Consultation Paper

CP12/29**

Financial Services Authority

Personal pensions

– feedback to CP12/5 and final rules on disclosures by SIPP operators, and consultation on inflation-adjusted illustrations

November 2012

Financial Services Authority

Contents

This Consultation Paper reports on the issues arising from Chapter 5 of Consultation Paper 12/5 *(Quarterly Consultation)* and publishes final rules on disclosure requirements for SIPP operators. It also consults on proposals for inflation-adjusted illustrations for personal pensions. Comments on Chapters 3 and 4 should reach us by 1 February 2013.

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Comments on Chapters 3 and 4 may be sent by electronic submission using the form on the FSA website at: www.fsa.gov.uk/Pages/Library/Policy/CP/2012/cp12-29_response.shtml.

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A confidential response may be requested from us 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 Tribunal.

Copies of this Consultation Paper are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

Abbreviations used in this paper

COBS	Conduct of Business sourcebook
CP	Consultation Paper
FRC	Financial Reporting Council
FSMA	Financial Services and Markets Act 2000 (as amended)
KFI	Key Features Illustration
RDR	Retail Distribution Review
SIPP	Self-Invested Personal Pension
SMPI	Statutory Money Purchase Illustration

1 Overview

Introduction

1.1 This Consultation Paper (CP) covers the following:

- final disclosure rules for operators of self-invested personal pension schemes (SIPPs) following consultation in CP12/5; and
- consultation on inflation-adjusted Key Features Illustrations (KFIs).

1.2 In this CP we give feedback on the responses we received to Chapter 5 of CP12/5[1] and explain the final rules we have made, which are in Appendix 1. We are also consulting on proposals to move to inflation-adjusted illustrations for personal or stakeholder pension schemes (see the draft rules in Appendix 2). Chapter 4 contains our proposals for additional guidance for designing and drafting product information, to help firms produce information in a form that consumers can more easily understand.

Background

1.3 We consulted in CP11/3 on removing the exemptions for SIPP operators from the disclosure requirements for personal pensions and replacing them with exemptions that would only be available for personal pensions invested in certain types of investments. We also proposed rules to require firms to disclose whether they retain bank interest or receive commission in relation to money held in a bank account within a personal pension scheme. Then in CP12/5, we consulted on rule amendments to remove the SIPP exemption altogether and require firms to prepare complete disclosure documents, including projections, effect of charges and reduction in yield information. Chapter 2 of this CP sets out our response to the feedback we received to those proposals and explains the final rules we have made.

1 CP12/5 *Quarterly Consultation*, (March 2012): www.fsa.gov.uk/static/pubs/cp/cp12-05.pdf

1.4 We consulted in Chapter 4 of CP11/3[2] on possible future changes to pension illustrations to allow for inflation, but did not propose rule changes at that stage. This CP now makes proposals for changes to our rules requiring a move to inflation-adjusted illustrations. Since the final rules explained in Chapter 2 extend the disclosure requirements to all pension scheme operators, the new proposals we are consulting on will also apply to SIPP operators.

1.5 In Chapter 4 we discuss our proposals for additional guidance for designing and drafting product information. We have stated, on several occasions, that we are dissatisfied with the quality of some of the product information prepared by firms. Our research has confirmed that consumers struggle to wade through what they perceive as far too many pages of incomprehensible text which is poorly laid out and full of complex terminology.

1.6 We have therefore drafted guidance which should help firms prepare product information so it is more helpful for consumers.

Implementation and timetable

1.7 The final rules on disclosures by SIPP operators will come into force on 6 April 2013. We originally proposed 31 December 2012 for implementation, but have allowed further time in response to industry comments about other demands on firms.

1.8 The proposed new requirements for inflation-adjusted illustrations, if adopted following consultation, would come into force on 6 April 2014, with a transitional period allowing firms to start using them from 6 April 2013.

Equality and diversity issues

1.9 We have assessed the equality and diversity impact of the final rules on disclosure requirements for SIPP operators and the proposed move to inflation-adjusted illustrations. We do not believe that our proposals will give rise to any issues. However, we would welcome your comments on this.

Structure of this CP

1.10 The CP chapters cover:

- Chapter 2 – personal pensions – disclosure requirements for SIPP operators;
- Chapter 3 – Inflation-adjusted pension KFIs and related changes; and
- Chapter 4 – new guidance for product information.

2 CP11/3 *Product disclosure: Retail investments – changes to reflect RDR Adviser Charging and to improve pension scheme disclosure* (February 2011): www.fsa.gov.uk/pubs/cp/cp11_03.pdf

Who should read this paper?

1.11 All the chapters will interest life insurers and other providers of personal pensions, and also firms that advise on personal pensions.

1.12 Consumers will be interested in the effect of our proposals on the pension information they receive from firms.

2

Personal pensions – disclosure requirements for SIPP operators

Introduction

2.1 We are changing the way we regulate self-invested personal pension schemes (SIPPs). Operators of self-invested personal pension schemes (SIPPs) became regulated by the FSA in 2007. At that time we saw a distinction between mainstream personal pension schemes and schemes that allowed individual members control over the choice of underlying assets, schemes which were described as SIPPs. Given the way the market was operating, we decided that if a scheme was a SIPP then there was no need for firms to give clients a projection in a key features illustration (KFI) (for most SIPPs), or an effect of charges (EoC) table and reduction in yield (RIY) information (for any SIPP).[3] Additionally, at that time, although many SIPPs give scheme members the ability to hold cash within the scheme, we did not identify a need to regulate in this area.

2.2 The definition for a SIPP is framed widely and the SIPP market has evolved. The most recent product sales data submitted by firms now shows that roughly half of all pension schemes sold are SIPPs. Most 'SIPPs' are virtually indistinguishable from ordinary personal pension schemes. They have become mainstream products. Given this, we now consider that a more consistent market-wide regulatory approach is appropriate.

2.3 As sales of SIPPs have continued to grow, regulatory concerns have emerged. We have identified disclosure documents for pension schemes that are not of the quality we require, particularly for charges disclosure. Thematic reviews have also shown that some consumers have been switched into SIPPs without good reason, thereby incurring extra charges unnecessarily. And a recent review[4] showed, among other issues, poor firm conduct,

3 The 'projection' exemption does not apply if income withdrawals are being taken from the SIPP or if the SIPP is being used to contract out of the State Second Pension.

4 The report on Self-Invested Personal Pensions (SIPP) operators July 2012.

inadequate risk identification and risk mitigation planning, and evidence of regulatory breaches in respect of the holding and controlling of client money. Also, the volume of non-mainstream assets, such as unregulated collective investment schemes, held within SIPPs has risen, as has the tendency for some schemes to be heavily weighted in cash.

2.4 We have noticed that SIPP operators' approach to our disclosure requirements varies widely. Although some SIPP operators do use the exemptions, many do not and produce personalised KFIs, including projections, EoC tables and RIY information. This has made it a little difficult for us to estimate industry-wide costs.

Previous consultations

CP11/3

2.5 To address our concerns, in CP11/3 we consulted on removing the SIPP exemptions from our disclosure requirements and replacing them with exemptions that would only be available in relation to personal pension schemes invested in: commercial property, commodity investments, 'synthetic' exchange traded funds or shares (that are not shares in an investment trust).

2.6 We also proposed rules to require firms to disclose whether they retain bank interest or receive commissions in relation to money held in a bank account within a personal pension scheme.

2.7 The objective was to ensure that consumers and their advisers have the information they need to make good choices when comparing pension products.

2.8 Over 30 respondents replied and there were diverse and often conflicting views. It became clear that practical difficulties, regulatory risks and unwarranted costs would arise from our original proposals. In particular, confusion could arise if firms did not need to provide information in relation to certain volatile and hard-to-value non-mainstream assets within a scheme. There would also be an ongoing need to maintain this list of 'exempted' assets.

2.9 There was a mixed response in relation to the proposals to require disclosure of bank interest retentions and bank commissions. Some respondents were very supportive. However, others claimed that it would be difficult to disclose volatile or stepped interest rates. Others argued that secrecy was necessary to protect commercial confidentiality; they argued that disclosure of the rates retained would jeopardise the negotiation of favourable terms and thus lead to consumer detriment.

2.10 It was also suggested that, in addition to bank commissions, commissions for non-cash assets received by scheme operators should be disclosed as well.

2.11 We listened to what the respondents said and, as the responses to CP11/3 indicated that a better policy approach was possible, we decided to re-consult on a revised approach.

CP12/5

2.12 In CP12/5, we consulted on rule amendments that would remove the SIPP exemptions altogether, without replacing them with alternative exemptions. Instead, we proposed rules to require firms to prepare complete disclosure documents, including projections, effect of charges and reduction in yield information, for all schemes regardless of the following – the underlying assets, whether the personal pension scheme was marketed as a 'SIPP', and whether it was an income-drawdown product. Our objective was a level playing field for competing pension schemes and sufficient information for consumers and their advisers.

2.13 This revised approach also had the advantage of being consistent with the approach of the Department for Work and Pensions (DWP), which requires Statutory Money Purchase Illustrations (SMPIs) for all personal pension schemes, whether branded a SIPP or not, and regardless of the underlying assets.

2.14 We acknowledged that preparing projections for some assets will be a challenge. To help, we proposed guidance to make it clear that, when preparing projections, firms are expected to use the best available reasonable assumptions in relation to assets that are volatile or hard-to-value. So, for example, firms are not expected to commission formal valuations for assets when reasonable assumptions can be made from available data.

2.15 In both CP11/3 and CP12/5 we consulted on requiring scheme operators to disclose whether they receive commissions or retain bank interest in relation to money held within a pension scheme. In CP12/5, we went further and proposed requiring disclosure of commissions received for any asset (both cash and non-cash), alongside information about fees, costs and charges payable. We did not consider commercial confidentiality to be a reason why firms should be able to conceal their bank interest rate retention and the commissions received.

Feedback and response to feedback on the CP12/5 proposals

Deleting SIPP exemptions and requiring KFI, EoC and RIY information for all schemes

2.16 Most of the 22 responses indicated qualified support for removing the SIPP exemptions, subject to strong support for an implementation delay. A handful of respondents disagreed vociferously and continued to argue that SIPPs were a special case, but they did not suggest a way by which various SIPPs could be differentiated. Given the wide scope of the 'SIPP' definition which we discussed in CP11/3, the growth in the SIPP market, and the poor disclosure documents identified we cannot justify maintaining the status quo.

2.17 A number of respondents indicated that they would like us to provide further guidance on the 'best available reasonable assumptions' firms should use when projecting for assets that are difficult to value. We do not propose to expand on this high-level guidance, as we think the ordinary meaning of these words is clear. However, if it appears necessary, following further analysis and discussion with the industry, we may provide further comment or individual guidance on this in future.

2.18 Some respondents indicated they preferred the approach outlined in CP11/3, but did not offer suggestions how the problems with this approach could be resolved.

2.19 One respondent suggested that we consider introducing different rules for retail clients who were 'sophisticated pension investors' rather than ordinary pension investors. We reflected on this but concluded that creating a new client categorisation and separate regime for such investors would introduce unhelpful complexity.

2.20 Overall, there was strong support for our aim that all retail consumers get enough information to make informed pension choices and we are encouraged by this.

