MS16/1.3: annex 2

Retirement Outcomes Review

Final report: annex 2: Regulatory developments in the market

June 2018

1. In this annex we provide details on recent regulatory changes and developments in the pensions and retirement income market. We believe that these developments will have a positive effect on the market, and many of them support our work on ROR. We have considered these changes in developing our proposed remedies.

2. We grouped these changes and developments into:

- policy, supervision and competition work; and
- other developments in the pensions market

Policy, supervision and competition work

Review of non-advised drawdown sales

3. The FCA undertook a Thematic Review to assess whether providers are providing necessary information, at the right time and in a format that enables consumers to make informed decisions when accessing retirement benefits. We also wanted to understand whether consumers are receiving adequate on-going information to help them decide if drawdown continues to meet their retirement income needs.

4. We assessed non-advised drawdown sales for a number of providers since the introduction of Pension Freedoms in April 2015 up to April 2017.

5. Based on our review, we found that providers generally provide sufficient information to enable consumers accessing pension benefits on a non-advised basis to make informed decisions.

6. Despite this, we found that some consumers appear not to be fully engaging with the information and are therefore potentially putting themselves at risk of harm, particularly:

   - Many consumers are now choosing to access their benefits ahead of their intended retirement date. They appear to have already made the decision to enter drawdown before contacting providers. This means that some consumers appear not to be open to exploring the full range of options available to them. This includes shopping around for other decumulation options.
   - Consumers have often not thought about the investment choices of drawdown. This is particularly the case when their main aim is to access their tax-free cash only, without taking any immediate income. As a result, we have seen some consumers remain in low-risk assets after following lifestyling[1] strategies. We have seen others stay in cash funds because they have had to enter into a new contract[2] to access drawdown. Both these options increase the risk of consumers running out of money in retirement, or having less money than they were expecting.

7. We have provided feedback to all providers that participated in the review. Individual providers have been asked to review aspects of their non-advised sales processes, and in some instances elements of their training, to ensure that improvements are made.

[1] Lifestyling is an investment option designed to lock in investment growth as customers near retirement age. It involves moving from riskier assets into less risky investments as customers approach retirement.

[2] Most customers of life companies transferred into a new product with the same provider to access pension savings, whereas SIPP customers either transferred to a new SIPP provider or accessed benefits via their existing SIPP.

Platforms market study

8. Investment platforms are increasingly used by consumers and financial advisers to access retail investment products and to manage investments. The platform market has steadily grown over the last 8 years, with Assets under Administration for both adviser and direct platforms increasing from £108 billion in 2008 to £592 billion in 2016.

9. Many platforms offer investors and their advisers a range of information and tools to help them make investment decisions and some also offer their own investment products. As part of the study, we explore whether platforms help investors make good investment decisions and whether their investment solutions offer investors value for money.

10. The study looks at both investment platforms and providers that provide similar services by allowing investors or their advisers to access retail investment products through an online portal.

11. This Market Study follows on from the Asset Management Market final report published in June 2017, which highlighted a number of potential competition issues in the platforms sector.

12. Some consumers use platforms to make their pensions investments and the findings and conclusions of this study will affect the sector.

Competition in non-workplace pensions

13. In February 2018 we published a Discussion Paper[3] on 'effective competition in non-workplace pensions'[4], through which we sought to understand whether:

- competition is working well in the market for non-workplace pensions; and
- there is a need to go further to protect consumers

14. We asked all interested parties to provide their views and evidence about:

- the factors that influence the behaviour of consumers and providers; and
- whether the current market dynamics ensure fair outcomes for consumers

15. Following the feedback we received, we are conducting further diagnostic work: we are conducting empirical research to help us understand the issues from a consumer perspective and will issue a data request to pension providers concerning their products and customers.

16. ROR sought feedback from stakeholders regarding remedies in relation to drawdown which will apply irrespective of whether the consumer accumulated their pensions savings via workplace or non-workplace pensions.

Amends to the perimeter guidance manual

17. The Financial Advice Market Review (FAMR) found that providers were unclear on whether certain activities might amount to a personal recommendation and were

[3] DP18/1 - Effective competition in non-workplace pensions; www.fca.org.uk/publication/discussion/dp18-01.pdf

[4] 'Non-workplace pensions' is an umbrella term we are using to represent individually arranged contract-based DC pensions, most commonly individual personal pensions, stakeholder personal pensions, and self-invested personal pensions. It is a large and significant market, which serves a diverse group of people.

therefore reluctant to offer services that might benefit consumers because of the risk involved.

18. To address this concern, the FCA published an amended Perimeter Guidance Manual (PERG) in January 2018. This includes an explanation of our views as well as a number of examples based on areas of uncertainty highlighted by providers to help providers better understand the principles that determine whether or not a service amounts to a personal recommendation.

