP16/15***

Capping early exit pension charges

May 2016

Contents

We are asking for comments on this Consultation Paper by 18 August 2016.

You can send them to us using the form on our website at:
www.the-fca.org.uk/cp16-15-response-form.

Or in writing to:

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Canary Wharf
London E14 5HS

Email: cp16-15@fca.org.uk

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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Abbreviations used in this paper

CBA	Cost benefit analysis
FCA	Financial Conduct Authority
FSMA	Financial Services and Markets Act 2000
RDR	Retail Distribution Review
TPR	The Pensions Regulator

1. Overview

1.1 On 19 January 2016 the Chancellor announced that the Government would introduce legislation to place a new duty[1] on the FCA to cap early exit charges in certain pension contracts.[2]

1.2 This Consultation Paper (CP) sets out our proposals on the application and level of a cap – and the changes to our Handbook rules – that we believe are required to discharge the duty being placed upon us.

1.3 This consultation is specifically concerned with our approach to discharging the duty to be imposed on the FCA to cap early exit charges for consumers accessing the pension freedoms. The primary legislation defines early exit charges and the purpose of the cap and the duty is narrowly focused on these charges. This consultation does not cover other charges that firms may apply during the lifetime of a pension policy and is not directly related to our recent thematic review of the fair treatment of long-standing customers in the life insurance sector.[3]

Who does this consultation affect?

1.4 Our proposals will most directly impact on:

- consumers with pensions savings who would incur an early exit charge for accessing the pension freedoms
- providers of personal and stakeholder pensions – including operators of self-invested personal pensions

1.5 Our proposals may also be of interest to:

- individuals and firms providing advice and information in this area
- trade bodies representing financial services firms
- consumer bodies

1 The duty is contained in the new s.137FBB FSMA which will be inserted by the Bank of England and Financial Services Act 2016, Royal Assent granted on 4 May 2016.

2 Personal (individual and group/workplace) and stakeholder pensions – including self-invested personal pensions

3 TR16/2: Fair treatment of long-standing customers in the life insurance sector: www.fca.org.uk/static/documents/thematic-reviews/tr16-02.pdf

Is this of interest to consumers?

1.6 Our proposals are likely to be of most interest to those consumers with personal pensions who, after our rules come into effect, face early exit charges when they wish to access their pensions savings at or after age 55[4] but before their expected retirement date.[5] The statutory duty, and hence our proposals, do not make any provision for consumers that have already exited early from their policy or policies.

Context

1.7 The Government announced a series of pension freedoms in the 2014 and 2015 Budgets, which came into effect in April 2015.

1.8 In July 2015, the Treasury launched a consultation[6] concerning barriers consumers may encounter when seeking to access their pension savings under the new freedoms - including early exit penalties.

1.9 The Treasury published its response to the consultation on 10 February 2016[7], concluding that significant numbers of individuals currently face early exit charges at levels that present 'a real barrier to accessing' the freedoms and that action needs to be taken to limit these charges.

1.10 Their response document confirmed that the Government would introduce legislation to place a new duty on the FCA to cap early exit pension charges. The duty will apply in relation to existing contracts which contain an early exit charge and also new contracts.

Summary of our proposals

1.11 In anticipation of the coming into force of the new duty, which gives us discretion over the level and structure of a cap on early exit charges,[8] we outline in this CP:

- our proposals in relation to the application and level of a cap on early exit charges for both existing and new personal pension contracts
- the changes to our Handbook rules that we believe are required to bring a cap into force.

1.12 We consider that the impact for firms in complying with our proposals will be proportionate to the level of protection those proposals offer eligible consumers from the deterrent effect of early exit charges.

1.13 Our proposals will apply to early exit charges as defined in the new legislation[9] at the following levels:

4 This is the age at which consumers currently become eligible to access the pension freedoms.
5 Often called a vesting date.
6 www.gov.uk/government/uploads/system/uploads/attachment_data/file/449861/PU1847_Pensions_transfers_v4.pdf
7 www.gov.uk/government/uploads/system/uploads/attachment_data/file/498871/pension_transfers_and_early_exit_charges_response.pdf
8 The duty does not require or permit us to determine whether or not there should be a cap.
9 The duty is contained in the new s.137FBB FSMA which will be inserted by the Bank of England and Financial Services Act 2016. Royal Assent granted on 4 May 2016.

Contract	Cap level (% of member's policy value)
Existing personal pension contracts	1%
New personal pension contracts	0%

1.14 Where existing contracts have early exit penalties set at less than 1% of the member's policy value[10] our proposed cap will prevent these being raised.

1.15 Separately, the Department for Work and Pensions (DWP) is consulting on a cap on early exit charges in occupational pension schemes.

Equality and diversity considerations

1.16 Our rules will benefit members of personal and stakeholder pensions only when they are over minimum retirement age (i.e. have reached the age at which they become eligible to access the pensions freedoms), but have not yet reached expected retirement date (in accordance with the pension scheme). We recognise that this discriminates against the population under age 55 who may wish to transfer their pensions early.

1.17 We have considered the need to eliminate prohibited / discriminatory conduct, the need to advance equality of opportunity and to foster good relations between those who share a protected characteristic and those who do not. We have in particular taken into account that both Parliament in making new legislation and the FCA in making the rules required under our new duty, are exempt from age discrimination legislation – which shows that sometimes it is necessary to make rules which do impact different consumer age groups in different ways, in order to achieve an important policy aim. In this case, the important aim we are seeking to achieve is to enable consumers over minimum retirement age, who want to access their pensions, to do so at an earlier age than they would otherwise have been able to do.

1.18 Although it is important that we advance equality of opportunity and foster good relations between those who fall into the 55 and over age group and those who do not, we have concluded that the most appropriate age group to benefit at this time is the age group in respect of whom Parliament has decided we must act, who benefit from the pension freedoms that were introduced in April 2015 and who are entering their retirement years.

1.19 We do not rule out that other policy initiatives may be appropriate in relation to other age groups at a later stage. At this time we are taking the action which we believe is appropriate for the FCA, creates appropriate protection for consumers and is consistent with our legal obligations and powers.

1.20 We do not consider that our proposals raise other concerns with regard to equality and diversity issues. We do not believe they will result in direct or indirect discrimination for any of the other groups with protected characteristics, i.e. disability, sex, marriage and civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.

1.21 Members of personal and stakeholder pension schemes who become eligible to access the freedoms will benefit from the proposals, regardless of whether they belong to any of the other protected diversity groups.

10 Defined in our draft rules as the value of the member's accrued rights under the scheme.

Q1: Do you have any comments about the impact of our proposals on equality and diversity?

Next steps

What do you need to do next?

1.22 We are asking for feedback on the proposals set out in this Consultation Paper and in particular we would welcome responses to the consultation questions set out in Annex 2.

1.23 Please send your responses to us at: cp16-15@fca.org.uk by 18 August 2016.

How?

1.24 Use the online response form on our website or write to us at the address on page 2.

What will we do?

1.25 We will consider your feedback and - subject to legislation and assuming it is appropriate to do so - aim to publish a Policy Statement confirming final FCA Handbook rules in autumn 2016, with a view to these rules coming into force on 31 March 2017.

1.26 We anticipate that the duty under FSMA will commence in advance of making the final rules.

2. Purpose

Introduction

2.1 In this chapter we explain the background of the statutory duty to be placed upon us by Parliament to cap early exit pension charges and the scope of that duty.

Background

2.2 The Government announced a series of reforms to the UK retirement market in the 2014 and 2015 Budgets. These reforms included the following pension freedoms, which came into effect in April 2015 and enable consumers from the age of 55 to:

- take their pension savings as cash (in one lump sum or in smaller amounts over time)
- buy an annuity (or other income generating guaranteed products that may emerge)
- use drawdown without any limits applied
- use a combination of these

2.3 The Government wants to ensure that consumers can access these new freedoms easily, and at reasonable cost.[11]

2.4 In July 2015, the Treasury launched a consultation concerning barriers consumers may encounter when seeking to access their pension savings under the new freedoms – including early exit penalties. The consultation ran in parallel with data-gathering exercises conducted by the FCA[12] and the Pensions Regulator (TPR).