Disclosure of bank interest received and retentions by firms

2.21 There was general support for the proposal to require firms to disclose, alongside a description of the nature and amount of the charges a client will or may be expected to bear, details of the interest to be received by clients on cash held within the scheme. This is encouraging, as we want to see an end to information about unattractive interest rates being hidden away in small print or on obscure website pages.

2.22 There was also some support for the proposal to require firms to disclose the fact and extent of interest rate retentions by scheme operators or scheme trustees. However, some respondents had strong objections to disclosing the amount of interest retained, if any. Some firms argued that calculating and disclosing these amounts will involve significant costs, breach commercial confidentiality and provide limited benefits for clients. We appreciate the challenges that will arise if firms need to alter their approach to client money. But we also consider that, to understand the charges they will be paying and how they will be paying them, consumers do need this information.

Disclosure of commissions received and retained

2.23 A number of respondents agreed with the proposal to require disclosure of commissions received and retained by firms. Others suggested these rules should be consistent with those applying to platforms.

Final rules

2.24 As responses to CP12/5 have been mixed it is clear that some stakeholders will object whatever approach we adopt. But we see a real need to address our concerns about poor disclosure and the unintended impact of the SIPP exemptions. We want pension scheme members to be able to calculate and compare the fees, charges, commissions and retained interest that may apply to competing schemes. So we have decided to proceed with the proposals consulted upon, with one modification.

Deleting the SIPP exemptions and requiring all personal pension schemes to provide KFIs, effect of charges, and reduction in yield disclosures

2.25 We are proceeding with the proposal to remove the SIPP exemptions in the rules, and to introduce guidance to make it clear that if a scheme is invested in assets that are volatile or difficult to value, the standard deterministic projections should be prepared using the best available reasonable assumptions.

Requiring the disclosure of bank interest received and retained

2.26 We will require firms to disclose, as part of the information in a key features illustration, details of the interest to be paid to clients on money invested within the scheme. We will also require firms to disclose, as part of 'the appropriate charges information', whether or not the scheme operator or the scheme trustee is retaining any interest on money held within the scheme and, if so, the amount retained. In our view, favourable interest rates obtained from banks should be used to obtain competitive advantage and benefit the consumer rather than provide a secret profit for the operator (if the interest is not used to offset other charges). Where the interest receivable is volatile we do not expect detailed calculations and recalculations. Operators should be able to make reasonable assumptions, based on the income they receive or expect to receive from interest retention, and disclose accordingly.

2.27 Although there was support for the proposal to require specific disclosure of commissions, we agree that our policy and rules regarding pension scheme disclosure should be consistent with our approach to platforms. As many personal pension schemes are held on platforms a consistent approach is desirable.

2.28 CP12/12 set out our intention to prevent platforms from being funded by payments from product providers. We felt that for the client to be clear about how much a platform service will cost, and to remove the potential for product bias in the market, the end consumer should pay the platform service directly through a platform charge. We also asked the question whether this proposal should be read across to other markets such as the SIPP market. So, before making further rules in this area, or considering whether we may need to go further than improved disclosure, we will wait for the outcome of the platforms consultation.

2.29 This postponement does not alter the view expressed in CP11/3 and CP12/5 that firms owe their clients a fiduciary duty not to act for their own benefit and make and retain a secret profit from a scheme member's assets. If commissions are received, we take the view that, taking into account the information needs of their clients, firms should disclose these payments and obtain informed consent from their clients to any commission that is retained.

2.30 These final rules reflect amendments that other instruments have made or will make to the relevant rules before the implementation date of this instrument. In particular, the final rules reflect the RDR adviser charging rules. However, the policy effect is the same as consulted on, these new disclosure requirements will apply to all personal pension schemes (whether SIPPs or not, and whether adviser charges are facilitated through the product or not).

Implementation delay

2.31 Several respondents to CP12/5 referred to the other demands on the industry in 2012 and asked for more time to implement these changes. So, instead of the start date of 31 December 2012 originally proposed, these changes will come into force on 6 April 2013. This date coincides with the start date for other relevant changes for firms and should help them introduce changes in a more cost-efficient way.

Cost benefit analysis

2.32 An updated cost benefit analysis is in Annex 2.

3

Inflation-adjusted illustrations for personal pensions

Introduction

3.1 In this chapter, we are consulting on changes to the way in which the effect of inflation is portrayed when illustrating a personal or stakeholder pension. Currently firms are required to provide information about the impact of inflation on benefits. They can choose to do this by providing an inflation-adjusted projection in addition to the three standard deterministic projections in monetary terms.

3.2 Our proposed changes would require firms to provide standard deterministic projections that explicitly include the effect of inflation and show the potential outcome in real terms instead of nominal terms.

3.3 We are also proposing to remove:

- the ability to provide deterministic projections that are in addition to the mandated ones (COBS 13.4.1 R); and
- the option of omitting the intermediate projection when providing projections for existing business (COBS 13 Annex 2 R 1.10).

3.4 If adopted following consultation, we propose to bring the rules into force from 6 April 2014, with a transitional rule allowing firms to provide inflation-adjusted illustrations earlier if they wish, from 6 April 2013.

Background

3.5 Our Key Features Illustration (KFIs) rules for personal and stakeholder pensions require projections in nominal terms on three growth rates (subject to maximum rates). These give customers an indication of the potential variability of outcome. Further, KFIs include a table showing the effect of charges over the lifetime of the contract on the value of the fund, and a measure, the reduction in yield (RIY), which shows how the charges effectively reduce the investment growth. The RIY enables comparisons of the overall cost of investing.

3.6 Our existing rules allow firms to provide alternative projections, giving them scope to provide projections in real terms as well as stochastic projections, as long as the projections required by our rules are the most prominent.

3.7 Having purchased a personal or stakeholder pension, customers receive an annual pensions statement each year in line with Department for Work and Pensions (DWP) rules for Statutory Money Purchase Illustrations (SMPIs). The technical detail is managed by the Financial Reporting Council (FRC). An SMPI is a single projection based on the intermediate growth rate adjusted to allow for 2.5% inflation a year.

3.8 Since the introduction of SMPIs in 2003, there has been potential for consumer confusion, because the point-of-sale pension projection is in nominal terms but the SMPI is in real terms. Clearly, it is desirable that firms provide point-of-sale projections and SMPIs consistently. So we stated our intention to move to inflation-adjusted point of sale projections in CP134[5] and again in PS07/18[6], where we permitted firms to add inflation-adjusted projections into KFIs in addition to nominal projections. However, we deferred changing our rules until the outcome of the DWP's ongoing review of SMPIs was known.

3.9 In 2011, in CP11/3[7], we repeated our intention to move to real projections and sought feedback from the industry on how this should be done.

3.10 We have also continued to liaise with DWP and the FRC on the underlying assumptions and content of KFIs and SMPIs. In the light of those discussions, we think it is now the right time to consult on introducing inflation-adjusted illustrations.

3.11 Personal pensions have been included in the European Commission's draft proposal for a Regulation on Key Information Documents for Investment Products (also known as the 'Packaged Retail Investment Products', or 'PRIPs' Regulation). The Regulation is not expected to come into force until at least 2015, and its scope is subject to further discussion before it is finalised. But, at present, given the projection requirements permitted in the Solvency II Directive and the support for a move to inflation-adjusted projections, we do not see any reason to further delay their introduction.

5 CP134 *Pension Projections* (April 2002).
6 PS07/18 *Conduct of Business Regime* (October 2007).
7 CP11/3 *Product Disclosure: Retail Investments – changes to reflect RDR Adviser Charging and to improve pension scheme disclosure* (February 2011).

3.12 In Chapter 2 we confirm that SIPPs will be included within the KFI regime. So these proposals will also apply to SIPP operators.

Our research

3.13 Following the feedback received to CP11/3, which showed substantial support for our proposals, we commissioned research to help us decide how projections in real terms could best be presented. We felt this would be helpful, because many KFIs had grown so long and cluttered that consumers were unlikely to engage with the new style of illustrations unless the presentation was improved. We appointed Strictly Financial to conduct the research, which involved working with groups of consumers as well as advisers.

3.14 Strictly Financial used a two-stage approach to the research:

i) Co-creation workshops with consumers

Here FSA staff were actively involved in discussions with consumers, obtaining feedback on sample inflation-adjusted KFI designs. The insights gained from these sessions are given at Annex 3.

ii) Qualitative research

After we had discussed the insights from the workshops with Strictly Financial, we asked them to carry out qualitative research, first with independent financial advisers and then with consumers. Both groups were asked to give their views on a current pension KFI using a typical example (updated to include adviser charges), and then their reactions to versions showing inflation-adjusted projections. FSA staff observed some of the consumer sessions.

3.15 The insights gathered from the workshop sessions and from previous research were used to prepare two KFI designs containing inflation-adjusted projections. We aimed to:

a. incorporate good practice principles for design and language style;

b. avoid pitfalls in design of the KFI itself that could have lead to consumers disengaging from it before reaching the inflation-adjusted projections;

c. avoid unnecessary technical language and jargon;

d. minimise the concepts that consumers needed to understand; and

e. minimise the figure work on the KFI. So we tested an approach not tried in the co-creation sessions. This was a KFI that showed projection rates net of inflation (the extent that investment growth beat or was beaten by inflation). This avoided consumers being distracted by their perceptions of the reasonableness of the growth and inflation rates.

3.16 Strictly Financial's final report[8] is being published alongside this CP, together with the sample inflation-adjusted KFI designs used in the consumer workshops. The report lays out the process followed, and the outcomes. We refer to Strictly Financial's findings, where relevant, in our proposals below.

Our proposals for inflation-adjusted illustrations

Projections

3.17 For SMPIs, the existing fund plus future expected monetary contributions are rolled up at a monetary growth rate and then discounted using an explicit inflation assumption to determine the fund at retirement in real terms. This is the same as rolling up the fund plus future real contributions using a real growth rate. Our research tested both of these methods of presentation to find out how consumers responded to the different styles.

3.18 However it was presented, the consumers in the research thought they should be made aware at the point of sale of the possible effect of inflation on the buying power of their pension, although they were often shocked by the figures they saw. They thought this would allow them to plan for their retirement more effectively. Their views were supported by advisers, which adds more weight to our proposal to introduce projections in real terms.

3.19 The research indicated that consumers had a clear preference for projections using real growth rates. The alternative method of rolling up the fund at a monetary rate and then reducing it to take account of inflation was distracting. Most consumers wanted to see fewer numbers in their illustrations, not more.

3.20 Advisers' preference was also for real growth rates, although it was less marked than with consumers. So we propose that firms should show only net growth rate after inflation has been taken into account (as applied to the real value of contributions). Also, when providing a projection of the fund to be annuitised, firms should show it only in real terms, accompanied by a risk warning on the impact of inflation and that the product may pay back less than paid in, if that may be the case (COBS 13 Annex 2 5.1R(1)).

3.21 In CP11/3, we asked respondents whether a single inflation rate should be used or different inflation rates which might, theoretically, more closely correspond to the lower and higher growth rates. At that stage, the flanking rates were 2% for both the growth rate and inflation rate, which would cancel out the variable outcomes that three projections seek to demonstrate. Views were split on the approach, although those preferring different inflation rates did not comment on how three nearly identical projections would be perceived by consumers.

