FINANCIAL CONDUCT AUTHORITY

Improving outcomes in non-workplace pensions – feedback on CP21/32 and our final rules and guidance

Policy Statement

PS22/15

December 2022

This relates to

Consultation Paper 21/32
which is available on our website at
www.fca.org.uk/publications

Email:
cp21-32@fca.org.uk

Moving around this document
Use your browser's bookmarks and tools to navigate.
To **search** on a PC use Ctrl+F or Command+F on MACs.

Sign up for our
news and publications alerts

See all our latest press releases, consultations and speeches.

Contents

1 Summary 3
2 Default investment strategy 8
3 Cash warnings 21
4 Cost benefit analysis 31

Annex 1
List of non-confidential respondents 32

Annex 2
Abbreviations used in this paper 34

Appendix 1
Made rules (legal instrument)

1 Summary

1.1 Consumers can save for a pension through a non-workplace pension (NWP) or a workplace pension. This paper covers proposals to improve outcomes for consumers with NWPs, using our experience from previous work on workplace pensions and investment pathways for drawdown in pensions.

1.2 NWPs are used by a wide range of consumers, including the employed, the self-employed, the unemployed and those in newer types of employment. As the market for NWPs has developed, the range of investments that could be included in an NWP has grown.

1.3 In 2018, we published a Discussion Paper (DP18/1) to improve our understanding of how well the NWP market was working for consumers. In 2019, we published a Feedback Statement (FS19/5), which found similar demand-side weaknesses to workplace pensions. Limited consumer engagement, combined with complex and confusing products and charges, had led to a lack of competitive pressure to drive better value for consumers with NWP products. We also found that non-advised consumers buying an NWP often have little investment expertise and may find it difficult to engage with the choice and complexity of investments. Some may end up in investments that are unlikely to meet their needs and objectives for retirement or may remain in cash. Others may be put off from buying an NWP at all.

1.4 So, in November 2021 we consulted (CP21/32) on proposals to require firms to offer a default option to non-advised consumers buying an NWP. A firm would design this option for the typical non-advised consumer in its target market and make it available alongside other investments. Non-advised consumers choosing this option would be able to depend on the firm for an investment strategy that meets the objective of building a pension pot for future access. We also proposed to require cash warnings to notify consumers invested in cash that their pension savings are at risk of being eroded by inflation.

1.5 This Policy Statement sets out our response to the feedback we received to CP21/32 and details the final rules and guidance we are introducing.

Who this affects

1.6 The Policy Statement will primarily be of interest to firms that operate NWPs, including:

- life insurers
- platform providers
- Self-invested Personal Pension (SIPP) operators

1.7 This Policy Statement is also relevant to other stakeholders with an interest in NWPs, including:

- industry associations and trade bodies
- independent governance bodies

- asset management firms
- individuals and firms providing advice and information in this area
- consumer representative groups
- charities and other organisations with a particular interest in the ageing population
- consumers

The wider context of this policy statement

1.8 Our interventions to improve outcomes for non-workplace pension savers complement our other regulatory initiatives that intend to drive better outcomes for consumers and guide them to better products.

1.9 Our aim is to deliver a pensions system that helps consumers achieve the best outcomes within the means available to them.

1.10 More broadly, the interventions in this paper will help firms meet our expectations in the Consumer Duty for them to act to deliver good outcomes for retail consumers. For pension products, this will include enabling and supporting savers to pursue their financial objectives. The interventions also support the aims in our Consumer Investment Strategy to give consumers the confidence to invest.

How it links to our objectives

Consumer protection

1.11 Our final rules for a default option aim to protect non-advised consumers who find it difficult to engage with investments and end up making poor choices for their NWP. The range of investments available today can be very wide and complex. Some non-advised consumers may choose investments that are not properly diversified or otherwise aligned with their pension objectives. We want to ensure that there is support for consumers faced with this complexity, in an easy-to-access, standardised investment NWP option. We expect default options designed by firms to meet the pension objectives of the typical non-advised consumer in the firm's target market, to deliver substantially better pension outcomes for these consumers.

1.12 Our final rules for cash warnings are intended to protect consumers who have already held a significant and sustained level of cash in their NWP. The cash warning would highlight how inflation erodes the value of cash investments. It is intended to prompt consumers to consider whether they should remain in cash or switch to growth assets.

Competition

1.13 NWP providers known for a well-designed and good value default option could attract a greater share of new NWP business. This may promote competition between providers in the interests of consumers.