2.5 The Treasury published its response to the consultation on 10 February 2016,[13] concluding that significant numbers of individuals currently face early exit charges at a level that presents 'a real barrier to accessing' the freedoms and that action needs to be taken to limit these charges.

2.6 The response document confirmed the Chancellor's earlier announcement[14] that the Government would introduce legislation to place a new duty on the FCA to cap early exit

11 Treasury consultation, Pension transfers and early exit charges: www.gov.uk/government/uploads/system/uploads/attachment_data/file/449861/PU1847_Pensions_transfers_v4.pdf
12 www.fca.org.uk/static/documents/pension-freedoms-data-collection-exercise.pdf
13 www.gov.uk/government/uploads/system/uploads/attachment_data/file/332714/pensions_response_online.pdf
14 At Treasury Oral questions in the House of Commons on 19 January 2016.

pension charges for the personal pensions we regulate[15] and that the duty will apply in relation to existing contracts which contain an early exit charge and also new contracts.

2.7 Separately, the Department for Work and Pensions (DWP) is consulting on a cap on early exit charges in occupational pension schemes.

Legislation

2.8 Amendments will be made to FSMA obliging the FCA to make general rules prohibiting authorised persons from imposing (or including, in new pension contracts, provision for the imposition of) specified early exit charges on members of 'relevant pension schemes'. The objective, as stated in the legislation, is to secure appropriate protection against early exit charges deterring consumers from taking, converting or transferring their pension benefits (these are the ways in which consumers can access the pension freedoms).

2.9 Early exit charges are defined by the legislation. In summary, these are charges borne by the members of personal or stakeholder pensions:

- when taking, converting or transferring pension benefits
- on or after the age at which members become eligible to access the pension freedoms (currently age 55) but before the member's expected retirement date
- only imposed, or only imposed to that extent, if the member takes, converts or transfers benefits before their expected retirement date (in some contracts expressed as a vesting date).

2.10 We are required to make rules that apply both to existing pension contracts and to new contracts.

2.11 In its consultation on "Pensions transfers and early exit charges" (July 2015) and in the Consultation response, the Government made it clear that it did not intend for Market Value Adjustments to be captured as exit charges, for the purposes of the FCA cap. As part of the Government consultation on "Capping early exit charges for members of occupational pension schemes" the Government is seeking views on the approach to defining 'Market Value Adjustments' which will be excluded from the FCA cap.

15 'personal, individual workplace, group workplace, and stakeholder pensions (including self-invested personal pensions)

3. Proposals

Introduction

3.1 Following its consultation concerning barriers that consumers may encounter when seeking to access their pension savings under the new freedoms the Government concluded that action should be taken to limit the deterrent effect of early exit charges.

3.2 In this chapter we set out the approach we have adopted in determining the appropriate level of a cap on early exit charges and our proposals in respect of both existing and new pension contracts.

3.3 The Cost Benefit Analysis (CBA) of our proposals can be found in Annex 1. Since Parliament has enacted legislation to place a duty on the FCA to prohibit specified early exit charges, we do not have any discretion as to whether or not to create a cap, only over the details of exactly how we do so. Our CBA, therefore, focuses on how our proposals directly affect firms, consumers and competition in the market.

Our approach

3.4 Drawing on existing information sources and data collected directly from provider firms we have undertaken an analysis to determine the deterrent effect of early exit charges on consumers accessing the freedoms and the anticipated effect of a cap on firms.

Data collection

3.5 We collected data from a representative sample of provider firms[16] about:

- the number and value of all pension policies (as of 30 June 2015);
- the number of policies that exited early in the six month period from 30th June 2015 to 31 December 2015
- any early exit charges levied

We requested that our sample firms provide this data broken down into bands of policy values and bands of early exit charges, where these are/were levied.

3.6 We also requested forward-looking data on the number and value of policies in respect of policyholders who would reach age 55 between 1 July 2015 and 31 December 2020.

Methodology

16 The Cost Benefit Analysis in Annex 1 explains how we determined this sample.

3.7 We assessed the impacts of setting a cap at a number of possible levels over the four calendar years following implementation[17] ('the relevant period'). We have based our assessment on the relevant policies qualifying for the pension freedoms during this period as projections of consumer behaviour beyond this period are likely to become progressively less reliable.

3.8 We conducted a three-pronged analysis of the impacts:

Consumers	• Additional numbers of policies that we expect to exit during the relevant period as a result of the cap.
Firms	• The present value of the revenue loss to firms as a result of (a) additional numbers of policies exiting during the relevant period as a result of the cap; and (2) lower charges applied on those who would exit regardless of the cap. This represents a transfer to consumers. • Solvency impact and likelihood of firm exit. • Compliance costs.
Competition	• Provider firms' possible reaction to a cap on early exit charges. • Implications for innovation.

Consumer impacts

3.9 The data we collected for this consultation supplements and builds upon the pension freedoms data that we collected and published in 2015.[18] This new data corroborates our initial findings that most personal pension contracts (84% as at 30 June 2015) do not attract early exit charges.

3.10 For those that do, the new data gives us additional detail about the charges, including that they generally apply to old-style pre-Retail Distribution Review (RDR) contracts[19] – 'legacy contracts'. Firms told us that in these contracts, early exit charges were levied to recoup any portion of the up-front sale and advice costs left unrecovered at the point of exit.[20] They said these costs would otherwise have been recovered over the remaining life of the policy. However, we note that this has been calculated by firms as a flat percentage.

3.11 Most firms reported that the processing of an early exit does not give rise to additional administrative costs over and above those incurred in processing an exit at the expected retirement / vesting date and that early exit charges are not designed to recover such costs.

3.12 We projected the numbers and values of policies for policyholders eligible to access pension freedoms in the relevant period by applying certain assumptions[21] to the data provided by firms about the fund value and number of policies for policyholders who are or will become eligible to access the pension freedoms by the end of 2020.

17 For simplicity we have assessed the impact over the four year period starting 1 January 2017, rather than from the target implementation date. We would not expect this difference in start date to have a material impact on the outcomes of our analysis.

18 Pension freedoms data collection exercise: www.fca.org.uk/static/documents/pension-freedoms-data-collection-exercise.pdf

19 The Retail Distribution Review (RDR) introduced new rules at the end of 2012 which, among other things, realigned adviser and platform incentives by removing the commission advisers received from providers.

20 This explanation implies that exit charges fall over time for individual policy holders.

21 We assumed that
- Age 65 is the most common expected retirement date
- 10% of policy holders aged 55 or older as at 30.6.15 retire each year, and the age of policy holders is equally distributed between 55 and 65.
- 20% of policyholders will become eligible to access the freedoms between 2016 and 2020 each year and the ages of policyholders in this population is equally distributed between 50 and 54
- Zero growth in fund value between 30.6.2015 and 31.12.2016, which we consider to be reasonable given poor equity market conditions over the period from 30.6.15 to 16.5.16

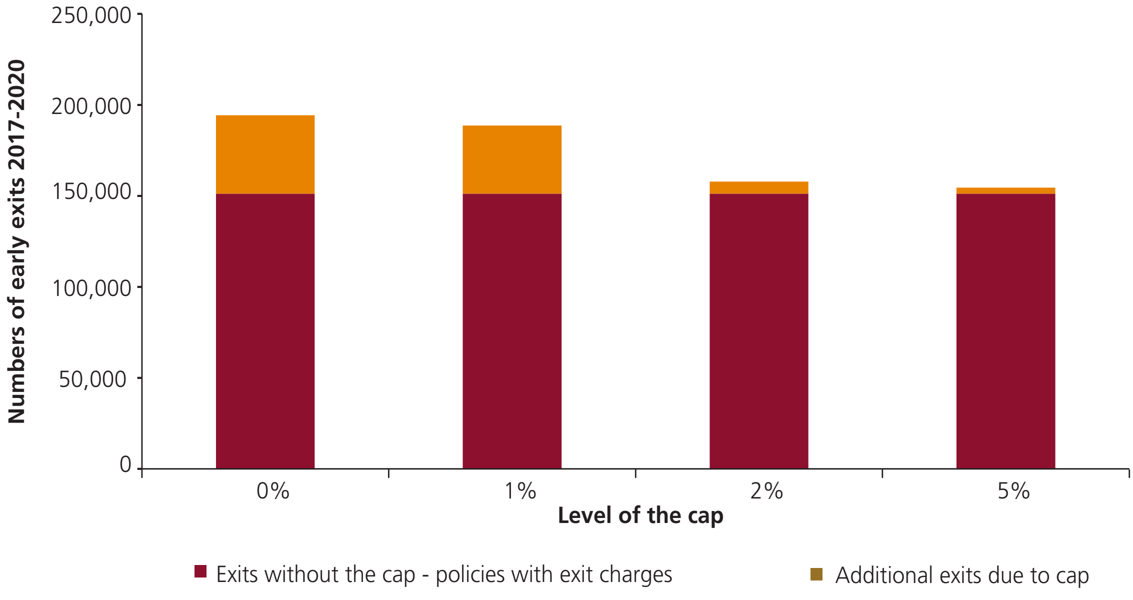
3.13 We then estimated the number of early exits that would occur with and without a cap in place.[22] We did this by estimating the rate of early exit that would occur with and without the cap, based on the pattern of early exits observed in the second half of 2015, according to the level of exit charge levied.