8 www.fsa.gov.uk/pubs/cp/illustrating-the-effect-of-inflation-on-future-retirement-income.pdf

3.22 We consider that for consumers to receive meaningful real projections there must be different real growth rates. This can be achieved by using the same rate of inflation with each of the three monetary growth rates. We therefore propose that the intermediate rate of price inflation should be used in all three growth scenarios to determine the maximum real growth rates.

3.23 PS12/17[9] lays out the new maximum monetary growth rates that will apply from 6 April 2014, with a transitional period allowing firms to use them from 6 April 2013. We recognise that the lowest growth rate will result in negative real growth. We tested this outcome in our research, and we consider that consumers should be aware of the possible consequences of low monetary growth rates and of investing in funds that are expected to produce low returns in the medium to long term. This view was supported by advisers involved in the research.

3.24 Several customers in our research, having appreciated the effect of inflation on a pension, did not then realise that inflation also affects other types of investment and savings in the same way. So they thought it might be preferable to save for their retirement in different ways. Therefore, as well as requiring firms to provide statements about inflation in KFIs, we have also added a requirement in our draft rules that will extend this statement to note the impact of inflation on all saving and investments.

Effect of charges information

3.25 The figures in the effect of charges table are currently consistent with the intermediate growth projection. Our draft rules will require the effect of charges table to be in real terms. Accordingly, the reduction in yield figures will also be expressed in terms of real yields.

3.26 We are also proposing some consequential changes to the rules in COBS 13 Annexes 3 and 4 for the effect of charges table to reflect the change of projection basis to better explain the table. First, we are proposing that a statement is included with the table to tell consumers that it can be used to compare charges with other personal pension plans. Secondly, we have drafted a minor change to one of the example column headings suggested by our research respondents. They suggested that the heading *If there were no charges* would be better if it stated *Before charges are taken* since it is not possible to have a plan without charges.

3.27 We are proposing that the new rules become effective from 6 April 2014. However, as SIPP operators will be required to prepare KFIs for the first time from 6 April 2013, we are proposing a transitional period which will enable firms to adopt the new rules from this earlier date.

> **Q1:** Do you agree with our proposals for presenting projections in real terms? If not, please explain what alternative approach you think is more appropriate.

9 PS12/17 *Projections and transfer value analysis* (November 2012).

Q2: Do you agree with our proposals for changing the text relating to the effect of charges table? If not, please explain what alternative approach you think is more appropriate.

Drawdown pensions

3.28 Illustrations of income drawdown analyse its effect on the residual value of a personal pension contract, using three different nominal growth assumptions. The analysis shows how the value may reduce (or increase) during retirement. SMPIs are not required once a personal pension goes into drawdown, so no confusion is caused by a different basis.

3.29 Some consumers and advisers may find it helpful to see the analysis in real terms and others may find that this complicates the analysis. We have not tested this in our research, so are not proposing to change our rules for drawdown pensions at this stage.

3.30 In response to queries received we are also proposing a refinement to COBS 13 Annex 2. 2.9R to place an age limit on the analysis where the pension fund will not be exhausted at the higher rate of return. We propose age 99 in case some firms' systems have a two digit field length.

Q3: Do you agree that illustrations for drawdown pensions should remain in nominal terms? If not, please explain what alternative approach you think is more appropriate.

Q4: Do you agree that a maximum age of 99 is reasonable for drawdown analyses? If not, what age limit would you suggest and why?

Generic illustrations

3.31 In specific circumstances, firms may use generic (i.e. example) illustrations in place of a personalised KFI. Currently firms are able to provide generic illustrations in either nominal or real terms. For consistency, we propose that only generic projections in real terms may be prepared in future.

Q5: Do you agree that we should only permit generic illustrations in real terms? If not, please explain what alternative approach you think is appropriate.

Alternative illustrations

3.32 Currently firms can produce alternative projections in addition to those required for the KFI. So our rules enable firms to provide projections which are in addition to the three standardised deterministic projections as well as allowing the provision of stochastic projections.

3.33 We have seen firms that project on less than the maximum rates (where the underlying assets are unlikely to produce those rates), yet still provide an additional projection at the maximum rate. Such projections are unnecessary and misleading. Further, the current rule could allow firms to provide pension projections in nominal terms in addition to the proposed three inflation-adjusted projections.

3.34 Feedback from the consumers in our research suggests that providing further projections is confusing. In general, consumers want as few numbers as possible in as short a document as possible.

3.35 Many consumers in our research commented favourably on the shorter documents used in testing compared with those that they had received recently from their own pension providers.

3.36 We therefore propose that only stochastic projections can be provided in addition to the three standardised deterministic projections, for both life and pensions products. We will retain the existing requirements for stochastic projections, so that they can only be provided if there are reasonable grounds for believing that a consumer will be able to understand them. The differences between the stochastic projection and the deterministic projection must be explained. For consistency with our proposals for pension projections, stochastic projections for pensions will also need to be in real terms.

Q6: Do you agree with our proposals for alternative projections?

Projections for existing business

3.37 In CP11/3, we proposed that it should no longer be possible to omit the intermediate growth rate on in-force projections. This would have affected very few firms. While we did not change this rule at that time, we said that we would reconsider it when we consulted on introducing inflation-adjusted illustrations. We now consider it is appropriate to remove the exemption allowing the intermediate rate to be omitted.

3.38 The SMPI can act as a call to increase contributions. But, if the recipient then requests a projection of the possible effect of the increase, the lack of a projection at the intermediate growth rate will prevent this.

3.39 We consider that the implementation of this change fits comfortably alongside the work that firms will be undertaking to introduce real projections. Further, it enables firms to consider consolidation of systems used for point of sale, existing business and SMPIs.

> **Q7:** Do you agree that we should now remove the exemption allowing the intermediate growth rate to be omitted for in-force projections?

Other types of projections

3.40 There are other types of projection or quotation where a consumer may find it helpful to see the possible impact of inflation on the value of the benefits. These are transfer value analyses and conventional and investment-linked annuities.

3.41 Transfer value analysis (TVA) reports usually contain projections to enable consumers considering a pension transfer to compare the benefits being given up in their defined benefit scheme with those that could be provided by the personal pension scheme recommended by the adviser. It could be confusing for consumers to receive a TVA report in monetary terms, but the illustration for the recommended personal pension in real terms. Respondents to CP12/04 indicated that pension scheme members already struggle to understand the consistency between TVA reports and KFIs. Allowing TVA reports to remain in monetary terms is unlikely to help the situation.

3.42 The expected duration of conventional annuities continues to increase, and inflation could have a significant impact on the value of income over an annuitant's lifetime. Most conventional annuities are set up with level income. So we are interested in respondents' views on whether there should be a mandatory statement of the effect of inflation on annuity quotations or illustrative examples of the buying power of the annuity after, say, 10 or 20 years.

3.43 We would like views on the extent to which these other types of projections and quotes should refer to, or include, a specific allowance for inflation.

> **Q8:** Do you think we should allow for inflation in transfer value analysis reports? Please give your reasons and provide evidence for your views, where possible.

> **Q9:** Do you think we should allow for inflation in annuity quotations? If so, please explain how and give your reasons.

Rule clarification

3.44 We are taking this opportunity to make a minor rule clarification to the wording of COBS 13.6.1R that some firms comply with by providing KFIs. This rule covers the commencement of, or changes to, facilitated adviser and consultancy charges from an in-force packaged product. Firms may do this by providing sufficient information for the retail client to be able to understand the effect of the change. The rule is unclear about the timing of the provision of sufficient information. So instead of … *in good time before that information has to be provided* we are proposing … *in good time before it takes effect.*

Q10: Do you agree that the proposed change to the wording of COBS 13.6.1R will make this rule clearer?

Cost benefit analysis

3.45 The cost benefit analysis for this chapter is in Annex 4.

Q11: Do you have any comments on the cost benefit analysis for Chapter 3?

4

New guidance for product information

Introduction

4.1 In this chapter, we discuss our proposals for additional guidance for designing and drafting product information. We have stated, on several occasions, that we are dissatisfied with the quality of some of the product information prepared by firms. Our research has confirmed that consumers struggle to wade through what they perceive as far too many pages of incomprehensible text which is poorly laid out and full of complex terminology.

4.2 We have therefore drafted guidance which should help firms prepare product information to make it more helpful for consumers. If adopted following consultation, this would come into force on 6 April 2014. Firms can use the guidence earlier if they so wish.

4.3 The research by Strictly Financial is published with this consultation. The next section gives an overview of the key findings.

Background and research findings

4.4 Although we have formally assessed good and poor practice for KFIs (as we did with key features documents[10]), many of the KFIs we have seen are of poor quality and not of the standards achieved by marketing literature and current key features documents.

4.5 We have made known our views on the quality of KFIs in various ways, such as at trade association and firm meetings, as well as through industry working groups and presentations. In particular, in PS11/14, we made it clear, in response to industry's criticism of the illustration regime, that we consider the problems arise largely from the way firms have implemented the regime. Few firms have taken advantage of the simplified rules introduced in COBS in 2007 or have introduced the improved technology used, for

10 www.fsa.gov.uk/pubs/other/key_features.pdf and www.fsa.gov.uk/pubs/other/kfd_annex.pdf

example, in utility bills. Items and text have been added to KFIs without considering whether the existing content could be improved.

4.6 We have seen no evidence to suggest that the fundamental aims of the illustration regime are misplaced: that consumers must be given an indication of what they might get back (and the potential for variability); and that they should understand the effect of charges on their investment and be able to compare them. Our rules are designed to deliver those aims, but do not prevent firms from presenting the information in ways which encourage consumers to engage with these documents.

4.7 As part of the research, consumers looked at a document which was based on a better than average example of current practice. Although consumers said it was better than the KFI they recalled receiving for their own pension plan, they still found it daunting and approached it with trepidation.

4.8 They struggled with language that they perceived as being legal or regulatory phraseology instead of what they want: language which is simple and direct. The use of certain words or phrases often created emotive reactions; ‘cancelling units’ was seen as ‘stealing my money’. The term ‘annuity’ was unfamiliar to many, and even after an explanation, many thought that by purchasing a pension plan they had already purchased a retirement income.

4.9 Disclaimers were seen as a way for firms to protect themselves rather than helping consumers understand the assumptions and warnings.

4.10 Inconsistent use of language or unnecessary information only served to further confuse consumers and make them question whether they were doing the right thing.

4.11 A lack of scene setting meant that although consumers acquired a superficial understanding of what the document was attempting to achieve, they lacked understanding about what the information meant for them individually. Many saw the adviser as essential for helping them to comprehend the document.

Our proposals

4.12 The documents that we devised and tested for our research into inflation-adjusted illustrations were seen as an improvement over the versions the participants had received for their own plans.

4.13 It was noted that the documents were significantly shorter than existing ones. The language was perceived as clearer, and this was felt to be more important than over-shortening the document. However, our guidance urges firms to consider the length of such documents. In our research, consumers were unable to face KFIs of more than three to four pages.

4.14 Layout is vital: by making the document visually accessible, consumers are more likely to engage with it and read it. Our guidance encourages firms to consider techniques such as good use of white space, line widths, font size and line spacing, appropriate use of paragraphs, avoiding large blocks of text, and the use of short sentences.