What we are changing

1.14 In CP21/32 we proposed to require firms to:

- offer non-advised consumers buying an NWP a ready-made, standardised investment solution (a 'default option'), and make this available alongside other investments
- send a notification ('cash warning') to consumers with significant and sustained levels of cash in their NWP to warn them that their pension savings are at risk of being eroded by inflation

Outcomes we are seeking

1.15 The key outcomes we seek are:

- default options that are fair value and designed to meet the needs of the typical non-advised consumer choosing them
- on average, a better pension outcome for consumers choosing a default option than they could otherwise achieve on their own
- fewer consumers holding significant and sustained levels of cash in their NWPs over the longer term

Measuring success

1.16 For default options, we expect to see a significant level of take up by non-advised consumers and options that offer value for money. For cash warnings, we want to see consumers responding to warnings and the proportion of consumers with significant and sustained cash investments to fall over time.

Summary of feedback and our response

1.17 We received 29 consultation responses, from a mix of stakeholders. These were mostly from industry, but we also had responses from consumer representatives. Respondents were mostly supportive of our policy proposals. Some respondents disagreed with specific aspects and suggested alternatives. We summarise the approach we have taken below.

1.18 Most respondents agreed with the proposal to require firms to offer a single default option, although a small number argued for more flexibility, including offering several default options to serve different groups of investors. Our final rules still require providers to offer a single default option to support consumers who are struggling to make a decision. Providers can offer additional investment options, alongside the default option should they wish to do so, for consumers who are willing and able to engage in investment decisions. This allows flexibility whilst providing support for those consumers who need it – which is the purpose of this policy initiative.

1.19 Firms also agreed with exempting bespoke SIPPs that did not offer investment options and firms with legacy-only business from offering a default option. However, some firms asked us to clarify what we meant by legacy-only business and the requirements for bespoke SIPPs. We have added guidance in response to this feedback.

1.20 A few firms suggested we consider alternative names to the proposed name of the default option – the 'Standardised Investment Solution'. Suggestions included the 'Starter Fund' or allowing firms to choose the name, as long as it is clear that it is the default option. We have amended our rules to be more outcomes focused and give providers more flexibility regarding the name of the default option. Providers must ensure consumers can identify the default option and understand its purpose, which is consistent with the principles of the Consumer Duty.

1.21 Our proposals on the design of the default option, as consulted on, aimed to be flexible to allow different models of default option, for example by using third party manufacturers. They also intended to ensure firms take account of ESG risks, as already required in FCA rules, and the need for lifestyling. In the feedback we received, most firms agreed with the approach we have taken, saying we should not be prescriptive on the design. About a third of firms who responded disagreed with the requirement for firms to implement lifestyling, believing this should be for firms to decide. We have considered the feedback and amended the rules to clarify that while we expect lifestyling to be appropriate in many cases, it is not required if firms decide it is not appropriate for a target market.

1.22 Most firms agreed with the principle behind cash warnings. However, a number asked us to make the requirements less prescriptive or that we align them with existing requirements for drawdown funds. For example, by showing illustrations of the effects of inflation over 5 years like in the cash warnings for non-advised consumers entering or transferring into a drawdown fund rather than our proposed 10 years. Our final rules are unchanged from the proposals consulted on. We consider that the proposal to require cash warnings up to 5 years before the normal minimum pension age to be appropriate. Providers can choose to give additional cash warnings on top of those required by our rules, up to and after this age. Providers can set the triggers and frequency for these additional warnings at a level they deem appropriate.

1.23 Most industry respondents disagreed with 3-month assessments of cash holdings, for a variety of reasons although a consumer group agreed with our proposals. Some preferred 6 month/annual assessments and to send out warnings together with the annual benefit statements to reduce the burden of compliance with the rules. Other respondents argued for less prescriptive rules on how firms should carry out the assessments to give them flexibility to decide how to assess whether a consumer has held significant cash holdings. We retained the 3-month assessments as consulted on. Increasing the period between assessments would increase the time a consumer could hold cash before they receive a warning. Our final rules mean the maximum time a consumer can have significant and sustained cash holdings before they receive a cash warning is 12 months. We believe this is an appropriate balance to deliver good outcomes for consumers.

1.24 We proposed an implementation period of 12 months. Many firms requested at least 18 months for implementation due to the number of regulatory changes occurring at the same time. We have retained the 12-month implementation period, as these rules are consistent with the principles of the Consumer Duty which come into force, for products open to sale, 6 months before the NWP rules come into force.