3.14 We have assumed that rates of early exit in the second half of 2015 were abnormally high because this was shortly after the introduction of the pension freedoms on 6 April 2015 and represented the first opportunity to exercise the freedoms for consumers. We have therefore assumed that the exit rates observed in the six month period from July to December 2015 were effectively double those which would persist in the future.[23]

3.15 To predict the additional exits that would occur for a cap of different levels; we assumed that a reduction in exit charge will result in an increase in early exit rates for affected consumers in proportion to the observed pattern since the freedoms came into force. It is also feasible that a cap on early exit charges could prompt policy holders – who would otherwise have waited until the charge fell to a level they considered acceptable – to take more immediate advantage of the pension freedoms.[24]

3.16 Our analysis suggests that a cap on early exit charges would result in increased numbers of eligible consumers accessing the freedoms in the four years after the imposition of the cap, 2017-2020 inclusive ('relevant period'). We consider the impact of a cap on exit charges on those consumers whose policies include an exit charge and would therefore potentially be affected by a cap (our estimate of this 'relevant population' is just over 747,000 policies). Diagram 3.1 shows the estimated number of early exits from the relevant population that we expect to occur with and without a cap in place.

Chart 3.1: Number of early exits on policies with exit charges over 2017-2020 at different cap levels



22 On the basis of the data provided by firms.

23 The assumption was consistent with the views of many providers, but not all. We performed sensitivity analysis on the results to examine the effect of varying the rate of early exit.

24 This is a theoretical benefit that we could not test against the historical data. Our analysis does not quantify this benefit or any resulting cost.

3.17 Table 3.1 shows our projections of the likely increase in early exits to access the freedoms over the relevant period if a cap were applied to early exit charges in existing contracts at 0%, 1%, 2% or 5% of policy value.

Table 3.1: Additional exits as a result of a cap on early exit charges

Cap (% of exiting member's policy value)	**0**	**1**	**2**	**5**
Estimated additional exits with a cap in place	43,102	37,397	6,632	3,281
Increase in exits (as a percentage of exits without the cap)	28.5%	24.7%	4.4%	2.2%

Impacts on firms

3.18 A small minority of provider firms do not currently impose exit charges on any of their existing pension contracts. While early exit charges are rare in post-RDR contracts, most provider firms have some existing contracts (typically referred to as legacy contracts) on which early exit fees are charged.

3.19 Some firms have recently announced plans to phase out or cap these charges, but only for workplace pensions. Our analysis of the financial impact on firms assumes that the level of charges applicable to all existing contracts remains unchanged from the dates of our data collection exercises. Where firms have voluntarily limited charges on existing personal and/or stakeholder pensions before our proposed rules come into force, the financial impact of complying is likely to be less than outlined in this paper (but our proposed cap for new contracts protects against the risk that, in the absence of a cap, these firms could choose to re-introduce or increase early exit charges in future).

Revenue losses

3.20 In respect of existing contracts, we calculate the revenue loss to firms as a result of two factors:

- the additional exits by consumers who would otherwise have continued to pay ongoing charges over some or all of the remaining life of the contract
- the transfer to consumers who would have exited anyway but who will now pay lower exit charges

3.21 For the additional exits, we have assumed that firms' uncapped early exit charges equal the amount of revenue that the firm would have recovered from the policy in respect of upfront costs had the policyholder stayed in the scheme until expected retirement date. This is consistent with firms' submissions that exit charges generally apply to old-style pre-RDR policies in which the charging structure was designed in order to recover up-front costs including adviser commission over the life of the policy. We treat the difference in the uncapped charge and the capped charge as a loss to the firm.[25]

3.22 For the transfer to customers who would exit without the cap, our calculation recognises that the firm will lose the difference between what it would charge them without a cap and the amount it can charge with the cap in place.

25 Exit charges are levied in order to recoup the unrecovered portion of the up-front costs in the event that the customer withdraws the funds earlier than selected retirement date.

3.23 We have estimated the lost revenue as a result of both these factors over a four-year period directly following the implementation of the cap. We used a discount factor to illustrate the present value of these revenue losses.[26]

3.24 We consider our assumptions are reasonable, but they nevertheless introduce a degree of uncertainty around our central estimates. The assumption with the highest impact and around which there is most uncertainty is the forward-looking exit rate. We have therefore assessed the sensitivity of the results by varying the base case exit rate.[27] The impact of the other modelling assumptions is not as great and we consider that our sensitivity analysis is sufficient to capture the likely range of results from varying these other assumptions.[28]

3.25 We have estimated the lost revenue as a result of these factors over a four-year period directly following the implementation of the cap. We recognise that costs could continue beyond this period for some firms. Where this is the case, firms may need to take this into account in their business planning. While we recognize that firms may also experience revenue losses in respect of other charges attached to these policies we consider these to be of only minimal significance.

Table 3.2: Impacts for the industry

	Cap level (% of exiting member's policy value)			
	0%	**1%**	**2%**	**5%**
Loss of revenue (£m) – base case	104	65	34	10
Loss of revenue (£m) – range	74-143	46-89	24-46	7-14
Implementation costs (£m)	17	17	17	14

Solvency impact

3.26 We assessed the potential solvency impact and likelihood of firm exit by comparing the revenue impacts on firms with an estimate of the capital that firms hold over and above the regulatory minimum. This gave us a measure of their ability to absorb the likely revenue loss resulting from a cap while remaining solvent. Based on this analysis, we do not expect a cap of 1% to materially affect the financial status of affected firms or significantly compromise their solvency.

Compliance costs

3.27 These are the costs of implementation firms have told us may arise from updating literature and communication documents, training operational and contact centre staff, and preparing questions and answers for client-facing departments. Other costs include introducing changes to policy administration software systems, and updating internal model valuation and projections.

26 We assumed annual real fund growth rate of 5% and an estimate of firms' weighted average real pre-tax cost of capital of 10%.

27 Our base case estimate of average early exit rates is 6.3% per year. Our sensitivity analysis considers the impact of varying this base case between 4.4% and 8.8% per year, i.e. a range of -30% to +40%.

28 In general, we consider that we have taken a cautious approach to the modelling which may tend to overstate revenue losses to firms rather than understate them.

Table 3.3: Implementation costs

	Cap level (% of exiting member's policy value)			
	0%	1%	2%	5%
Implementation costs (£m)	17	17	17	14

Competition impacts

Existing contracts

3.28 The effects of the cap will not be felt uniformly across the market. These will vary according to the numbers of policies on firms' books that feature early exit charges. While some provider firms will experience a negligible loss (or no loss, if they do not levy exit charges on any contracts), others could experience a more significant monetary loss (in these cases, our analysis suggests that the sums in question are unlikely to be significant enough to result in market exit).

3.29 This non-uniformity is an important feature, as it implies that providers will find it difficult to recover losses through price rises (since, if they did so, other firms with lower costs may undercut and win business). This may be regarded as a positive competition effect.

3.30 While we do not consider it very likely that firms will make general price rises to compensate for a cap, responses to the measure are inherently hard to predict.