4.15 Clear language is crucial if consumers are to gain any understanding of what the KFI is trying to tell them. Our guidance encourages firms to consider the likely level of financial understanding of their target market. Our rules do not prevent firms from adopting different approaches for different target markets as proposed by the The Actuarial Profession's Consumer Information Working Party.[11] Firms should be careful to use consistent language throughout the document and not assume that consumers understand their concepts, jargon or terminology.

4.16 Few firms use modern design techniques (used regularly by other service industries) to aid consumer understanding. Our guidance encourages firms to consider using side annotations, shading, colour, bulleted lists, tables and graphics. Our research indicated that consumers had split views on the use of graphs. Some preferred graphs, but they were unable to interpret them sufficiently correctly. So firms should consider designing graphs so they are clear for their target market.

4.17 We have also included guidance reminding firms to be aware of the eventual means of printing or displaying the product information. For example, we have heard favourable comments from consumers on the use of colour. At the same time, the inclusion of colour can result in multiple shades of confusing indistinguishable grey, if the document will be printed on a black and white printer.

4.18 Firms need to consider carefully whether the information they include in a personalised illustration is relevant to the consumer's understanding of the suitability of the investment for them at an individual level. Far too often, firms include background information or information on the application process which distracts from the main messages and would be better located in another document.

4.19 On the other hand, our KFI designs contained information which was new to some participants, i.e. that they could switch funds, change retirement date and had a range of choices about the payment of their retirement income and that the decision can be left to that time. Our guidance urges firms to focus on the key product information that consumers require to make an appropriate judgement on the product.

Q12: Do you have any comments on our proposals to introduce additional guidance on preparing product information?

11 www.actuaries.org.uk/sites/all/files/documents/pdf/bajweb-versionupdatedpdf.pdf

Cost benefit analysis

4.20 The cost benefit analysis for this chapter is in Annex 4.

Q13: Do you have any comments on the cost benefit analysis for the proposed new guidance on preparing product information in Chapter 4?

Annex 1

List of non-confidential respondents to Chapter 5 of CP12/5

Aegon

AJ Bell

Association of British Insurers

Association of Member-Directed Pension Schemes Aviva

Axa Wealth

Capita Financial Software

Capita Life & Pensions Regulated Services

Financial Service Consumer Panel

Friends Life

Hargreaves Lansdown

The Hornbuckle Mitchell Group Limited

Investec Wealth & Investment

L&G

LV=

Andy Leggett

Scottish Life

Suffolk Life

Xafinity

There were three confidential responses

Annex 2

Updated cost benefit analysis for Chapter 2

1. When we consulted in CP12/5 we undertook a cost benefit analysis (CBA), as required under section 155 of FSMA. This was not a straightforward process as within the SIPP sector there are very different business models. The costs involved in amending their approach to disclosure may be significant for some firms and insignificant for others. We also accept that certain one-off costs, such as consumer or adviser testing on revised literature, or staff training on new software, may arise which were not reflected in our original CBA.

2. This CBA is also updated to remove any reference to the costs and benefits that would have arisen if we had proceeded with a rule requiring disclosure of all commissions received on pension scheme assets.

Firms to provide disclosure documents for all pension schemes, including SIPPs

One-off costs

3. We originally assumed that most scheme operators would offer pension drawdown facilities or accept contracted-out funds (no respondents argued otherwise). So, to comply with existing requirements, we took the view that most firms operating pension schemes would already have the means of providing compliant KFIs and should not incur significant one-off costs in introducing these documents. The exception would be firms that primarily offer SIPPs as a tax wrapper for consumers investing in non-traditional underlying assets.

4. We also assumed that, as the Department for Work and Pensions has required statutory money purchase illustrations (SMPIs) for all personal pension schemes since 2003 (there are no exclusions for SIPPs), all scheme operators should currently have the means to establish

reasonable charge and growth rates for each of the major assets in their SIPPs, as well as the systems needed to provide this type of illustration.

5. In addition, some KFI software that we have looked at already enables firms to produce KFIs largely as we now propose.

6. So, while some firms' software will need enhancement, we believed that for most firms this could be done for modest cost as part of current maintenance agreements, and we maintain that view. We also believe that the one-off cost of staff training on new software, and the cost of consumer or adviser testing on revised literature, will be modest.

Ongoing costs

7. The product sales data for January to June 2012 shows that 110 firms took on new schemes branded as 'SIPPs', with fewer than 100 firms doing significant business. It is these firms who will face additional costs, if they do not currently produce KFIs including the information required by these changes. The product sales data also indicates that around 200,000 schemes described as 'SIPPS' are sold annually, and we estimate that at least 20% will involve pension drawdown. The data also indicates that roughly half of SIPPs are sold with advice. So, each year, we estimate that a maximum of 160,000 new schemes could be affected by the need for enhanced KFI disclosure.

8. Our investigations show that over 60% of SIPP operators, including most of the market leaders, provide KFIs that include projections anyway (of varying quality). This would indicate that the amendments will have less impact on industry costs. But, as we intend to help consumers and their advisers to more readily compare charges, we have to assume that more than one KFI could be prepared for each potential advised sale (around half of all SIPPs sold are sold with advice). This would indicate more impact on costs. Finally, many investors use operators' web-based KFIs rather than ask for paper versions to be supplied, and this indicates less impact on costs.

9. So, taking all these factors into account, we maintain our estimate that around 50,000 extra KFIs will be required as a result of these amendments. Assuming an average cost of producing an enhanced KFI of £2 (paper documents will be more expensive, electronic versions will be cheaper), we estimate an ongoing cost to the industry of around £100,000 per year. Depending on industry competition, we accept that some or all these costs could be passed on to consumers.

Benefits

10. For the benefits of these proposals to arise, consumers or their advisers will need to be able to compare personal pension schemes and alternative products more effectively, so that this, in turn, can contribute to more suitable decisions and to the benefit of the consumer.

Disclosure of bank account interest payable to scheme members

11. It is an existing requirement for pension scheme operators to disclose the interest that scheme members will be paid on cash invested in a scheme. Our revised rule will simply require that the location of this disclosure is alongside appropriate charges information.

One-off and ongoing costs

12. We estimate that amending the location interest information is disclosed will involve minimal one-off and ongoing costs for most firms as they will be able to amend existing documents and web pages as part of business-as-usual updates.

Benefits

13. If this information about bank account interest is presented alongside the information about charges we believe it will be easier for consumers and their advisers to gain an overall indication of a scheme's benefits and make more suitable purchasing decisions.

Disclosure of bank account interest retained by firms

14. Requiring firms to disclose the bank account interest they retain, alongside information about charges payable and bank interest rates receivable, if any, will incur minimal costs for those firms that retain interest. This disclosure requirement will not affect pension scheme operators that do not retain bank interest, other than the minimal cost of revising KFIs, as part of business-as-usual updates, to say that they do not retain interest, if they do not say this already.

One-off and ongoing costs

15. As this is not currently disclosed, it is not always clear whether a scheme retains interest. However, we believe that up to 75 firms may retain interest. If a firm's disclosure documents need to be revised and reprinted, our estimated one-off cost of revising a firm's documents is £800 per firm: (total industry cost: 75 x £800 = £60,000).

Ongoing costs

16. There will be ongoing costs associated with providing new consumers with up-to-date information on bank interest retention in the paper or web-based KFI. The annual cost of providing KFIs was estimated in the previous section.

Benefits

17. The disclosure of retained interest will help consumers and their advisers gain a better understanding of the overall costs and benefits applying to different SIPPs. As a result, with the benefit of this 'big picture' overview, some consumers may make better-informed purchasing decisions. However, we expect this effect to be modest as research indicates that many consumers typically do not pay sufficient attention to product charges when purchasing investment products. Further, some consumers are already aware of what interest they receive on the cash they hold in SIPPs (even if, currently, they do not necessarily know how much operators retain).

Annex 3

Insights from the FSA-consumer workshop sessions

1. We know that some consumers do not read long documents. They also have difficulty understanding detailed explanations and investment concepts and are often intimidated by figure work. Introducing the effect of inflation on the value of pensions would add another layer of information and potential complexity. So we tested various ways of minimising the figures, as well as explaining the possible impact of inflation on the future buying power of pensions.

2. We took a co-creation approach as a first step whereby consumers and FSA staff were facilitated by an independent research firm, Strictly Financial, in discussions about current and proposed KFI designs and content. The participants had all bought a personal pension or SIPP recently or were thinking of doing so.

3. We aimed to:

   - identify consumers' general attitudes towards pension planning and their expectations for pensions and their role in planning for later life;
   - examine usage and understanding of the current KFI designs and how well it meets consumers' needs;
   - assess alternative approaches to KFI documents in terms of ease of understanding, key messages and approach to inflation; and
   - suggest guidelines for KFIs which can be used to inform future developmental work.

4. First, we asked the participants to read and review a current version of a KFI at home so they could discuss its pros and cons. We wished to avoid discussion about obvious shortcomings in design and language but to focus on the fundamentals. So we based the

example on a current KFI that was better than average although, in our view, it was too long at seven pages. Some participants spontaneously confirmed that the example was better than the version they recalled receiving.

5. The example KFI included an example of the effect of inflation on the 'buying power of money', but not inflation-adjusted projections.

6. We divided the participants into groups based on age in the expectation that engagement with pensions might be different. In the group discussions the facilitators identified where explanations and other information would be contained in the accompanying key features document or fund guide.

Main responses to current KFI
• Consumers approach this material with trepidation. The mindset of 'I wont be able to understand' means that they easily give up when they hit the first stumbling block such as an unfamiliar concept, a dense paragraph, jargon or too many figures. • Written technically/legally and from regulatory perspective. • Needs to be written from the consumer perspective – simple and direct. • Initially daunted by all the figures. • Many unaware that their contributions are invested in funds to build a pot which can be used to buy an annuity – the concept of deferred pay was not grasped. • Suggest more should be made of the positive aspect of tax relief.
Importance of design • Keep it visually accessible by white space. Unbroken paragraphs overwhelm key information. • Modernity appreciated (as in some modern utility bills). • Use layout (e.g. indents, clear headings hierarchy) to aid communication and navigation.
Importance of scene setting and of a logical order information • Explain the purpose of the illustration. • Logical flow of information, build the story.
Superficially understood, but when probed fundamental issues in comprehension • This was an above average KFI example, other examples likely to cause more problems.
Consumers can respond emotionally to words/concepts • Repeated use of *assuming* or *assumptions* can irritate. • *Expenses* (why are they different to charges?). • *Cancelling units* implies *stealing my money*.
More direction/reminders about choices • Even the most sophisticated audiences choose the default/unaware of their chosen funds. • *Intended retirement date* reassures because it shows that it can be changed.

Main responses to current KFI
Easily confused by the charges • Prefer real amounts rather than percentages. • Initially puzzled why there are both product and fund charges. • Just show total fund charges not separate annual management charges and fund expenses. Not interested in the detail. • Asked for one overall charges figure without realising the purpose of the (reduction in yield) statement under the effect of charges table. • Explain the purpose of the effect of charges table. • Inability to 'do the maths' in the effect of charges table renders the figures meaningless to many. Providing enough information to be able to do the maths, even roughly, would reassure and increase understanding.
Three rates of growth accepted/unquestioned. • However people get lost in the projections because of poor explanation and layout. • Some desired more information about risk and reward in the document. • Confused by the relevance of interest rates to annuities.
Avoid including (inadvertent) 'red herrings' • Mentioning that inflation-adjusted figures are not provided simply highlights the issue and poses the question why not. • Including unnecessary information and detail adds layers of complexity and potentially causes confusion. Consumers willing to refer to other documents (e.g. key features document) for background and detail.
Desire for adult/direct approach in language and explanations • E.g. more explicit about what happens on death.