1.25 In summary, following consultation feedback, we are finalising the rules and guidance on default options and cash warnings largely as consulted on, with the following changes and clarifications:

- providing clarity on the scope of the exemption for firms with legacy-only business
- clarifying what we consider to be a 'bespoke SIPP'
- amending requirements on the naming of the default option to allow firms flexibility in its naming
- adding a definition of 'distributes' for investments
- adding guidance to clarify that where a firm outsources the manufacturing of a default option, the firm remains responsible for complying with the requirements in the new default fund conduct of business rules
- other miscellaneous clarifications and amendments aimed at improving clarity

Equality and diversity considerations

1.26 Our final rules in this paper affect consumers using NWPs to save for their retirement. Overall, we do not consider that the proposals materially impact any of the groups with protected characteristics under the Equality Act 2010. The default option may help improve the accessibility of NWPs since it would be for non-advised consumers unable or unwilling to choose investments. So, it may have a positive impact on potentially vulnerable consumers.

1.27 Respondents to CP21/32 did not identify any equality or diversity issues with our proposals.

Next steps

1.28 We set out the final rules and guidance in the Appendix of this paper. Firms affected by these changes will need to ensure they comply by 1 December 2023.

2 Default investment strategy

2.1 This chapter summarises the feedback we received on our proposal to require firms to offer non-advised consumers a ready-made, standardised investment solution (a 'default option'). We also set out our response to the issues raised, including how we are making changes in response to the feedback received.

Our proposals for a default option

2.2 We consulted on rules to require firms to offer non-advised consumers a default option for their NWP. While we proposed that firms make a single default option available to non-advised consumers, we did not prescribe a choice architecture. But we wanted non-advised consumers to be aware that the default option is available.

2.3 So we proposed that firms should present the default option in an appropriately prominent way, when non-advised consumers first set up their NWP and at other times when they are choosing investments. Non-advised consumers who have no need for the default option can simply decline or ignore the offer. We did not require firms with only legacy NWP non-advised business to make a default fund available to their existing customers.

2.4 We asked:

Q1: ***Do you agree that we should require firms to offer a single default option rather than multiple default options/ investment pathways?***

Q2: ***Do you think there is a case for requiring firms with only legacy NWP business to make a default option available to their customers?***

Feedback and our response

2.5 Most respondents agreed with our proposal to require firms to offer a single default option. They agreed that consumers in the accumulation stage generally have the same objective and that multiple options would risk adding complexity.

2.6 However, some respondents saw merit in offering consumers a variation of the default or presenting a small range of standardised investment solutions. They argued that this would work better for a broad range of consumers with different risk appetites and abilities to engage with their pensions, rather than offering the same default option to all non-advised consumers. One respondent acknowledged that alternative investments solutions could be offered in other ways, such as through a decision tree tool that would sit alongside the default option.

2.7 Most respondents did not think there was a case for requiring firms with only legacy NWP business to make a default option available to their customers. However, some firms requested that we clarify what fell within the definition of legacy business.

2.8 Five respondents thought that firms with only legacy NWP business should be required to offer a default option because the risk that consumers are invested in inappropriate investments existed whether the business was new or legacy.

Our response

As set out in CP21/32, we found that many consumers struggle to make investment choices beyond deciding that they want a pension. Presenting consumers with multiple options would not address the harm of consumers not being able to choose an investment option. We maintain that an individual consumer should be presented with only one default option to support those who are struggling to make a choice.

We are aware that some NWP providers already offer a range of 'standardised solutions' which take account of different consumer needs. Firms can use questioning or filtering tools to identify standardised solutions for consumers with particular needs or characteristics (as described in PERG 8.30A.1G and PERG 8.30A.9G). However these should be shown alongside the default option to ensure that consumers can fallback on the default option if they struggle to make a choice.

While pre-purchase filtering tools can be helpful in terms of identifying standardised solutions for consumers with particular characteristics, we are concerned whether this is an appropriate way to identify a default option for consumers, particularly for the least engaged or informed. We want to ensure that consumers who are unable or unwilling to engage with detailed questionnaires have a good investment solution readily available to them. We therefore require firms to present consumers with an appropriate default option without them having to answer detailed questions in advance. A default option would also be offered when a non-advised consumer first purchases the NWP product, which may be before a consumer is presented with tools to support the selection of particular investments.