New contracts

3.31 We do not expect a cap to reduce the scope for innovation in new products as most firms told us that early exit charges are not a feature of new policies in the current product and distribution landscape (and are rare in policies sold since we implemented the Retail Distribution Review).

3.32 This suggests that few providers would:

- introduce exit charges on new policies
- increase charges up to the level of the cap on existing policies that do not currently include them

3.33 But it also suggests we can fully protect consumers from the introduction of charges they would not otherwise incur and which could act as a deterrent from accessing the freedoms, with little financial impact on most firms, by introducing a cap of 0% on contracts entered into after our proposed rules come into effect.

Our proposals

3.34 Firms told us that, in the vast majority of cases, the exit charge is related to the value of the policy, rather than a fixed cost. We therefore propose to introduce caps on early exit charges expressed as a percentage of the member's policy value at exit.

3.35 Furthermore, given that individual policy values vary greatly, we believe a cap expressed in these terms would deliver more consistent levels of protection against the deterrent effect of early exit charges than a cap expressed as (or by reference to) a single monetary amount.

Cap level

Existing personal and stakeholder pension contracts

3.36 After considering alternatives, we propose a cap at 1% of a member's policy value at exit. Where existing contracts have early exit penalties set at less than 1% of the member's policy value our proposed cap will prevent these being raised.

3.37 A cap at 0% would not materially increase the benefit (number of additional exits), but the impact on firms would be significantly greater, while a cap at 2% would offer significantly less protection from the deterrent effect of the charge.

3.38 Our analysis concludes that a cap at 1% strikes an appropriate balance between:

- ensuring that these charges do not act as a deterrent to consumers accessing the pension freedoms
- recognising that a significant proportion of legacy contracts will have some up-front sale and advice costs left unrecovered if the consumer withdraws their funds before their expected retirement / vesting date

New personal and stakeholder pension contracts

3.39 We propose to cap early exit charges at 0% of existing member's policy value in new contracts entered into after our rules come into force.

3.40 Data we collected from providers reveal that exit charges are not a feature of the vast majority of existing personal and stakeholder pension contracts.[29] Most providers told us that the driver for early exit charges (as defined in the legislation) existed only for older policies (where they were designed specifically to recover outstanding up-front sale and advice costs).

3.41 There is no such justification for early exit charges in the post-RDR adviser and product landscape. So we believe that a 0% cap for new personal and stakeholder pension contracts entered into after our rules come into effect will protect consumers from the emergence of early exit charges that could act as a deterrent on accessing the freedoms.

Q2: Do you agree with our methodology?

Q3: Do you agree that a cap of 1% on early exit charges in existing pension contracts is appropriate? If not, do you consider that a cap at a different level, or applied in a different manner, would be more appropriate (and, if so, why)?

Q4: Do you agree that a cap of 0% on early exit charges in new pension contracts is appropriate? If not, do you consider that a cap at a different level, or applied in a different manner, would be more appropriate (and, if so, why)?

Q5: Would our proposals have any other implications on pension providers or on consumers that we have not considered in our analysis?

29 84% of policies held by eligible consumers as at 30 June 2015 were not exposed to an early exit charge.

Annex 1
Cost benefit analysis

Introduction

1. Section 138I of the Financial Services and Markets Act 2000 (FSMA) requires us to publish a cost benefit analysis (CBA). A CBA requires an analysis of the costs together with an analysis of the benefits that will arise if the proposed rules are made, and (unless in the opinion of the FCA either the costs or benefits cannot reasonably be estimated or it is not reasonably practicable to produce an estimate[30]) an estimate of those costs and benefits.

2. Under section 138L(3) there is an exemption from the requirement to produce a CBA if we consider that, making the appropriate comparison, there will be no increase in costs resulting from our proposals or that there will be an increase in costs but that increase will be of minimal significance.

3. Our CBA focuses on how the proposals in Chapter 3 directly affect firms, consumers and competition in the market, but also illustrates the impacts of alternatives we considered. The Government has concluded that, in the context of pension reforms, action needs to be taken to prohibit specified early exit charges and Parliament has legislated to place a duty on the FCA to prohibit specified early exit charges. This means we do not have any discretion as to whether or not to create a cap, only over the details of exactly how we do so.

4. Our analysis presents estimates of the significant impacts of our proposals for a cap on early exit charges in existing contracts. We provide monetary estimates of these where we believe it is reasonably practicable to do so, and provide estimates of outcomes in other dimensions where it is not. In the latter cases it is not always possible to then convert these estimates into monetary values. So our proposals are based on a careful weighing up of the monetary and non-monetary dimensions to reach a judgement on the appropriate level of consumer protection.

5. Under s138L(3) FSMA, we do not consider it necessary to carry out a cost benefit analysis in respect of:

   i. Our proposals to cap early exit charges at 0% in new contracts established after our rules take effect. Even though the vast majority of providers do not currently include early exit charges on new policies, we cannot rule out the possibility that policies with early exit charges may feature in some firms' forward looking business models. We have considered the potential for these firms to incur costs as a result of the cap and have concluded that such costs will be of minimal significance.

30 In these cases slightly different requirements apply.

ii. Our proposal that – where existing contracts have early exit penalties set at less than 1% of the member's policy value - our proposed cap will prevent these being raised. We consider that this proposal imposes no costs on firms as it simply prevents them from doing something they are not currently doing.

Market overview

6. The pension freedoms came into effect in April 2015 and gave those aged 55 and over the ability to access their retirement savings flexibly.

7. However, after the freedoms took effect, the Government became aware that some consumers were facing a range of potential barriers when seeking to access their pension savings under the new freedoms – including early exit charges.

8. In response to these issues, the Government launched a consultation in July 2015.[31] The consultation ran for 12 weeks and ran in parallel with data-gathering exercises conducted by the FCA and TPR.

9. The firm population for our data-gathering exercise was determined by selecting all those firms that held FCA permissions for establishing, operating or winding up a personal pension scheme (which includes the vast majority of the firms that hold permissions for establishing, operating or winding up a stakeholder pension). The time period covered by our data request was 6 April to 30 June 2015 – the three months following the introduction of the pension freedoms.

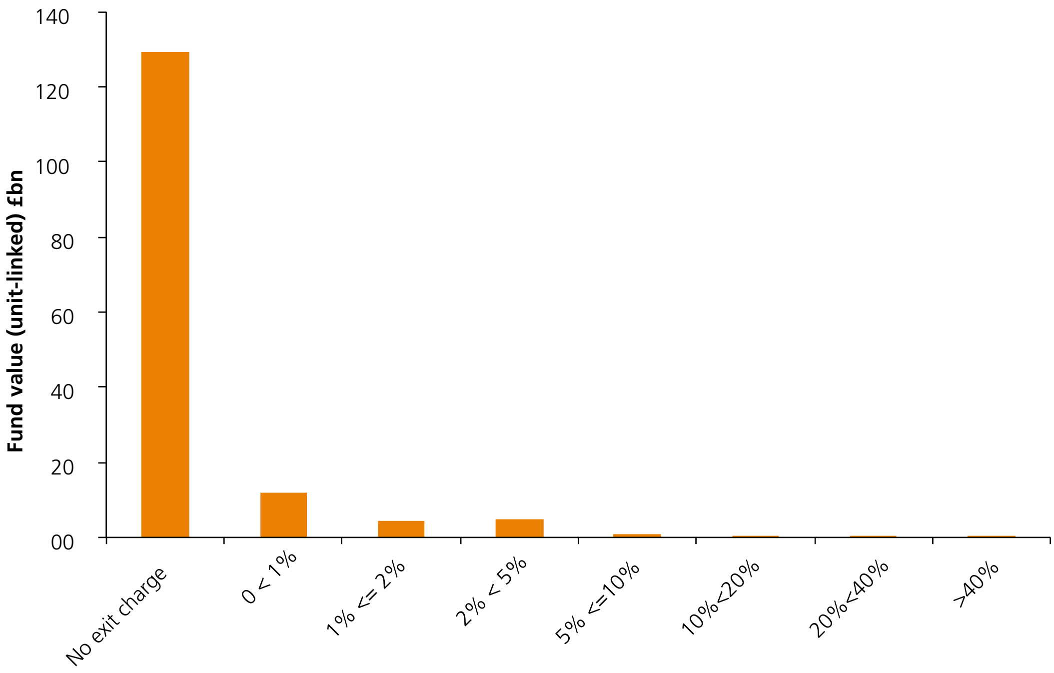
10. We received 116 responses. Firms responding to the survey consisted of three main groups:

- life insurers
- investment companies
- SIPP operators

The following diagram represents a snapshot of the exit charge position across the firms' personal pension contracts eligible to access the pension freedoms as of 30 June 2015:

31 www.gov.uk/government/uploads/system/uploads/attachment_data/file/449861/PU1847_Pensions_transfers_v4.pdf

Chart A1.1: Eligible policies by exit charge band (30 June 2015)



11. The data we received from firms indicates that 84% of contracts are not subject to early exit charges. Those contracts that are subject to exit charges tend to be those sold before the RDR came into effect [32] – sometimes referred to as legacy policies.