7. After commenting on the current example, the participants were asked to discuss two alternative, but relatively conventional, presentations of KFIs that showed the possible impact of inflation. Both included facilitated adviser charges and the effect of charges table required from 31 December 2012. These are being published with the report by Strictly Financial, at the same time as this CP.

	Example A	Example B
Length	4 pages	3 pages
Structure	**Page 1:** Introduction, personal information, payment details and chosen investment funds. **Page 2**: Charges. **Page 3**: Projections and assumptions. **Page 4:** Effect of charges.	**Page 1:** Personal information, introduction and projections. **Page 2**: payment details, chosen investment funds and assumptions. **Page 3:** Charges and effect of charges.

	Example A	Example B
Content	• More white space. • Includes alternative pension if tax-free cash is taken. • Effect of charges table ◦ For years 1, 2, 3, 4, 5 and final; ◦ includes accumulated contributions in monetary terms. • Statements showing how product charges and how total charges reduce investment growth. • Section showing the combined effect of charges and inflation for the final year. • Statements showing how product charges plus inflation and total charges plus inflation reduce real investment growth.	• Headings and sub-headings in blue. • Effect of charges combined with effect of inflation in a single table. • Effect of charges and inflation table for years 1, 3, 5 and final. • Statements showing how product charges plus inflation and total charges plus inflation reduce real investment growth.

8. In summary, the participants' views were:

Main responses to inflation-adjusted KFIs in current style
Appearance • Prefer a short document but very little information was regarded as superfluous. • Dense pages are off-putting and are unlikely to engage the reader. • Lots of pages are also daunting but white space can offset this. Therefore prefer well-designed longer document than dense shorter one. • Desire some use of colour.
Structure • Explain purpose of the document. • Order and flow of information needs to be logical and chronological. No desire to see the projections first. • Avoid cross references to other pages in the same document. • Appreciated the message that yearly statements will be sent so that performance can be tracked.
Content • Impact of inflation on pension can be understood and is welcomed provided the KFI engages the reader. • The post 31 December 2012 effect of charges table was better understood than the current version. • Minimise figures. ◦ Combine the annual management charge and additional expenses. ◦ Combined effect of charges and inflation in single box was preferred. • Liked the column for accumulated contributions in the effect of charges table. • Availability of choices at retirement was welcomed.
Language • Keep it simple, consumers can then understand as long as they engage with the KFI. • Use 'power phrases' *Buying power, Keeping track* and active and direct language.

9. Overall the generally poor understanding of pensions, even for those who have already purchased a pension product, means that consumers do not necessarily know what information they need until they read the document. There is a natural desire for better presentation and shorter documents, but the participants were unable to identify the information that they thought they did not need.

10. Anticipating the desire for shorter documents, participants were then shown two experimental KFIs. These were intended to test different ways of reducing both the length of the KFI as and the number of figures they contain. The projections and the effect of charges information was presented in a different way. Neither KFI included a separate 'effect of charges' table. Both were two pages long, used plain language, with coloured headings and explanatory side notes and coloured shading in the tables. They both included:

- on **Page 1**; prominent personal information, introduction, three columns of projections in nominal terms at different rates to the end of years one, three, five and the selected retirement date; and
- on **Page 2**; the plan and adviser charges, signpost to fund charges on the left, with the effect of the charges (the so called reduction in yield) in a shaded box in the centre with coloured explanatory notes on the right.

  The investment fund choices and the assumptions made to calculate the fund/pot and the monthly income.

  The 'yearly charge' for each fund (i.e. the TER) was shown next to the fund selection rather than in the charge section.

	Example C	Example D
The regular income presentation and the effect of inflation	After the three projections of the pension fund in nominal terms: • The inflation-adjusted fund. • The monthly income this might provide. • The alternative (inflation-adjusted) tax-free cash and reduced monthly income.	After the three projections of the pension fund in nominal terms: • The monthly income provided in nominal terms. • The inflation-adjusted monthly income.
Impact of charges and inflation on investment growth	• Reduction in investment growth caused by plan and fund charges. • Additional impact of inflation on real growth. • The additional effect of adviser charges on both the preceding figures.	• Reduction in investment growth caused by plan and fund charges. • The additional effect of adviser charges. • A warning about inflation.

11. In summary, the participants' views were:

Main responses to inflation-adjusted KFIs in experimental styles
Appearance • Approach generated more comment and more engagement with the material itself than other versions. • Very prominent reference to the individual consumer is welcomed. • Visual clutter outweighs benefits of shorter length. • Demonstrates the difference between what consumers say they want and the reality. • Spreading the information over more space may mitigate some of the concerns. • Seen as a modern approach to presenting difficult information. • Colour, layout, headings etc. • Divergent views on the use of coloured shading. • Some saw the possibility for better KFIs if on-line. E.g. rolling over the cursor for pop-up explanations. • There was a desire to see how graphical presentations might work.
Personalisation • Prominent personalisation is important to engage the reader (this is for me) and to reduce the number of assumptions (although there are limits to this).
Structure and logical flow • Want the scene to be set and for contributions to be shown before the projections (the 'bottom line').
Language and content • Once read the new KFIs were better understood than the current example. • The reduction in technical language was welcomed e.g. pension 'pot' preferred to pension fund. Not the dry and dusty approach that is expected. • Main message – the effect of inflation is understood. • Action focused. ◦ You can shop around. • Suggest that good news is given prominence. ◦ Tax free cash sum, tax relief from the government.

12. The insights above were then taken to the next stage of research. We prepared two different presentations of the effect of inflation.

Guiding framework for the approaches taken to the next stage of research

Context

The high level of distrust and poor understanding of pensions and annuities cannot be addressed by a KFI on its own.

- Unrealistic or out-of-date expectations of pension income.
- A flawed belief in the relative worth of alternative investments.
- The low understanding of the concept of deferred pay means that the disappointing figures may dissuade investment.
- Positive pension messages about tax relief are buried or contaminated by disappointing projections.
- Showing the effect of inflation is generally welcomed but the extent (compounding) of it can surprise.
- Intangibility a significant issue. Many uncertainties exist (investment return, inflation, mortality, date of retirement, the cost of an annuity) but cannot be overcome.
- Fear factor surrounding both pensions and inflation may cause denial in the least knowledgeable.
- Better presentation and content means the KFI's role should be clarified to the consumer. Because of previous experience of dull regulated documents, consumers may think an improved KFI is a sales document rather than a regulated disclosure (although they are not sure how to react to this).

Presentation/'pickupability'

- Prominent personalisation reassures and encourages engagement.
- Modernity of presentation aids engagement. Frugal use of colour to aid navigation.
- Use white space, clear headings and sub-headings and short paragraphs.
- Test reaction to, and understanding of, graphs.
- Minimum of three pages, maximum of five.

Structure

- Explain purpose of KFI and how it fits with other documents.
- Put information in natural order.
- Use descriptive headings.
- Try to insert page breaks before major sections – charges, projections, and the effect of charges.

Content

- Explain purpose of each section; in particular the effect of charges.
- Cut down verbiage without compromising clarity/comprehension.
  - Use active (rather than passive) voice and power phrases.
  - Avoid jargon and phrases that are likely to cause confusion.
  - Make every word count, eliminate all redundant words.
  - Do not repeat information contained (or more appropriately contained) in the Key Features document or fund guide.
- Highlight the good news about tax relief (e.g. 'Paid by the government').
- Minimise the figure work.
  - Use real numbers rather than percentages where possible.
- Inflation information can be understood.
  - Particularly when layman's language used, but phrases like 'today's money', 'real terms' or 'buying power' are not necessarily understood without explanation.

Annex 4

Cost benefit analysis for Chapters 3 and 4

Chapter 4 – inflation-adjusted illustrations

1. Our proposals in Chapter 3 are designed to address:

   a) the lack of consistency between our rules and those governing annual SMPIs; and

   b) the need for consumers to understand the impact of inflation on the value of their pension.

Firms affected by the new requirements

2. Our proposals will apply to all product providers providing individual or group personal and stakeholder pension schemes, including SIPP operators and mutual firms. Using the latest Product Sales Data submitted by firms, there are now 132 firms (including SIPP operators) providing new personal pensions.

Direct costs to the FSA

3. We do not expect the FSA to incur any additional costs as a result of these changes.

Compliance costs to firms

4. In 2006, we asked PwC to conduct in-depth research into the costs for making changes to illustrations.[1] We updated some of the figures from this research in the cost benefit analysis for CP11/3, and the feedback from the industry was that the figures derived from the 2006 research, updated for inflation, still held. So, for determining the costs on this occasion, we have also used the 2006 research.

1 PWC, November 2006: Compliance costs of proposed changes to the investment product disclosure regime (www.fsa.gov.uk/pubs/consumer-research/compliance_costs.pdf)

5. Between November 2005 and June 2006, PwC obtained estimates from the industry on the expected costs of replacing the current illustrations with ones expressed in real terms. The average cost per company, updated with actual Consumer Prices Index (CPI) inflation from 2006 to 2011 and forecast 4%pa from 2012 to April 2013, are shown below:

	Average cost per company (£'000)	
	2006	2013
Large company	2,014	2,632
Medium company	690	902
Small company	7.8	10

6. These costs largely relate to the updating of systems, including calculation coding changes as well as the wording and formatting of documents, but also include training and related staff costs as well as management time. Since 2006 some providers have voluntarily added real projections to KFIs in various ways. We have noted that a small number have modernised their software so, in practice, the cost of introducing the new projections may not be as high as indicated.

7. In CP11/3, we asked firms to provide information on the likely costs and benefits to their firm of moving to inflation-adjusted illustrations. Although not many firms responded, the costs derived above were broadly consistent with those that were provided.

8. Our proposals could affect up to 45 providers of personal, stakeholder and group personal pensions, including mutual firms (but excluding SIPP operators). Firms within the same group have been considered as one entity, as this is consistent with the 2006 data and also with how firms typically report cost data to us for policy purposes. However, the 2006 data took account of multiple systems within groups, so these costs are overstated where groups have since rationalised their systems.

Firm size	No. of firms	Cost per firm £'000	Total £'m
Large	6	2,632	15.8
Medium	10	902	9.0
Small	29	10	0.3
Total	**45**		**25.1**

9. These figures exclude SIPP providers, as we believe the cost benefit analysis included in Chapter 2 (covering the introduction of KFIs for SIPPs) is enough to apply to the introduction of inflation-adjusted illustrations. We note that for some providers, there may ultimately be savings if our proposals enable firms to combine their systems for FSA regulated illustrations and SMPIs, as suggested by some respondents to CP11/3. They also do not take account of the savings that arise for firms who choose to use generic projections for Group Personal Pensions.

10. We do not believe that there will be significant ongoing costs for firms, once they have updated their systems to include inflation-adjusted KFIs.