19. Notably, it clarifies that presenting a product in a way which links it to a particular investment objective, as we envisage 'pathways' will, need not be a personal recommendation in itself.

20. We hope that this clarity that PERG brings will alleviate providers' concerns about inadvertently making a personal recommendation, and will result in an increase in innovation in the market, to the benefit of consumers. We will continue to monitor how innovation develops in the market.

Advising on pension transfers

21. There has been an increase in demand in recent years for pension transfer advice, primarily for transfers from DB to DC pension schemes. Transferring from a pension which has safeguarded benefits (primarily DB pensions) to one without them is an important decision for consumers to take. It is the view of the FCA that DB pensions offer valuable benefits and most people will benefit from keeping them.

22. Given this, we wanted to ensure that those providing regulated financial advice fully consider the client's circumstances and properly consider the various options available to them.

23. To protect consumers, since April 2016, legislation sets out that 'appropriate independent advice'[5] is mandatory for anyone looking to transfer safeguarded benefits worth over £30,000.[6]

24. We have been closely monitoring advice provided on DB to DC transfers and have assessed a number of DB transfer cases where the recommendation was to transfer. We found that a considerable proportion of advice was unsuitable.[7]

25. Based on our supervisory work, and in light of recent developments in the pensions market, we therefore consulted on changes to our rules and guidance on how advice should be provided to consumers on pension transfers (CP17/16).[8] This was published in June 2017. Following this consultation we published a Policy Statement (PS18/6) in March 2018.[9]

26. The Policy Statement introduced new rules and guidance aimed at providing advisers with a framework which better enables them to give good quality advice. This will help

[5] S48 of the Pension Schemes Act 2015 requires trustees and managers of to check that appropriate independent advice has been taken before a transfer or conversion of safeguarded benefits is made. Appropriate independent advice is further defined in The Pension Schemes Act 2015 (Transitional Provisions and Appropriate Independent Advice) Regulations 2015.

[6] The DWP consulted on this advice limit in late 2016, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/555564/consultation-valuing-pensions-for-the-advice-requirement-and-introducing-new-consumer-protections.pdf

[7] In 17% of the cases, the recommendation to transfer to a DC scheme was unsuitable and in 36% of the cases it was unclear whether the recommendation was suitable or not.

[8] CP17/16: Advising on Pension Transfers, www.fca.org.uk/publication/consultation/cp17-16.pdf

[9] PS18/6: Advising on Pension Transfers – feedback on CP17/16 and final rules and guidance www.fca.org.uk/publication/policy/ps18-06.pdf

consumers make better informed decisions. Given the significant proportion of unsuitable advice we have seen, we are maintaining our guidance that an adviser should start from the assumption that a transfer will be unsuitable. The existing guidance on the starting assumption does not, however, prevent an adviser from recommending a transfer where this can be demonstrated to be suitable for the consumer.

27. Following on from CP17/16, we issued a further consultation paper in March 2018 (CP18/7).[10] This consulted on a number of topics raised by responses to various discussion questions in CP17/16, along with a number of new issues that were raised. CP18/7 also asks discussion questions about adviser charging structures and whether restrictions should be applied to them.

28. Our intention is that outcomes for consumers who transfer from DB to DC pension schemes are improved through improving the quality of advice on pension transfers and increasing adviser confidence in our expectations.

29. Consumers who do transfer from DB to DC schemes and go into drawdown will benefit from the remedies we are considering in the Retirement Outcomes Review. Many of these consumers will have no or limited experience in financial investments, particularly as their DB pots were managed for them, and therefore our proposed remedies would be useful in ensuring that they make good decisions.

Implementing information prompts in the annuity market

30. Our Retirement Income Market Study (RIMS), published in March 2015, found that competitive discipline in the annuity market has weakened. Our interim report confirmed this view and identified that a significant proportion of annuity sales are still being made to providers' existing customers, which suggests low levels of switching and competitive pressure.

31. RIMS proposed to address this competition issue by requiring providers to provide a quotation comparison to consumers looking to buy an annuity. This would help consumers who decided to buy an annuity to easily identify whether they could be getting a better deal by shopping around, and thereby increase the competitive pressure.

32. We commissioned consumer behavioural research to test how this information prompt could work in practice, and sought feedback on our proposals in November 2016.[11] In May 2017 we set out our final rules[12] which require providers to inform consumers how much they could gain from shopping around and switching provider, before they buy an annuity. The rules came into force on 1 March 2018.

33. While the number of consumers purchasing annuities has decreased following the introduction of the pension freedoms in April 2015, the market for annuities remains significant, and improving competition in it remains an important objective for the FCA.