Data from firms

12. We sought data on the level and scope of early exit charges by issuing a data request to a representative sample of provider firms. We arrived at this sample by referring to the recipients of our July 2015 data-gathering request[33] and excluding those life insurers and investment companies that:

- positively indicated in response to the July request that they do not levy exit penalties
- those firms whose book was likely to be too small to yield useful data

13. We, separately, contacted a representative sample of SIPP operators, asking more focused questions, relevant to their product offerings.

14. The data we received back indicates that early exit rates are affected by the level of early exit charges levied. It enabled us to model the likely impacts of different levels of exit charge cap on exit rates and the consequential impact on firms, consumers and competition, providing the basis for our CBA.

32 31 December 2012 in relation to rules concerning commission.
33 www.fca.org.uk/static/documents/pension-freedoms-data-collection-exercise.pdf

15. We recognise there are some inherent limitations on the data we have used, not only as a result of firms using different assumptions when responding to our data request but most particularly as we have only six months of exit data under the pension freedoms. We have accepted this data at face value and made conservative assumptions when modelling and projecting, as outlined below.

Our analytical approach

16. Our starting point is that benefits arise from an increase in the number of policyholders that, as a result of the cap, access their pension freedoms in the relevant period.

17. We adopted a modelling approach to understand the impact of an exit charge cap on consumers, firms, and on competition.

18. We considered the impact of exit charges on willingness to take early exit by examining historical data on the rate at which consumers have exited early since the pension freedoms became available in April 2015 according to the level of exit charges.

19. We aim to implement the cap by March 2017. As the contracts on which exit charges are levied were generally written in the 1980s and 1990s it is likely that many of these polices will reach their selected retirement ages by 2020, at which point they will no longer face early exit charges.

20. For this reason and because projections of consumer behaviour beyond this date are likely to become progressively less reliable,[34] we have based our assessment on the relevant policies qualifying for the pension freedoms between the calendar years[35] 2017 and 2020.

21. Our proposals will inevitably have some continuing impact where the expected retirement date / vesting date of some of these existing policies is set beyond 2020. We recognise that revenue losses beyond this period have the potential to be significant for some firms given the long term nature of pension contracts. While in some cases firms may need to make immediate adjustments to reflect the longer term impact, the longer time frame may afford others adequate time in which to make necessary adjustments.

Modelling assumptions

Exit rates

22. For each exit charge band, firms experienced different exit rates over the period. We weighted the firm-specific exit rates within each exit charge band according to the number of contracts in that exit charge band. This produces an industry average exit rate for each exit charge band, weighted by number of contracts.

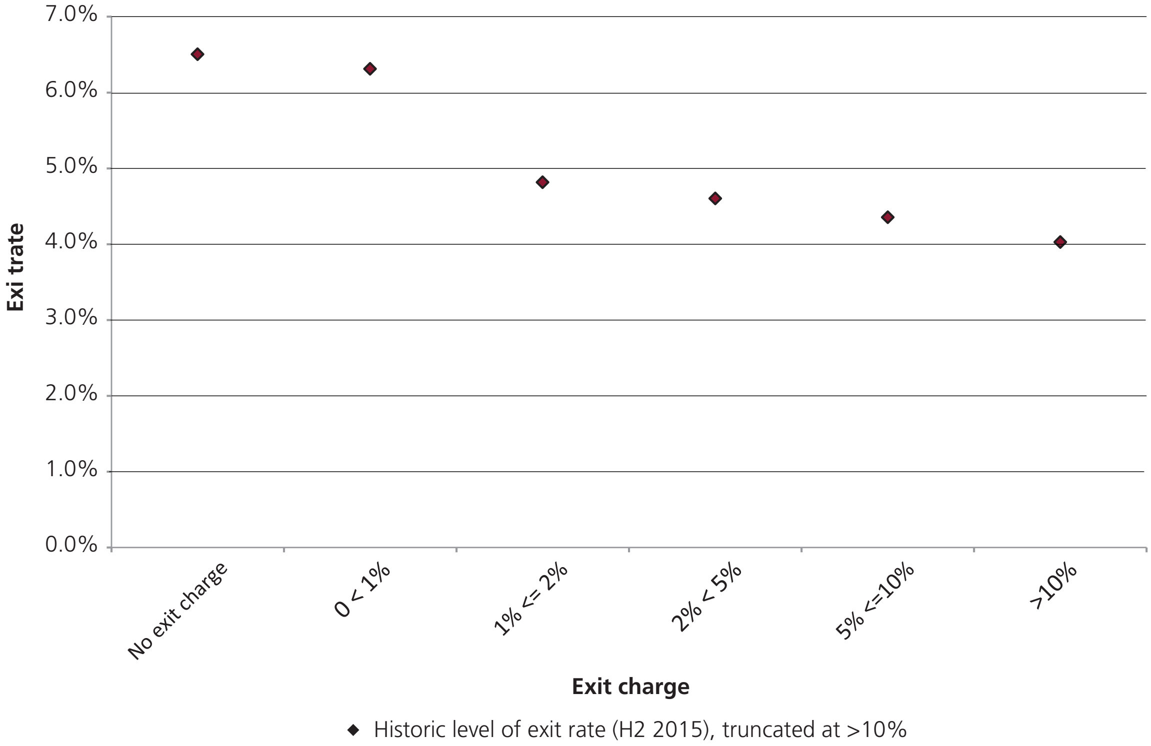
23. These industry averages present a picture of the relationship between exit rates and exit charges in the period following the introduction of the pension freedoms.

24. Exit rates during the second half of 2015 (actual exit rates) indicate that people were less likely to access their funds early where significant exit charges were applied.

34 Given the adjustments that firms are likely to make in response to the cap when it comes into force.

35 For simplicity we have assessed the impact over the four year period starting 1 January 2017, rather than from the target implementation date. We would not expect this difference in start date to have a material impact on the outcomes of our analysis.

Chart A1.2: Actual rates of exit by early exit charge level (second half 2015)



25. Importantly, we have assumed that the average rate of exit of 6.3% in the second half of 2015 was abnormally high due to pent-up demand and the publicity surrounding the introduction of the pension freedoms on 6 April 2015, effectively double the exit rate that we expect to persist. As a result we estimate exit rates of 6.3% *a year* on average during the period 2017-20, assuming no cap were imposed.

26. This was consistent with most answers respondents provided to the data collection and to some follow-up questions on the expected average exit rate.

27. Our assumption is also consistent with data from the latest instalment of the Retirement Income Data Collection exercise. During the third quarter of 2015, 178,990 pensions were accessed by consumers to take an income or fully withdraw their money as cash. During the fourth quarter of 2015, 127,094 pensions were accessed by consumers, to take either an income or withdraw money as cash, i.e. a 36% decrease from the previous quarter's figures.

Impact on consumers

28. In giving us the duty, Parliament set us the specific objective to secure an appropriate degree of protection against early exit charges being a deterrent to consumers accessing the pension freedoms. We consider it is therefore appropriate to focus on the relationship between early exit charges and exit rates in order to estimate the extent to which the early exit charge has a deterrent effect, rather than modelling all of the factors that affect consumers' decisions to access the pension freedoms.