Benefits

11. Our research showed there are two opposing impacts from presenting consumers with inflation-adjusted projections:

a) a better understanding of the impact of inflation may result in more realistic contribution levels and more informed investment risk taking; and

b) some individuals perceived the effect of inflation as an erosion of their pension fund in much the same way as the product and adviser charges. Such individuals may be deterred from purchasing a pension contract if they perceive the benefits to be poor value for money, which may reduce new business for pension providers.

12. Some consumers did not translate their understanding of the impact of inflation to savings and other investments, which they perceived to be better value. This perverse outcome could result in individuals having an even lower income in retirement than the one which would be shown in the proposed illustration. By choosing not to invest in a pension, the individual will lose out on tax relief and possibly employer contributions. Our proposal to require a statement on the KFI for pensions pointing out that inflation reduces the real value of all savings and investments should help to mitigate this risk.

13. The research shows that advisers can mitigate the risk of perverse outcomes. Research participants expected their advisers to talk them through the documents and explain any concepts they did not understand. At the same time, the advisers indicated that inflation-adjusted illustration documents could help them to educate consumers about appropriate levels of contributions and risk taking when investing in a pension.

14. Although there is a risk that pensions could be negatively affected, particularly where there is no adviser, we do not consider that the risk of such misconceptions should prevent the introduction of more helpful pension illustrations.

15. Our proposals will enable consumers to obtain a better understanding of the significant impact of inflation on their investments. This will give them the opportunity to invest more realistic levels of contributions and to appreciate the level of investment risk they should be taking over the long term to try and beat inflation. While shocked and potentially discouraged by the impact of inflation, the research participants felt that this realism was necessary and they may be more likely to review and increase their pension contributions. Our view is that the need for realism outweighs the risk of consumers regarding pensions as poor value for money, and that impact a) above outweighs impact b). This view was shared by advisers.

16. Further, the consistency between pre-sale illustrations and subsequent annual pension statements will reduce confusion and increase consumer engagement. For example, a

consumer will be able to request an illustration for a top-up that they can simply add to their most recent SMPI to see the impact of the top-up.

17. A further advantage of consistency between documents produced under the requirements of different authorities is that it will help to improve consumer confidence and trust in the industry. The current situation where a consumer receives an illustration in monetary terms and then an annual statement which shows much lower figures engenders mistrust.

18. Our research indicated that there would also be benefits to advisers in introducing the new documents. Advisers saw an overlap between the principles in the new document and their current process for explaining the impact of inflation to their clients, and suggested that the new document could aid that process, potentially saving time. Advisers also considered that the document presents more realistic outcomes, which would facilitate discussions about the level of investment risks as well as encouraging more frequent reviews of their clients' pension provision. This would benefit both consumers and advisers.

19. Feedback to previous consultations by us and the FRC has also indicated that pension providers believe these changes will benefit consumers. All respondents to CP11/3 said that there needed to be consistency between point of sale illustrations and annual pension statements. For some firms, this in itself will create efficiencies, as using a consistent basis will allow them to streamline their projection systems.

Chapter 4 – new guidance for product information

20. We consider that there is no compliance cost to the new Handbook guidance on the principles of good practice for KFIs. This guidance is reinforcing Principle 7 of our Principles for Businesses, by showing how firms can make KFIs 'fair, clear, and not misleading'. If firms were to follow best practice and, in particular, reduce the length of KFIs, there could be cost savings due to reduced production costs. As well as the examples shown and tested for this CP, a previous consultation, CP11/3, and the subsequent Policy Statement, PS12/4, indicated how firms could meet the minimum requirements in a way which is consistent with our proposed guidance.

21. The guidance draws on our research for developing KFIs. If it leads to better presented KFIs which influence customers' pension decisions, it should benefit consumers. Documents which are clearer and free of jargon are easier for consumers to engage with and understand. The guidance also clarifies the flexibility available to firms to adapt KFIs for different types of consumers to maximise engagement. In particular, given the intention that clear disclosure of charges can be used support product comparisons, improved presentation of charges has positive market impacts and promotes effective competition. In general, greater clarity in consumer information can also help to improve consumer confidence and trust in the industry.

Annex 5

Compatibility statement

Introduction

1. In this annex we set out our view on how the final rules explained in Chapter 2 and our proposals in Chapters 3 and 4 of this CP are compatible with our general duties under Section 2 of FSMA and our regulatory objectives set out in Sections 3 to 6 of FSMA. We also outline how our proposals are consistent with the principles of good regulation (also in Section 2 of FSMA), to which we must 'have regard'.

Compatibility with our statutory objectives

2. The final rules and proposals outlined in this CP are designed to help us meet our statutory objectives of maintaining confidence in the financial system and securing the appropriate degree of protection for consumers. We do not consider that they have any material impact on our financial crime or financial stability objectives.

Market confidence

3. The final rules and proposals in this CP are intended to ensure that consumers receive appropriate information, which allows them to take informed decisions on their pension provision.

Consumer protection

4. The new requirements for SIPP operators, and the proposals on inflation-adjusted illustrations and presentation of product information are intended to ensure that consumers receive information that is both appropriate and presented in a form that is meaningful to them and easier to understand.

Compatibility with the principles of good regulation

5. Section 2(3) of FSMA requires that, in carrying out our general functions, we have regard to the principles of good regulation.

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

6. The final rules and proposals in this CP build on or update existing requirements, and so do not place onerous new requirements on either firms or supervisors.

The responsibility of those who manage the affairs of authorised persons

7. Our final rules and proposals do not interfere in any way with the responsibilities of senior management, but rather allow firms to adopt an approach that is consistent with their business model and tailored to the needs of their customers.

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

8. We have carried out a CBA for the final rules and proposed rule changes. We are satisfied that the costs of our proposals are proportionate to the benefits.

The desirability of facilitating innovation

9. Our proposals are not expected to hinder innovation, but allow a flexible approach, subject to firms meeting the overarching requirement for communications to be clear, fair and not misleading.

The international character of financial services and markets and the desirability of maintaining the competitive position of the UK

10. We do not consider that these final rules and proposed rule changes will adversely affect the competitive position of the UK.

The need to minimise the adverse effects on competition

11. We do not consider that our final rules and proposals will have a material effect on competition.

The desirability of facilitating competition

12. We do not consider that our final rules and proposals will have a material effect on competition.

Acting in a way that we consider most appropriate for the purpose of meeting our statutory objectives

13. The final rules and proposals in this CP are designed to help us meet our objectives of maintaining confidence in the market and protecting consumers, by ensuring that consumers have appropriate information to be able to take informed decisions on their pension provision, and that they receive this information in a form that they can understand. So, we consider the proposals to be the most appropriate for meeting our statutory objectives.

Annex 6

List of questions for Chapters 3 and 4

Q1: Do you agree with our proposals for presenting projections in real terms? If not, please explain what alternative approach you think is more appropriate.

Q2: Do you agree with our proposals for changing the text relating to the effect of charges table? If not, please explain what alternative approach you think is more appropriate.

Q3: Do you agree that illustrations for drawdown pensions should remain in nominal terms? If not, please explain what alternative approach you think is more appropriate.

Q4: Do you agree that a maximum age of 99 is reasonable for drawdown analyses? If not, what age limit would you suggest and why?

Q5: Do you agree that we should only permit generic illustrations in real terms? If not, please explain what alternative approach you think is appropriate.

Q6: Do you agree with our proposals for alternative projections?

Q7: Do you agree that we should now remove the exemption allowing the intermediate growth rate to be omitted for in-force projections?

Q8: Do you think we should allow for inflation in transfer value analysis reports? Please give your reasons and provide evidence for your views, where possible.

Q9: Do you think we should allow for inflation in annuity quotations? If so, please explain how and give your reasons.

Q10: Do you agree that the proposed change to the wording of COBS 13.6.1R will make this rule clearer?

Q11: Do you have any comments on the cost benefit analysis for Chapter 3?

Q12: Do you have any comments on our proposals to introduce additional guidance on preparing product information?

Q13: Do you have any comments on the cost benefit analysis for the proposed new guidance on preparing product information in Chapter 4?

Appendix 1

Made Handbook text

CONDUCT OF BUSINESS SOURCEBOOK (PENSION SCHEME DISCLOSURE) INSTRUMENT 2012

Powers exercised

A. The Financial Services 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 138 (General rule-making power);
(2) section 156 (General supplementary powers); and
(3) section 157(1) (Guidance).

B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on 6 April 2013.

Amendments to the Handbook

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

Citation

E. This instrument may be cited as the Conduct of Business Sourcebook (Pension Scheme Disclosure) Instrument 2012.

By order of the Board
31 October 2012

Annex

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

13.4.1 R A *key features illustration* must include *appropriate charges information*, information about any interest that will be paid to *clients* on money held within a *personal pension scheme* bank account and, if it is a *packaged product* which is not a *financial instrument*:

(1) must include a *standardised deterministic projection*;

…

…

13.4.4 R There is no requirement under *COBS* 13.4.1R to include a *projection* in a *key features illustration*:

(1) …; or

(2) if the product is~~:~~

~~(a) a *SIPP* from which no *income withdrawals* are being taken; or~~

~~(b)~~ a *life policy* that will be held in a *CTF* or sold with *basic advice* (unless the *policy* is a *stakeholder pension scheme*).

…

13 Annex 2 Projections

This annex belongs to COBS 13.4.1R (Contents of a key features illustration), COBS 13.5.1R (Projections for in-force products) and COBS 13.5.2R (Projections: other situations).

…

G		
2.7	…	
	(7)	If a *personal pension scheme* is invested in assets that are volatile or difficult to value, the *standardised deterministic projection* should be prepared using the best available reasonable assumptions.

…

13 Annex 3 Charges information for a packaged product

(except for a personal pension scheme and a stakeholder pension scheme where adviser charges or consultancy charges are to be facilitated by the product)

This annex belongs to COBS 13.4.1R (Contents of a key features illustration)

R			
Charges			
1	Appropriate charges information		
1.1	*Appropriate charges information* comprises:		
	(1)	(a)	a description of the nature and amount of the *charges* a *client* will or may be expected to bear in relation to the product and, if applicable, any investments within the product;
		(b)	if applicable, a description of the nature and amount of the *adviser charges* a *retail client* has agreed may be taken, including whether it is taken before or after the investment into the product;
	(2)	an 'effect of charges' table; ~~and~~	
	(3)	'reduction in yield' information; and	
	(4)	in relation to a *personal pension scheme*, the amounts (or if the amounts cannot be given, the formula by which the amounts can be calculated), if any, which a *personal pension scheme operator* or *pension scheme* trustee will receive as retained interest in relation to money held within the *personal pension scheme*.	
1.2	…		
1.2A	The information described in 1.1(4) must be disclosed alongside information about any other *charges* the *client* will be expected to bear, and information about any interest that will be paid to *clients* on money held within a *personal pension scheme* bank account.		
Exceptions			
1.3	An effect of charges table and reduction in yield information are not required for:		
	…		
	(2)	~~a *SIPP*~~ [deleted];	
	…		

…

13 Annex 4 Charges information for a personal pension scheme and a stakeholder pension scheme

(where adviser charges or consultancy charges are facilitated by the product)

This annex belongs to COBS 13.4.1R (Contents of a key features illustration)

R			
Charges			
1	Appropriate charges information		
1.1	*Appropriate charges information* comprises:		
	(1)	(a)	a description of the nature and amount of the *charges* a *client* will or may be expected to bear in relation to the product and, if applicable, any investments within the product;
		(b)	if applicable, a description of the nature and amount of the *adviser charges* and *consultancy charges* a *retail client* or employer has agreed may be taken before investment into the product;
		(c)	if applicable, a description of the nature and amount of the *adviser charges* and *consultancy charges* a *retail client* or employer has agreed may be taken after investment into the product;
	(2)	an 'effect of charges' table; ~~and~~	
	(3)	'reduction in yield' information; and	
	(4)	in relation to a *personal pension scheme*, the amounts (or if the amounts cannot be given, the formula by which the amounts can be calculated), if any, which a *personal pension scheme operator* or *pension scheme* trustee will receive as retained interest in relation to money held within the *personal pension scheme*.	
1.2	…		
1.2A	The information described in 1.1(4) must be disclosed alongside information about any other *charges* the *client* will be expected to bear, and information about any interest that will be paid to *clients* on money held within a *personal pension scheme* bank account.		
…			

The provision rules

14.2.1 R A *firm* that sells:

…

(3) the variation of a *life policy* or *personal pension scheme* to a *retail client*, must provide that *client* with sufficient information about the

variation for the *client* to be able to understand the consequences of the variation ~~(unless the policy or scheme is a *SIPP*)~~;

…

on condition that it complies with each of the other *rules* in this section in relation to the provision of the document, as if references in those *rules* to a "*key features document*" or "*simplified prospectus*" were a reference to the "NURS KII document".