34. In addition to these measures, we are also consulting on making changes to some of these rules to increase awareness of enhanced annuities, and ensure that these rules also apply to income-driven quotes. These follow our thematic review of annuities sales

[10] CP18/7: Improving the quality of pension transfer advice, www.fca.org.uk/publication/consultation/cp18-07.pdf

[11] CP16/37: Implementing information prompts in the annuity market, www.fca.org.uk/publication/consultation/cp16-37.pdf

[12] PS17/12: Implementing information prompts in the annuity market, www.fca.org.uk/publication/policy/ps17-12.pdf

practices (TR16/7) which found that some providers were not making consumers aware of the availability of enhanced annuities.

Transaction cost disclosure in workplace pensions

35. Since January 2018 our rules have required FCA regulated firms managing money on behalf of DC workplace pension schemes to:

- disclose administration charges and transaction costs to the governance bodies of those schemes, in response to a request; and
- require firms to calculate transaction cost information using a standard approach, and to obtain information from other firms where they do not hold it themselves

36. The availability of consistent and comparable information enables governance bodies of these schemes to better meet their obligations to review and consider the value for money of transaction costs and administration charges.

37. We have also been working with the Department for Work and Pensions (DWP) on the publication and disclosure of the costs and charges information to members of occupational pension schemes. Their final regulations were laid on 26 February 2018 and we will consult on our proposals to achieve similar outcomes for workplace personal pension schemes in the second quarter of 2018.

38. These measures, together with our proposed measures to increase prominence of charges (see chapter 5), should increase the prominence of charges and value for money in pensions.

Other developments in the pensions market

The FCA and TPR's strategy for pensions

39. The Financial Conduct Authority (FCA) and The Pensions Regulator (TPR) work in tandem to address risks and harms in the pensions and retirement income sector. We are working together to develop a joint pensions strategy which will look at how we will work over the next five to ten years to tackle the risks we see facing the sector.

40. On Monday, 19 March 2018 we published a Call for Input. The feedback we received from this Call for Input, and from supporting stakeholder engagement events, will inform our final strategy document, which we intend to publish later this year.

Automatic enrolment review

41. Automatic enrolment aims to enable and encourage people to save for their retirement. The legislation requires employers to provide their employees with the option of joining a workplace pension scheme, and sets minimum contributions into the scheme for both the employee and the employer.

42. It was introduced by government in 2012, and was rolled out in stages, initially only applying to larger employers. In 2018 the roll-out will be complete and will apply to all employers. With the aim of getting people to save more, minimum contributions are also being changed gradually, from 2% of earnings initially to 5% from April 2018, going up to 8% of earnings from April 2019 onwards.

43. DWP conducted a review of automatic enrolment, and published its report in December 2017.[13] The review identified three key strategic problems:

- current saving levels risk a significant proportion of the working-age population not meeting their retirement expectations
- there are significant gaps in pension coverage for a large proportion of the self-employed
- individuals are beginning to save but for multiple reasons do not actively engage with their pensions

44. It set out a number of measures that government aims to implement in the mid-2020s, including:

- lower the age criteria from 22 to 18, thereby getting people to save from an earlier age
- remove the lower earnings limit of £5,876 (in 2017/18), so that pension contributions are calculated from the first pound earned
- work to identify the most effective options to increase pension saving among self-employed people
- take measures, together with industry, to increase consumer engagement with pensions

45. Our ROR interim report found that most DC pots are currently relatively small, and that their size often determined how people treated them too. Automatic enrolment is likely to result in much more money going into workplace pensions[14], and all the more so once the new measures are introduced in the future. This would make these DC pots much more significant for consumers and the pensions industry alike.

Single Financial Guidance Body Act

46. The new Single Financial Guidance Body (SFGB) will bring together the Money Advice Service, The Pensions Advisory Service, and Pension Wise to provide debt advice, money guidance and pensions guidance. The new body will simplify the existing public financial guidance landscape, making it easier for people to access information and guidance to help them make effective financial decisions.

47. In June 2017 the Government introduced the Financial Guidance and Claims Bill in the House of Lords. Royal Assent was given in May 2018 and the Government anticipates that the SFGB will be launched no earlier than autumn 2018.

48. The new body will be funded in the same way that MAS, The Pensions Advisory Service (TPAS) and Pension Wise have been funded – from levies on the financial services industry (the financial services levy) and pension schemes (the general levy on pension schemes).

49. The measures we are taking through our final report aim to improve uptake of guidance and we will also be working closely with the guidance body to operationalise a drawdown comparison tool.

[13] Automatic Enrolment Review 2017: Maintaining the Momentum, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/668971/automatic-enrolment-review-2017-maintaining-the-momentum.PDF

[14] DWP estimates that by 2019/20 an extra £20 billion a year will be saved as a direct result of automatic enrolment.