29. The proposed 1% cap on existing contracts will meet the objective by enabling a significant number of additional consumers (from age 55) to access their pensions earlier than they would otherwise have done. The following chart and table illustrate our estimates of additional early exit when a cap is set at 0%, 1% 2%, 5% and 10% of an exiting member's policy value. Our estimates are based on a range of assumptions and unavoidably have wide margins of error.

Chart A1.3: Additional numbers of early exits due to cap (2017-2020)

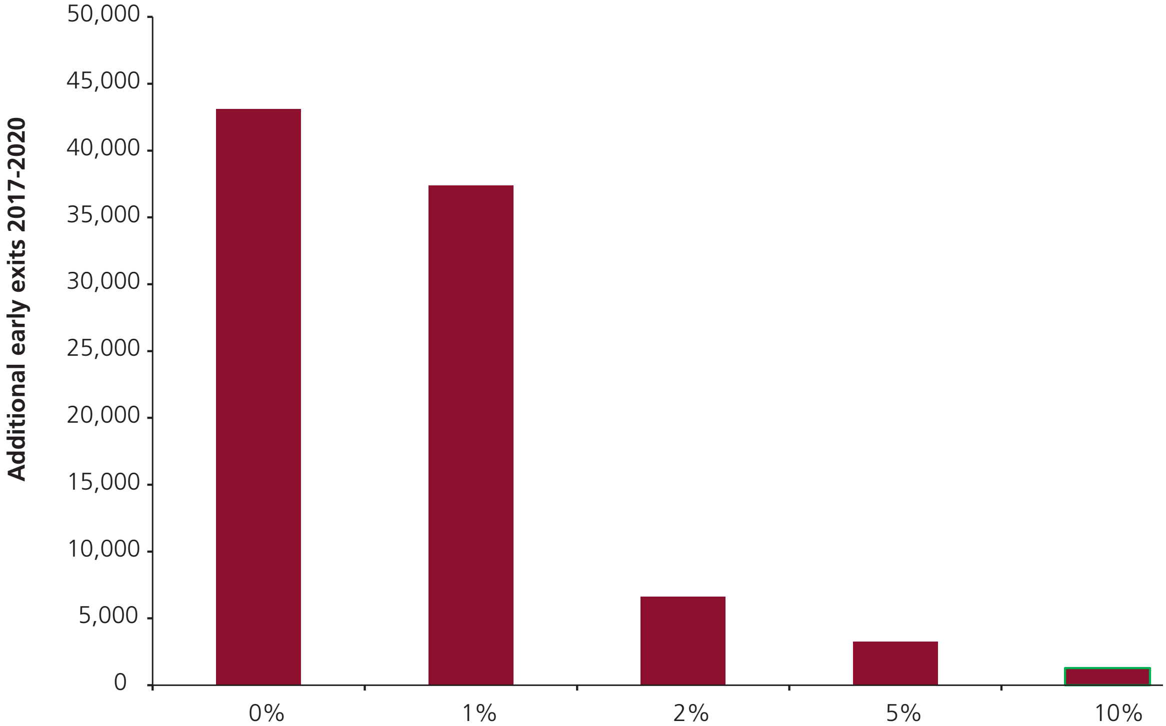


Table A1.1: additional exits (2017-2020) at different cap levels

	Cap level (% of exiting member's policy value)				
	0%	**1%**	**2%**	**5%**	**10 %**
Additional exits (000s)	43	37	7	3	1

30. As noted above, we have not modelled all of the factors that affect consumers' decisions to access the pension freedoms. Some of the additional consumers who exit as a result of the cap may be subject to certain behavioural biases. As these could influence whether or not consumers will experience a monetary benefit from accessing their pensions saving early, we do not consider it is feasible to calculate a reasonably accurate estimate of the monetary value of any consumer surplus associated with additional exits.

Impact on firms

31. We have taken into account three types of impacts on firms:

    i. The revenue loss to firms as a result of the cap

    ii. Compliance costs

    iii. Solvency impacts

Revenue loss

32. Given the range of different charging structures and approaches, not all firms would be exposed to losses as a result of a cap on early exit charges for existing contracts.

33. The two principal drivers of potential revenue loss for those firms that will be affected by the cap are:

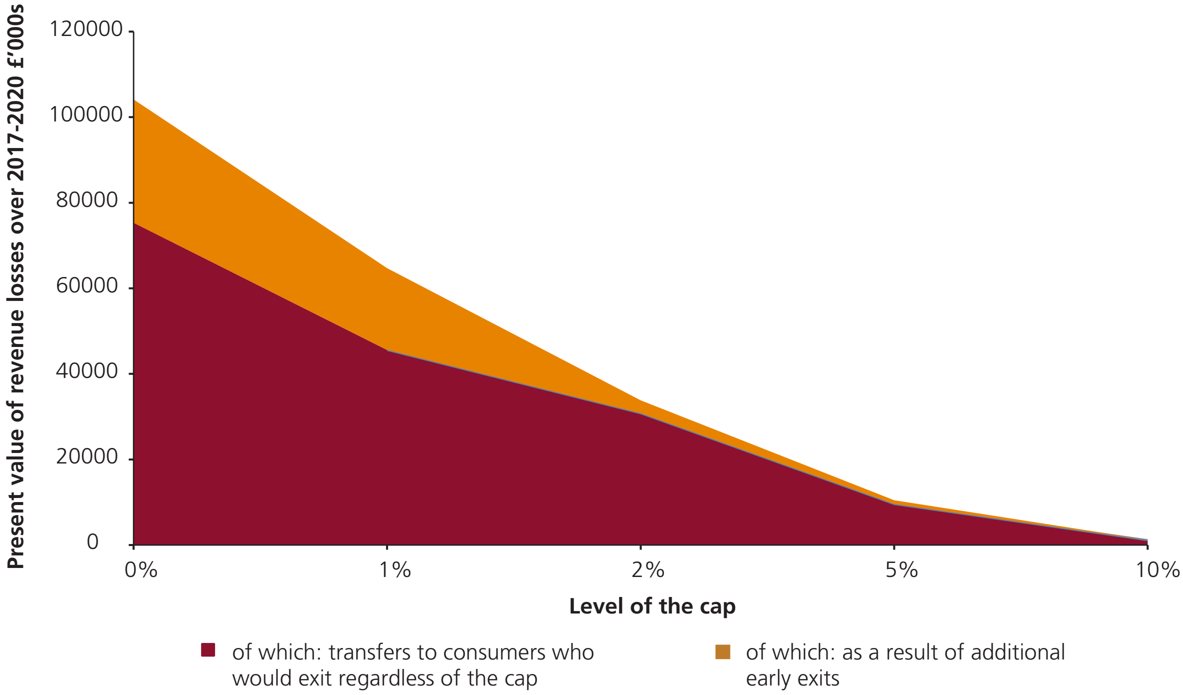
    - the number of additional customers that exit early/earlier when a cap applied
    - lower charges for those who would exit in the absence of a cap (this loss represents a transfer to customers who would exit early anyway)

34. We have estimated the lost revenue as a result of both these factors over a four-year period immediately following the implementation of the cap. While we recognize that firms may also experience revenue losses in respect of other charges attached to these policies we have not attempted to estimate these as we consider them to be of only minimal significance. We used a discount factor to illustrate the present value of these revenue losses.

35. Our estimates are shown in Chart A1.4 and our underlying assumptions are discussed in paragraphs 3.20 to 3.25. They do not take into account, however, the extent to which such losses might be offset by:

    - additional revenues generated by customers who, in accessing the pension freedoms, enter into a new contract with the same firm or another firm
    - how firms respond to the cap

Chart A1.4: Revenue losses during 2017/20 (by source) for different cap levels



Compliance costs

36. Our data request asked provider firms what implementation and compliance costs they may incur to comply with rules capping early exit charges at different levels.

Table A1.2: compliance costs

	Cap level (% of exiting member's policy value)			
	0%	1%	2%	5%
Implementation costs (£m)	17.4	17.4	17.4	14.3

37. While some firms told us the implementation costs would depend on the level and structure of the cap, firms told us that costs could arise from updating literature and communication documents, training operational and contact centre staff, and preparing questions and answers for client-facing departments. Other costs include introducing changes to policy administration software systems, and updating internal model valuation and projections.