Appendix 2

Draft Handbook text

Appendix 2

CONDUCT OF BUSINESS SOURCEBOOK (KEY FEATURES ILLUSTRATIONS FOR PERSONAL PENSIONS) (AMENDMENT) INSTRUMENT 2012

Powers exercised

A. The Financial Services 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 138 (General rule-making power);
(2) section 145 (Financial promotion rules);
(3) section 156 (General supplementary powers); and
(4) section 157(1) (Guidance).

B. The rule-making powers listed above are specified for the purposes of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force as follows:

(1) Part 1 of the Annex to this instrument comes into force on 6 April 2014;

(2) Part 2 of the Annex to this instrument comes into force on 6 April 2013.

Amendments to the Handbook

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

Citation

E. This instrument may be cited as the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012.

By order of the Board
[*date*]

Annex

Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

The text below is based on the text of COBS 13 as consulted on in CP 12/05 as if the changes published in that CP had been made by the Board.

Part 1: Comes into force on 6 April 2014

13.2 Product information: production standards, form and contents

13.2.1 G …

13.2.1A G When a *firm* prepares *documents* or information for a *life policy*, *personal pension* or *stakeholder pension* in accordance with this chapter, the *firm* should:

(1) consider the *rules* on communicating with clients (*COBS* 4). Those *rules* require a *firm* to ensure that a communication is fair, clear and not misleading. In particular, a *firm* should:

(a) take into account its target market's understanding of financial services when preparing *documents* and information;

(b) present information in a logical order;

(c) use clear and descriptive headings, and where appropriate, sub-headings to aid navigation;

(d) where possible, avoid the use of jargon, unfamiliar or technical language and use plain language;

(e) if it is necessary to use jargon, unfamiliar or technical language, provide accompanying explanations in plain language;

(f) use short sentences;

(g) (if the *key features illustration* is separate from the *key features document*) clearly cross-reference between the two and avoid duplication where possible; and

(h) concentrate on key product information, avoiding unnecessary duplication of background or reference information, disclaimers and information about the application process; and

(i) taking into account the means of printing or display.

(2) consider whether the following can be used to improve the *client's* understanding of the product, in particular:

(a) design devices such as side annotations, shading, colour, bulleted lists, tables and graphics; and

(b) the type size, line width, line spacing, and use of white space.

…

13.2.3 G The *Consolidated Life Directive information* can be included in a *key features document*, a *key features illustration* or any other *document*.

…

13.4 Contents of a key features illustration

13.4.1 R A *key features illustration* must include *appropriate charges information*, information about any interest that will be paid to *clients* on money held within a *personal pension scheme* bank account and, if it is a *packaged product* which is not a *financial instrument*:

(1) must include a *standardised deterministic projection*;

(2) the projection and charges information must be consistent with each other so that:

(a) a *projection* in nominal terms is accompanied by an effect of charges table and reduction in yield information in nominal terms; and

(b) a *projection* in real terms is accompanied by an effect of charges table and reduction in yield information in real terms;

(3) it may also include ~~*alternative*~~ *stochastic projections* if there are reasonable grounds for believing that a *retail client w*ill be able to understand the *stochastic projection* except that the most prominent *projection* must be a *standardised deterministic projection*.

…

13.5 Preparing product information: other projections

Projections for in-force products

13.5.1 R A *firm* that communicates a *projection* for an in-force *packaged product* which is not a *financial instrument*:

(1) must include a *standardised deterministic projection*;

(2) may also include ~~an *alternative*~~ a *stochastic* *projection* except that the most prominent *projection* must be a *standardised deterministic projection*; and

must follow the *projection rules* in *COBS* 13 Annex 2.

Projections: other situations

13.5.2 R A *firm* that communicates a *projection* for a *packaged product* which is not a *financial instrument*~~,~~:

(1) for which a *key feature illustration* is not required to be provided; and

(2) which is not an in-force *packaged product*;

must ensure that such a *projection* is either a *standardised deterministic projection* or ~~an *alternative*~~ a *stochastic* *projection* in accordance with *COBS* 13 Annex 2.

…

13.5.4 G The general requirement that communications be fair, clear and not misleading will nevertheless mean that a *firm* that elects to comply with the future performance rule in *COBS* 4.6.7R will need to explain how the combined *projection* differs from other information that has been or could be provided to the client, including a *projection* provided under the *projection rules* in *COBS* 13.4, *COBS* 13.5 and *COBS* 13 Annex 2, and in particular, the *firm* should identify where a *projection* in real terms is required under *COBS* 13.

…

13.6 Preparing product information: changes to adviser and consultancy charges

13.6.1 R A *firm* that agrees to start facilitating the payment of an *adviser charge* or *consultancy charge*, or an increase in such a charge, from an in-force *packaged product*, must prepare sufficient information for the *retail client* to be able to understand the likely effect of that facilitation, in good time before ~~that information has to be provided~~ it takes effect.

…

13 Annex 2 Projections

…	
R	
1.2	Calculating projections: additional requirements for a pension scheme

(1)	A *standardised deterministic projection* within a *key features illustration* for a *personal pension scheme* or *stakeholder pension scheme* must ~~include or~~ be in real terms and be accompanied by information explaining ~~the impact of inflation on those benefits~~ why price inflation has been taken into account and that price inflation reduces the worth of all savings and investments.		
(2)	~~Where a *firm* chooses to provide that information required in (1) in the form of one or more *projections* of benefits, it must include a~~ A *projection* in real terms~~, so long as it~~ must be ~~either~~ calculated using:		
	~~(a)~~	~~calculated using:~~	
	(a)	~~(i)~~	the appropriate *lower*, *intermediate* and *higher* ~~*rate*~~ *rates of return*;
	(b)	~~(ii)~~	the intermediate rate of price inflation, in accordance with *COBS* 13 Annex 2 2.5R; and
	(c)	~~(iii)~~	an annuity calculated in accordance with *COBS* 13 Annex 2 3.1R~~; or~~.
	~~(b)~~	~~consistent with the *statutory money purchase illustration* assumptions, with any material differences between the assumptions used and those otherwise required for accompanying *standardised deterministic projections* explained.~~	
(3)	A *standardised deterministic projection* for a *personal pension scheme* or *stakeholder pension scheme* must show only the numeric value of the three real rates of return after the appropriate price inflation assumption has been taken into account, that is, the real rate of projected growth which has been applied to the real value of the contributions, and must not show the nominal rates of return.		

G		
1.2A	A *projection* in real terms may be calculated by either:	
	(1)	accumulating the nominal value of the contributions at the appropriate rates of return and discounting the resulting value of the fund using the intermediate rate of price inflation; or
	(2)	accumulating the real value of the contributions (calculated using the appropriate rate of price inflation) at the appropriate rates of return after price inflation has been taken into account.

R			
1.3	(1)	…	
	(2)	A *projection* prepared on that basis may omit ~~benefits in nominal terms~~ projections at the *lower* and *higher rates of return* and only show a range of figures at the *intermediate rate of return*, of benefits in real terms.	
…			
R			
~~Calculating~~ Providing ~~an alternative~~ a stochastic projection			
1.5	~~An *alternative*~~ A *stochastic* *projection* must only be used if:		
(1)	~~(if the *alternative projection* is not a *stochastic projection*) not exceed the *higher rate of return*;~~ [deleted]		
(2)	~~(if the *alternative projection* is not a *stochastic projection*), use assumptions consistent with the assumptions which apply to *standardised deterministic projections* in this Annex, unless the reasons for any inconsistency are:~~		
	~~(a)~~	~~reasonable;~~	
	~~(b)~~	~~explained to a *retail client*, with enough information for the *retail client* to be able to understand the difference between the *alternative projection* and any *standardised deterministic projection* being provided; and~~ [deleted]	
(3)	~~(if the *alternative projection* is a *stochastic projection*) only be used if:~~		
	~~(a)~~	there are reasonable grounds for believing that a *retail client* will be able to understand it;	
(4)	~~(b)~~	it is based on a reasonable number of simulations and assumptions (including the impact of price inflation for *personal pension schemes* and *stakeholder pensions schemes*) which are reasonable and supported by objective data; and	
(5)	~~(c)~~	~~the *alternative projection*~~ it is accompanied by enough information for the *retail client* to be able to understand the difference between the ~~*alternative*~~ *stochastic* *projection* and any *standardised deterministic projection* being provided.	

G	
1.6	~~An *alternative*~~ A *stochastic projection* may be used either as part of a *key features illustration* or separately. However, it must not detract from any *standardised deterministic projection* required by *COBS* 13.4.1R or *COBS* 13.5.1R.
…	
R	
1.10	~~A standardised deterministic projection for an existing business *personal pension scheme* or *stakeholder pension scheme* may not omit the projection at the *intermediate rate of return*.~~ [deleted]

R			
2	Assumptions to follow when calculating projections		
…			
R			
Additional requirements: drawdown pensions			
2.9	(1)	…	
	(2)	A *standardised deterministic projection* for a *drawdown pension* must be based on an assumption that the current gilt-index yield will continue to apply throughout the relevant term and include:	
		…	
		(d)	(under the heading 'What the benefits might be'), the amount of income and the projected value of the fund at each fifth anniversary for the *lower, intermediate* and *higher rate of return* for as long as the fund is projected to exist at the *higher rate of return* or to age 99 if earlier;
		…	

R			
Drawdown Pension: Exception			
2.10	A *standardised deterministic projection* for a *drawdown pension* can be prepared in nominal terms, rather than real terms.		
…			
R			
5	~~How to present a projection~~ Projections: accompanying statements and presentation		
5.1	A *standardised deterministic projection* must be accompanied by:		
	(1)	appropriate risk warnings, including warnings about volatility and the impact of inflation and that the product may pay back less than paid in (if that could be the case), ~~the relationship between figures in real terms and those in nominal terms~~, and the degree to which any figures can be relied upon; and	
	(2)	a statement:	
		(a)	~~that *projection* rates are standardised or an explanation that *projection* rates that are lower than the standard rates have been used and why;~~ [deleted]
			…
		(d)	that increases in contributions have been assumed (if that is the case), together with sufficient information for a *retail client* to be able to understand the nature and magnitude of the assumed increases; ~~and~~
		(e)	of the sum of any actual *premiums* charged for any rider benefits or increased underwriting risks (where these have been charged); and
		(f)	(for *personal pension schemes* and *stakeholder pension schemes*) of the assumptions used to calculate the regular income and that the *client* may choose when to take this income (if that is the case).
5.1A	When presenting a *standardised deterministic projection* a *firm* must:		
	(1)	include a short introductory explanation of what the *projection* seeks to illustrate;	
	(2)	use a descriptive heading such as ‘What your regular income might	

		be worth in future or ‘What might I get back from my plan?’;
	(3)	place the *projection* and the associated explanation adjacent to each other on the same page; and
	(4)	explain that the *client* will be sent annual statements which will allow them to keep track of their benefits.