The Pensions Dashboard

50. Since October 2017, the Department for Work and Pensions has been leading the work to develop and launch a pensions dashboard. The FCA supports this initiative. It was a key recommendation from both RIMS (March 2015) and FAMR (March 2016).[15]

51. With people working for an average 11 employers during their working life, it is increasingly important to help people better understand their accumulated pension wealth across their multiple pension pots. Being able to see information about all their pensions savings in one place, would greatly help consumers to understand the total amount they have accumulated. This in turn would help them make more informed decisions and aid with retirement planning.

52. We think a pensions dashboard can help. It has the potential to increase consumer trust in pensions, enhance their engagement with their pensions and help them to make better decisions. We therefore believe it also has the potential to support some of the measures we are proposing in this final report.

Work and Pensions Committee - pension freedom and choice inquiry

53. In September 2017, the Work & Pensions Committee (WPC) launched an inquiry into whether and how far the pension freedom and choice reforms are achieving their objectives and whether policy changes are required. It published its report following the inquiry in April 2018.[16]

54. This inquiry had a wide scope, taking in the current picture of what people are doing with their retirement savings and how they chose their paths, the information and guidance available, and the way the pension product market is working. The FCA has provided both written and oral response to the inquiry, which in part build on the research and analysis in the ROR.

55. The Committee's reports are highly relevant to much of the work we are currently undertaking, and plan to undertake in future. It has formed an important part of our considerations and we set out throughout this report how our remedies relate to the inquiry's findings.

Work and Pensions Committee - Collective defined contribution pension schemes inquiry

56. Collective defined contribution pension schemes (CDCs) are a form of "Defined Ambition" (DA) pensions, which share features of both DB and DC schemes. CDCs pool together investment and longevity risk across a large number of pension savers. They provide their members with a target pension that will be paid for life (which is why some call them target pensions).

57. CDCs differ from DB schemes in that they do not guarantee a certain retirement income. Instead of a guarantee, they have a target or ambition for the amount that they plan to pay out at retirement. However, if the CDC scheme is under financed (e.g. due to low returns, or unexpected increase in life expectancies), it can change the target amount and even reduce pensions in payment.

58. In November 2017, the WPC announced an inquiry on CDC, which will explore the merits of this idea, the role that CDC schemes could play in the pension landscape, the

[15] See pages 7-8 of the FAMR final report, www.fca.org.uk/publication/corporate/famr-final-report.pdf

[16] Pensions freedom and choice inquiry www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/inquiries/parliament-2017/pension-freedoms-17-19/

potential benefits to savers and the wider economy, and the legislative and regulatory framework that would be required to make it work. In addition, Royal Mail and the Communication Workers Union (CWU) have agreed in principle to work towards introducing a CDC scheme for all employees.

59. Introducing CDC will require making legislative changes which will provide more detail and clarity on the proposals. We will continue to follow the work of the Committee and developments for Royal Mail.

The Pan-European Personal Pension Product (PEPP)

60. In June 2017, the European Commission tabled a legislative proposal for a Regulation on a pan-European Personal Pension Product (PEPP).

61. The general objective of the PEPP is to create the legal framework for a "simple, safe and cost-effective" new pension product, which enhances consumer choice—especially in EU countries with an underdeveloped domestic market—while also contributing to the completion of the Capital Markets Union (CMU) by unlocking capital for investment.

62. The proposal is not intended to replace or harmonise existing national personal pension schemes, but complement them by adding a pan-EU framework for pensions for those who wish to use it as a saving option. The Regulation would enable - but not require - providers to create a personal pension product that meets the requirements set out in the Regulation.

63. The unique feature of the PEPP is that it is designed specifically with the Single Market in mind. It can be sold at a distance from any EU country to a consumer in any Member State.

64. The regulation is subject to ongoing negotiation at European level. We continue to monitor its development and the consequent implications for UK providers and consumers. The degree to which the Regulation will be applicable to the UK will depend on the nature of our arrangements with the EU post our departure.

The Directive on Institutions for Occupational Retirement Provision (IORP II)

65. In 2014, the European Commission proposed a revision ('IORP II') of the existing Institutions for Occupational Retirement Provision (IORP) Directive of 2003, which covers certain occupational pension savings.

66. The proposed revision aims to improve the governance, risk management, transparency and information provision of IORPs and help increase cross-border IORP activity. IORPs fall under the regulatory jurisdiction of the Pensions Regulator, though many consumers may be transferring from IORPs to schemes within the FCAs regulatory perimeter to access the pensions freedoms.

67. It came into effect on 12 January 2017 and Member States have two years from then to transpose it into national law. The Pensions Regulator is the Competent Authority for IORP II.

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