As set out in para 2.6, we understand from feedback that some firms may want to develop more guided propositions that would allow the firm to offer a variation of the default, but would be prevented from doing so by our rules. Firms that want to develop such propositions and can demonstrate that they can still achieve the outcomes described in COBS 19.12.9G (2), can contact us bilaterally.

Legacy business is excluded by disapplying the new COBS 19.12.10R and COBS 19.12.15R rules to firms that do not enter into new non-workplace pensions with non-advised clients. In response to feedback, we have added guidance at COBS TP 2.47, to be clear when firms with legacy business will not be required to offer a default option is clearer.

In CP21/32, we proposed not to require firms with legacy NWP business to offer a default option, as we did not think the benefits would outweigh the costs. We note the concerns that consumers with legacy products may have inappropriate investments. While our proposals do

not apply to firms with legacy only business, the Consumer Principle in the Consumer Duty requires firms to act to deliver good outcomes for retail consumers. One of the four outcomes is that products and services offer fair value, including existing products and services. This new requirement on firms will help protect the interests of consumers in legacy products.

Engaged versus disengaged consumers

2.9 In CP21/32 we said consumers can engage with their pension without engaging with the underlying investments. Consumers need to engage with their projected income in retirement, how much they contribute, and when they plan to access their pension. This engagement is at the level above the underlying investments.

2.10 Moreover, engagement with investments by consumers who lack the skills or expertise to make appropriate investment choices can put pension outcomes at risk. For these consumers, a default option designed and governed by the firm is likely to deliver a better pension outcome than they could achieve on their own.

2.11 We asked:

> **Q3:** ***Do you agree that we should require firms to offer a default option to all non-advised consumers entering into an NWP? If not, what would you propose?***

Feedback and our response

2.12 Of the respondents who commented, 16 respondents agreed with our proposals, 4 disagreed and 3 neither disagreed nor agreed.

2.13 As alternatives, some respondents suggested exempting some consumers based on criteria such as age.

2.14 Some respondents argued that products and consumers varied, and it was not simply a case of advised or not advised. In some cases, they said offering all non-advised consumers a default option risked consumers choosing the default option instead of engaging with the tools or decision trees that many firms may have made available to identify potentially more suitable options. In their view, firms should be required to develop principles-led interventions to identify customers whose actions suggest low levels of engagement or potentially poor decision-making, and engaging with them to encourage more relevant behaviours, possibly through offering a default option.

Our response

As set out in paragraph 3.2 of CP21/32, consumers are being asked to make complex investment choices when they may not find it easy to engage with the options available due to behavioural biases and a lack of relevant expertise.

The availability of a default option does not prevent those consumers who want to or are able to from engaging with the other investment options available.

As set out in FS19/5, while we agree that a default option would take away the need to engage further with underlying investments for those consumers choosing one, we do not think this will cause engaged consumers to disengage with their pension choices. Many of the non-advised consumers taking up the default option will already have been unable or unwilling to engage properly with investments and will likely to remain less engaged throughout their pension journey. Even if they engage more, we think most of these consumers are unlikely to develop sufficient expertise to make optimal decisions about the mix of investments to include within their NWP.

Firms may be able to develop interventions that identify consumers whose actions suggest low levels of engagement or potentially poor decision-making, but given the difficulty in getting non-engaged consumers to engage, we think a simple solution at the point where consumers are most engaged, i.e. at the stage of entering into a non-workplace pension, is the most effective way of supporting consumers.

The providers covered by our proposal

2.15 Firms, such as insurers, platform providers and smaller SIPP operators operating NWP schemes would be in scope of our rules to offer a default option. Some firms operate schemes that, at an HMRC registration level, encompass both workplace and non-workplace arrangements. We proposed to apply our rules to the non-workplace arrangements only within the overarching scheme.

2.16 We proposed firms would not be required to offer a default option to consumers who received a personal recommendation for the investments in their NWP. This is because the adviser should recommend suitable investments. Firms that do not accept any new non-advised consumers into their NWP arrangements would not be required to make a default option available.

2.17 We proposed firms would not be required to offer a default option to consumers using discretionary investment management services.

2.18 We asked:

Q4: ***Do you agree that we should not require firms to offer a default option to advised consumers or consumers using discretionary investment management services for their NWP?***

Feedback and our response

2.19 Twenty-one respondents agreed with our proposals, noting that consumers will have received help and a personal recommendation on the most appropriate investment.

2.20 Two respondents disagreed. One respondent thought a default option should be offered to advised consumers as well. One trade association said in cases where a discretionary management service is one option in a broader range of non-workplace investment offerings, the default option should be offered.