13 Annex 3 Charges information for a packaged product

(except for a personal pension scheme and a stakeholder pension scheme where adviser charges or consultancy charges are to be facilitated by the product)

This annex belongs to *COBS* 13.4.1R (Contents of a key features illustration)

R			
Charges			
…			
Exceptions			
1.3	An effect of charges table and reduction in yield information are not required for:		
	…		
	(4)	a *stakeholder product* or a product that will be held in a *CTF* where the relevant product and the *CTF* levy their *charges* annually, if the following is included instead: "There is an annual charge of y% of the value of the funds you accumulate. If your fund is valued at £250 throughout the year, this means we ~~deduct~~ charge [£250 x y/100] that year. If your fund is valued at £500 throughout the year, this means we ~~deduct~~ charge [£500 x y/100] that year. [After ten years these deductions reduce to [£250 x r/100] and [£500 x r/100] respectively.]" where 'y' is the annual charge and 'r' is the reduced annual charge (if any).	
…			

R		
2	Effect of charges table	
2.1	Each 'effect of charges' table must be accompanied by, or refer to:	
	(1)	a statement that all relevant guarantees have been taken into account (if there are any);
	(2)	~~a warning that one effect of the *charges* referred to is that a *retail client* could get back less than they invest (if that is the case); and~~ [deleted]
	(3)	the rate of return (for *personal pension schemes* and *stakeholder pension schemes*, this must be the rate of return net of price inflation) used to calculate the figures in the table;
	(4)	an explanation of the purpose of the table, and what the table shows;
	(5)	a statement that the table and reduction in yield information can be used to compare charges with other *stakeholder pension schemes* and *personal pension schemes*.

2.2	The effect of charges table:		
	(1)	for a *life policy* must be in the following form unless the *firm* chooses to adopt the form of the effect of charges table in *COBS* 13 Annex 4; and	
	(2)	(for a *personal pension scheme* or *stakeholder pension scheme*) must be in the following form and the figures are shown in real terms:	
…			

(3)	must be completed in accordance with the following notes:	
…		
Note 4	This column is optional. If it is retained, it must show the total actual deductions to the end of each relevant year calculated using the following method:	
	(a)	apply the *intermediate rate of return*, after price inflation for a *projection* in real terms, for the relevant product to the figure in the 'effect of deductions to date' column for the previous year;

	…	
…		
Note 6	This column must show the *standardised deterministic projection* of the surrender value, cash-in value or transfer value, calculated in accordance with the *rules* in *COBS* 13 Annex 2 (Projections) at the appropriate *intermediate rate of return*, after price inflation for a *projection* in real terms, to the end of each relevant year.	

R		
Exception		
2.3	An effect of charges table may be amended, but only ~~if and to the extent that~~:	
	(1)	if it is necessary to properly reflect the nature and effect of, for example, the *adviser charges*, *consultancy charges* or the *charges* inherent in a particular product; or
	(2)	to ensure that the column labels and any explanatory text reflect the nature of the contract;
	(3)	to ensure consistency with the terminology used in relation to a particular product; or
	4)	to give the effect of charges table an appropriate title, for example, 'How charges and price inflation reduce the value of your plan'.

G		
2.4	~~The effect of 2.3R is that, for example, the column labels and explanatory text may be adjusted to reflect the nature of the contract.~~ [deleted]	
…		
R		
3	Reduction in yield	
3.1	Reduction in yield ('A') is 'B' less 'C' where:	
	(1)	'B' is the *intermediate rate of return* (*for personal pension schemes* and *stakeholder pension schemes*, net of price inflation) for the relevant product; and

	…		
3.2	A *firm* must present reduction in yield as 'A%', as part of a statement which explains that 'charges ~~and expenses~~ have the effect of reducing ~~your anticipated returns~~ <u>the investment growth (after price inflation for personal pension schemes and stakeholder pension schemes)</u> from 'B%' to 'C%', or in some other appropriate way.		
…			

13 Annex 4 Charges information for a personal pension scheme and a stakeholder pension scheme

(where adviser charges or consultancy charges are facilitated by the product)

This annex belongs to *COBS* 13.4.1R (Contents of a key features illustration)

…		
Exception		
1.2	An effect of charges table and reduction in yield information are not required for a *stakeholder pension scheme*, where *adviser charges* or *consultancy charges* are not being facilitated by the scheme, if the following is included instead: "There is an annual charge of y% of the value of the funds you accumulate. If your fund is valued at £500 throughout the year, this means we ~~deduct~~ <u>charge</u> [£500 x y/100] that year. If your fund is valued at £7500 throughout the year, we will ~~deduct~~ <u>charge</u> [£7500 x y/100] that year."	
…		
R		
2	Effect of charges table	
2.1	Each effect of charges table must be accompanied by:	
	(1)	an explanation of what the table shows;
	(2)	a statement that all relevant guarantees have been taken into account (if there are any);
	(3)	~~a warning that one effect of the *charges* referred to is that a *retail client* could get back less than they invest (if that is the case); and~~ <u>[deleted]</u>
	(4)	the rate of return <u>after price inflation</u> used to calculate the figures in the table<u>; and</u>

	(5)	a statement that the effect of charges table and reduction in yield information can be used to compare *charges* with other *stakeholder pension schemes* or *personal pension schemes*.
2.2	~~Subject to Note 2 below, an~~ An effect of charges table must be in the following form and calculated using a rate of return after price inflation:	

Note 1	Note 2	Note 3	Note 4	Note 5	Note 6
At end of year	~~Total paid in to date~~ The payments into your plan	Withdrawals	~~If there were no~~ Before charges are taken	If only ~~product~~ plan and investment charges are taken	After all charges are taken from this plan
	£	£	£	£	£
1					
…					
5					
At age [xx]					

Note 1	…
Note 2	This column ~~is optional. If it is retained it~~ must show in real terms the cumulative contributions paid to the end of each relevant year.
Note 3	…
Note 4	This column must show a *standardised deterministic projection* of the benefits, calculated in accordance with the rules in *COBS* 13 Annex 2 (Projections) at the appropriate *intermediate rate of return*, taking price inflation into account, to the end of each relevant year, but without taking any *charges* into account.
Note 5	This column must show a *standardised deterministic projection* of the benefits, calculated in accordance with the rules in *COBS* 13 Annex 2 (Projections) at the appropriate *intermediate rate of return*, taking price inflation into account, to the end of each relevant year, but taking into account only the charges described in *COBS* 13 Annex 4R paragraph 1.1(1)(a).

Note 6	This column must show a *standardised deterministic projection* of the benefits, calculated in accordance with the *rules* in *COBS* 13 Annex 2 (Projections) at the appropriate *intermediate rate of return*, taking price inflation into account, to the end of each relevant year taking into account all charges described in *COBS* 13 Annex 4R paragraph 1.1(1)(a) and (c). …

R		
Exception		
2.3	An effect of charges table may be amended, but only ~~if and to the extent that~~:	
	(1)	if it is necessary to properly reflect the nature and effect of, for example, the *adviser charges*, *consultancy charges* or the *charges* inherent in a particular product; or
	(2)	to ensure that the column labels and any explanatory text reflect the nature of the contract;
	(3)	to ensure consistency with the terminology used in relation to a particular product; or
	4)	to give the effect of charges table an appropriate title, for example, 'How charges and price inflation reduce the value of your plan'.

G	
2.4	~~The effect of *COBS 13 Annex 4* paragraph 2.3R is that, for example, the column labels and explanatory text may be adjusted to reflect the nature of the contract or the terminology used.~~ [deleted]

R		
3	Reduction in yield	
3.1	Product reduction in yield ('A') is 'B' less 'C' where:	
	(1)	'B' is the *intermediate rate of return* net of price inflation for the relevant product; and

	…	
3.2	Total reduction in yield ('D') is 'B' less 'E' where:	
	(1)	'B' is the *intermediate rate of return* net of price inflation for the relevant product; and
	…	
3.3	(1)	A *firm* must present the product reduction in yield as 'A%', as part of a statement which explains that 'product charges reduce ~~your anticipated rate of returns~~ the investment growth after price inflation from 'B%' to 'C%'', or in some other appropriate way.
	(2)	If *adviser charges* or *consultancy charges*, or both *adviser charges* and *consultancy charges* are to be facilitated by the product, a *firm* must also present the reduction in yield as 'D%', as part of a statement which explains that 'all charges reduce ~~your anticipated rate of returns~~ the investment growth after price inflation from 'B%' to 'E'%'', or in some other appropriate way and explain the difference between the two reduction in yield figures.
…		

Part 2: Comes into force on 6 April 2013

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 provisions: coming into force**
…					
2.5-A	*COBS* 13.4.1R	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to	From 6 April 2013 to 5 April 2014	6 April 2014

			the *Handbook* set out in that instrument were in force.		
2.5D	*COBS* 13.5.1R	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to the *Handbook* set out in that instrument were in force.	From 6 April 2013 to 5 April 2014	6 April 2014
2.5E	*COBS* 13.5.2R	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to the *Handbook* set out in that instrument were in force.	From 6 April 2013 to 5 April 2014	6 April 2014
2.5F	*COBS* 13 Annex 2	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to the *Handbook* set out in that instrument were in force.	From 6 April 2013 to 5 April 2014	6 April 2014
2.5G	*COBS* 13 Annex 3	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to the *Handbook* set out in that instrument were in force.	From 6 April 2013 to 5 April 2014	
2.5H	*COBS* 13 Annex 4	R	A *firm* may comply with the provision listed in column (2) as amended by the Conduct of	From 6 April 2013 to 5 April	

			Business Sourcebook (Key Features Illustrations for Personal Pensions) (Amendment) Instrument 2012 as if the amendments to the *Handbook* set out in that instrument were in force.	2014	

Appendix 2A

Designation of Handbook Provisions

FSA Handbook provisions will be 'designated' to create a FCA Handbook and a PRA Handbook on the date that the regulators exercise their legal powers to do so. Please visit our website for further details about this process.

We plan to designate the Handbook Provisions which we are proposing to create and/or amend within this Consultation Paper as follows:

Handbook Provision	Designation
COBS 13.2, 13.4, 13.5, 13.6	FCA
COBS 13 Annexes 2, 3, 4	FCA
TP 2.5A, 2.5D, 2.5E, 2.5F, 2.5G, 2.5H	FCA

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