Solvency impact

38. We have formed a view on the solvency impact and likelihood of firm exit by comparing the revenue impacts on firms with an estimate of the capital that the firms hold over and above the regulatory minimum. This gives us a measure of their ability to absorb the likely revenue loss while remaining solvent. Based on this analysis, we do not expect a cap of 1% to materially affect the financial status of affected firms or significantly compromise their solvency.

Early exit charges in new contracts

39. In reliance on section 138L(3)(b), we do not consider it necessary to carry out a cost benefit analysis in respect of our proposals to cap early exit charges at 0% in new contracts established after our rules come into force.

40. Data we collected from providers reveal that exit charges are not a feature of the vast majority of existing personal and stakeholder pension schemes.[36] Furthermore, firms told us that, since the implementation of the RDR, there is no longer a strong justification for early exit charges which were originally designed to recover initial commission costs that would otherwise have been recovered over the remaining life of the policy. Consequently, early exit charges are rare in policies marketed today. Capping them at 0% in new contracts should not give rise, therefore, to significant additional costs for firms.

41. We recognise there are many different charges that it is necessary for firms to impose on scheme members while providing and servicing these contracts. If firms currently anticipate including early exit charges in new contracts:

- our proposals do not rule out other efficient means of recovering reasonable costs
- consulting on these rules allows firms time to revise their approach

42. We cannot rule out that firms may experience costs if they operate less efficient charging structures but we consider that any such cost would be of minimal significance.

Q6: Do you agree that we have identified all the relevant costs and benefits?

Q7: Do you think the benefits to consumers, or the costs to firms, should be assessed in some other way (and, if so, how)?

Q8: Do you have any comments on the data we have used in completing our cost benefit analysis?

Q9: Do you think our analysis considers an appropriate range of cap levels?

Q10: Do you have any comments on our analysis of the data?

Q11: Do you consider we have omitted any significant points or issues?

36 84% of policies held by eligible consumers as at 30 June 2015 were not exposed to an early exit charge.

Annex 2
List of questions

Q1: Do you have any comments about the impact of our proposals on equality and diversity?

Q2: Do you agree with our methodology?

Q3: Do you agree that a cap of 1% on early exit charges in existing pension contracts is appropriate? If not, do you consider that a cap at a different level, or applied in a different manner, would be more appropriate (and, if so, why)?

Q4: Do you agree that a cap of 0% on early exit charges in new pension contracts is appropriate? If not, do you consider that a cap at a different level, or applied in a different manner, would be more appropriate (and, if so, why)?

Q5: Would our proposals have any other implications on pension providers or on consumers that we have not considered in our analysis?

Q6: Do you agree that we have identified all the relevant costs and benefits?

Q7: Do you think the benefits to consumers, or the costs to firms, should be assessed in some other way (and, if so, how)?

Q8: Do you have any comments on the data we have used in completing our cost benefit analysis?

Q9: Do you think our analysis considers an appropriate range of cap levels?

Q10: Do you have any comments on our analysis of the data?

Q11: Do you consider we have omitted any significant points or issues?

Annex 3
Compatibility statement

Compatibility with the FCA's general duties

1. We are required by section 138I(2)(d) of FSMA to explain why we believe the making of our proposed rules is compatible with our duties under section 1B(1) and (5)(a), namely to act so far as reasonably possible in a way which is compatible with our strategic objective, advances one or more of our operational objectives, and has regard to the regulatory principles in section 3B of FSMA. We are also required by section 138K(2) of FSMA to state whether the proposed rules will have a significantly different impact on mutual societies, as opposed to other authorised persons.

2. This annex also sets out our view of how the proposed rules are compatible with the duty on the FCA to discharge its general functions (which include rule-making) in a way that promotes effective competition in the interests of consumers (section 1B(4) of FSMA). This duty applies in so far as promoting such competition is compatible with advancing our consumer protection and/or integrity objectives.

3. This annex must be read in conjunction with the rest of the consultation paper and the cost benefit analysis (in Annex 1) in demonstrating that we meet our statutory duties and objectives.

Our objectives

4. The proposals set out in this Consultation Paper are intended to discharge our new duty in s.137FBB FSMA to make general rules which prohibit the imposition (and provision for the imposition) of specified early exit charges 'with a view to securing, so far as is reasonably possible, an appropriate degree of protection for members of relevant pension schemes against early exit charges being a deterrent on' accessing the pension freedoms.

5. In carrying out this duty, we must advance at least one of our operational objectives and meet the requirements of our competition duty. We consider that imposing a cap on early exit charges in personal and stakeholder pension schemes is compatible with the strategic objective of ensuring that relevant markets[37] function well, since it increases consumer choice and flexibility, supporting the legislative reforms which enable consumers to take their pension in different ways and at different times. Furthermore, we consider that our proposal advances our consumer protection objective. We view the new duty in s.137FBB FSMA as describing the detriment against which we must secure an appropriate degree of protection when making rules to further the consumer protection objective in s.1C FSMA.

37 Defined by s.1F FSMA.

6. To demonstrate that we have met our statutory duty and operational objective, we have considered the relationship between early exit charges and exit levels in order to show the extent to which the early exit charge has deterrent effect. We have also considered a number of costs which arise out of the imposition of a cap, and balanced these against the aim of securing an appropriate degree of protection against early exit charges being a deterrent to accessing pension freedoms, to arrive at a cap which we believe is appropriate.

Advancing the consumer protection objective

7. In designing the proposals we have had regard to the matters set out in section 1C FSMA in determining what degree of protection for consumers is 'appropriate', to the extent that considering these factors is relevant and compatible with the more specific duty imposed on us by section 137FBB FSMA. In particular, and as outlined below, we have considered how our proposals relate to the general principle that consumers should take responsibility for their decisions. we have also considered the possible differing expectations of consumers and consider that over the duration of these long-term investments, consumers' expectations are likely to have changed regarding the amount of (and access to) their pension funds. In particular we note that:

- consumers who entered into their pension contracts before 2015 will not have envisaged when they took out the contract that they might be able to take advantage of the pension freedoms which came into force in April 2015
- tax changes over recent years to pension contribution relief have altered the pensions landscape for some consumers

8. Against this backdrop, we view it as particularly important that a cap on early exit charges provides appropriate protection against such charges deterring consumers from taking, converting or transferring benefits where they wish to exercise the freedom and choice to do so.

Compatibility with the FCA's regulatory principles

9. In preparing the proposals set out in this consultation, we have had regard to the regulatory principles set out in section 3B of FSMA.

The need to use our resources in the most efficient and economical way

10. We have a duty to introduce a cap on early exit charges to secure an appropriate degree of protection. In developing the proposals for a cap, we have designed a methodology that has given us an appropriate evidence base, and we have undertaken a thorough analysis of the impact on firms and consumers.

11. We do not expect our proposals to have material implications for our resource requirements as we propose that industry implementation and compliance can be monitored and enforced through our existing risk-based supervision approach.

The principle that a burden or restriction should be proportionate to the benefits

12. In deciding on the level and the application of the cap, we have taken account of the need to be proportionate. We have considered the benefits in terms of the number of consumers who will exit their pension schemes earlier than they otherwise would have done. Against this benefit, we have considered the different costs that will arise for firms, and the competition implications. We have considered alternative options both as to the level of the cap and as to different ways of applying it. However, following comprehensive analysis, we have concluded that no alternative options for the level or application of the cap would deliver an appropriate degree of protection for consumers.

13. We believe that any additional costs to provider firms of complying with the charge caps are justified by, and proportionate to, the level of protection they offer consumers against the deterrent effect of early exit charges.

14. The cost benefit analysis in Annex 1 sets out these costs in more detail.

The desirability of sustainable growth in the UK economy in the medium or long term

15. Our proposals support the Government's stated policy objective of ensuring that consumers can access their pension savings flexibly.[38] We do not expect our proposals to have a negative impact on growth in the UK.

The general principle that consumers should take responsibility for their decisions

16. Where early exit charges apply in existing contracts, it is likely that the majority of these agreements were entered into before the conception of 'flexible' pensions. The Government has concluded that, in the context of pension reforms, action needs to be taken to prohibit specified early exit charges. So we believe our proposal on existing contracts is appropriate despite the decision consumers will have made to enter a contract with their uncapped exit charges.

17. The freedoms present consumers with many choices about how and when to access their pension savings. Our proposals reflect the principle that consumers should take responsibility for their decisions: our evidence suggests that, at present, consumers are deterred from exercising their choice to exit or transfer benefits by the existence of an early exit charge. .

The responsibilities of senior management

18. Our proposals create new rules and the senior management of provider firms are obliged to ensure compliance with the rules through existing regulatory requirements as to oversight and compliance. We believe that these obligations are appropriate and proportionate to comply with the duty in s.137FBB FSMA.

The desirability where appropriate of exercising our functions in a way that recognises differences in the nature and objectives of businesses carried on by different persons

19. In developing our proposals, we have had regard to the significant variation (between firms, between schemes and over time) in providers' charging structures. We have considered separately the appropriate cap level for existing contracts and contracts entered into in future. We have taken into account that the financial impact will not be felt uniformly across providers, but believe that a cap which applies to all relevant providers is proportionate in light of the protection which will be secured for consumers in this instance.

The desirability in appropriate cases of publishing information relating to persons on whom requirements are imposed

20. We not believe that our proposals affect or undermine this principle.

38 The Government's response to the 'Freedom and Choice in Pensions' consultation, published in July 2014.

The principle that we should exercise our functions as transparently as possible

21. In making our proposals as to the appropriate level of the cap to deliver our statutory duty, we have drawn heavily on data collected from firms.[39] This paper and the CBA it contains expose how we used this data and the conclusions we have drawn from it. We believe that by consulting on our proposals and CBA we are acting in accordance with this principle.

Compatibility with the duty to promote effective competition in the interests of consumers

22. In preparing the proposals in this Consultation Paper, we consider we have met our duty under section 1B(4) FSMA. This provides that we must, so far as is compatible with acting in a way that advances the consumer protection objective or the integrity objective, carry out our general functions in a way that promotes effective competition in the interests of consumers.

23. We have already set out that we are taking action which we believe advances the consumer protection objective. We recognise that the caps will likely lead to the creation of new market dynamics. Though we cannot predict how firms will change and adapt in response to our proposals we have considered the potential competition implications arising from the introduction of the caps.

24. In respect of existing contracts, the effects of the cap will not be felt uniformly across the market: not all pension providers apply early exit charges and for those that do, the scale of revenue impact from a cap at 1% of an exiting members' policy value(s) will depend on the numbers of policies on their books that include early exit charges. However, our analysis suggests that the sums in question are unlikely to be significant enough to result in market exit.

25. We think the likelihood of price rises to compensate for a cap on exit charges in existing contracts is low given the non-uniformity of revenue impacts. In a landscape where such charges are currently uncommon, the cap on charges in new contracts prevents the emergence of early exit charges in future with little financial impact for most firms.

26. Both caps could drive more effective competition in the market for decumulation products as firms seek to benefit from a potential redistribution of customers who access their pension savings following the cap (both within and between firms).

27. We do not believe we could secure the same level of protection for consumers as will result from a cap of existing contracts at 1% and a cap of new contracts at 0% in a manner which is more pro-competitive.

28. Our cost benefit analysis further explains the effects we expect to see on competition as a result of our proposals.

39 FCA pension freedoms data collection exercise (July 2015), FCA Early exit charges data collection (February 2016 - April 2016), FCA Quarterly Income data collection.

Expected effect on mutual societies

29. Section 138K of FSMA requires us to state whether, in our opinion, our proposed rules have a significantly different impact on authorised persons who are mutual societies, in comparison with other authorised persons.

30. We do not expect the proposals in this paper to have a significantly different impact on mutual societies than other authorised persons or present them with any more or less of a burden than other authorised persons.

31. We would welcome any comments or information you have on any issues relating to mutual societies that you believe would arise from our proposals.

Appendix 1
Draft Handbook text

PENSION SCHEMES (RESTRICTIONS ON EARLY EXIT CHARGES) INSTRUMENT 2016

Powers exercised

A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (The FCA's general rules);
(2) section 137FBB (FCA general rules: early exit pension charges);
(3) section 137T (General supplementary powers); and
(4) section 139A (Power of the FCA to give guidance).

B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on [31 March 2017].

Amendments to the Handbook

D. The Glossary of definitions is amended in accordance with Annex A to this instrument.

E. The Conduct of Business sourcebook (COBS) is amended in accordance with Annex B to this instrument.

Citation

F. This instrument may be cited as the Pension Schemes (Restrictions on Early Exit Charges) Instrument 2016.

By order of the Board
[*date*]

Annex A

Amendments to the Glossary of definitions

Insert the following new definition in the appropriate alphabetical place. The text is not underlined.

early exit charge has the meaning given in section 137FBB(6) of the *Act*, which is, in summary:

(a) a charge imposed on a member of a *personal pension scheme* or *stakeholder pension scheme*:

(i) when that member, having reached normal minimum pension age, takes the action set out in (b), but

(ii) is only imposed, or only imposed to that extent, if the member takes that action before the member's expected retirement date;

(b) the action is the member taking benefits, converting benefits into different benefits or transferring benefits to another pension scheme;

(c) in this definition:

(i) a reference to "benefits" includes all or any part of those benefits;

(ii) "charge" includes a reduction in the value of the member's benefits under the scheme;

(iii) "expected retirement date" means the date determined by or in accordance with the scheme as the date on which the member's benefits under the scheme are expected to be taken;

(iv) "normal minimum pension age" has the meaning given in section 279(1) of the Finance Act 2004, which is, in summary, and in relation to dates on and after 6 April 2010, 55.

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

After COBS 19.6 insert the following new section. The text is not underlined.

19.6A Restrictions on early exit charges in personal pension schemes and stakeholder pension schemes

Application

19.6A.1 R This section applies to an *operator* of a *personal pension scheme* or a *stakeholder pension scheme*.

Purpose

19.6A.2 G The purpose of this section is to make *rules* prohibiting the imposition of, and provision for, certain *early exit charges* on members of *personal pension schemes* and *stakeholder pensions schemes*. Section 137FBB of the *Act* requires the *FCA* to make such *rules*.

Exclusion

19.6A.3 R This section does not apply to any charge which is excluded from the scope of section 137FBB of the *Act* by the Financial Services and Markets Act 2000 (Exclusions to early exit pensions charges) Regulations 2016.

Prohibition on early exit charges on a member joining a scheme on or after [31 March 2017]

19.6A.4 R (1) A *firm* must not:

(a) impose; or

(b) include in the arrangements relating to a *personal pension scheme* or *stakeholder pension scheme* any provision for the imposition of:

an *early exit charge* on a member of the scheme.

(2) This *rule* applies in relation to a member who entered into a contract or other arrangement (providing for a right to benefits resulting from contributions to the scheme) on or after [31 March 2017].

Restriction on early exit charges on a member who joined a scheme before [31 March 2017]

19.6A.5 R (1) A *firm* must not impose an *early exit charge* on a member of a *personal pension scheme* or *stakeholder pension scheme* that exceeds the lower of:

(a) 1% of the value of the member's accrued rights under the scheme; or

(b) such lower amount as was provided for under the scheme arrangements as at [31 March 2017]; or

(c) where no such provision was made, no charge.

(2) A *firm* must not:

(a) include provision in such a scheme for an *early exit charge*, where such provision did not exist on [31 March 2017]; or

(b) vary provision for an *early exit charge* in such a scheme so as to increase or potentially increase the charge.

(3) The value of the member's accrued rights in (1)(a) is calculated at the point when the *firm* receives confirmation from the member of the instruction to take the action giving rise to the *early exit charge*.

(4) This *rule* applies in relation to a member who entered into a contract or other arrangement (providing for a right to benefits resulting from contributions to the scheme) before [31 March 2017].

Amend the following as shown. Underlining indicates new text and striking through indicates deleted text.

COBS TP 2 Other Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
…					
<u>2.25</u>	<u>*COBS* 19.6A.5R</u>	<u>R</u>	<u>*COBS* 19.6A.5R does not apply where the instruction for the action giving rise to the *early exit charge* was received by the *firm* before [31 March 2017].</u>	<u>From [31 March 2017] indefinitely</u>	<u>[31 March 2017]</u>

Financial Conduct Authority

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