Our response

As stated above, the intention of our proposals is to support consumers who may otherwise struggle to make an investment decision. Adviser consumers would have been recommended suitable investments, which addressed the harm we have identified.

Our proposals allow firms that do not accept any new non-advised consumers into their NWP arrangements to not make a default option available, which is a proportionate outcome. We also clarified (see changes to COBS TP 2.47 above) that a default option will not need to be offered where a firm does not enter into new non-workplace pensions with non-advised clients but still continues to offer, distribute or promote new investments, or promote platform services that distribute new investments to (or top-up existing investments for) existing non-advised clients to include in their non-workplace pension.

As set out in COBS 19.12.5R (2), a default option will not have to be offered if a discretionary manager has been appointed. Where discretionary management is one option alongside other offerings, the default option should still be offered.

We have amended COBS 19.12.1R to include a definition of 'distributes' which makes it clear that it includes a firm having an arrangement with a third party to arrange an investment, or to promote platform services that distribute investments. Such firms will need to offer a default option unless an exclusion is available.

Bespoke SIPPs

2.21 We referred to firms offering 'empty wrapper' SIPPs as bespoke SIPP operators. These firms do not offer a menu of investments from which a consumer must choose (nor do they have arrangements with others to offer investments). Rather, their business model is that they only deal with consumers who know what investments they want and directs the SIPP operator to make the investments.

2.22 Consumers using bespoke SIPPs are generally advised. Bespoke SIPP operators could avoid the requirement to offer a default option by turning away non-advised consumers unless they take advice. We proposed instead that firms which do not offer investments (including investments from third parties) to consumers for inclusion in the NWP would not be required to offer a default option.

2.23 We asked:

> **Q5:** ***Do you think we are right to exempt bespoke SIPPs? Do you see any issues with our proposed approach? If so, what would you suggest?***

Feedback and our response

2.24 Twenty-six respondents answered this question. They broadly agreed with our proposals to exempt bespoke SIPPS from the default option requirements.

2.25 A number of respondents requested that we should ensure the exemption for bespoke SIPPs is clear in the Handbook.

2.26 Three respondents disagreed with the exemption, noting that while bespoke SIPPs are generally sold on an advised basis, they can be sold on a non-advised basis and there have been cases where inappropriate investments have been accessed. Another respondent argued that SIPPs targeted at people who want to select investments from open markets rather than the full spectrum of investments possible in a bespoke should also be exempt from offering a default option.

2.27 A consumer group suggested that consumers taking out bespoke SIPPs should be made aware that there are simpler products with default options.

Our response

In response to feedback, we have clarified our guidance in COBS 19.12.3 G to ensure that it is clear that bespoke SIPPS are 'empty wrapper' SIPPs that do not offer a menu of investments from which a consumer must choose – instead their business model is solely to accept instructions from customers who have already identified the investments they want to include in their SIPP operators. Operators of such products will not be required to offer a default option.

We accept that there may be some instances where bespoke SIPPs are sold on a non-advised basis, however they are predominantly sold on an advised basis.

On balance we do not think it would be proportionate to require bespoke SIPPs to offer a default option, nor do we not want non-advised consumers to be denied use of bespoke SIPPs because of our rules if bespoke SIPP operators decide to turn away non-advised consumers.

When a default option would be offered

2.28 We proposed that firms be required to offer a default option to non-advised consumers upfront, at the time they enter into an NWP with the firm.

2.29 We proposed that firms should also offer a default option to non-advised consumers at the time they fund their NWP, if this is later than when they set it up.

2.30 When non-advised consumers are presented with a menu of investments available for inclusion in their NWP, we proposed that the default option should be included in a location most likely to bring it to the attention of the client. Just as the default option would be offered with any menus of investment choices, we think it should be presented alongside any decision trees or tools, at point of entry.

2.31 We asked:

> **Q6:** ***Do you agree that the default option should be offered upfront, in menus of investment choices, and alongside decision trees or tools? If not, what would you suggest?***

Feedback and our response

2.32 Most respondents agreed with our proposal, with respondents supporting the requirement to offer the default option upfront and at the point of making an investment decision if this is at a later point.

2.33 A few respondents argued that the provider is best placed to decide when the default option should be presented in the consumer journey, while others argued there were circumstances where the default option should not be offered.

2.34 One respondent argued that consumers with streamlined SIPPs tend to be engaged with their investment strategy and decision making and should be able to opt out of being offered the default option.

Our response

Consumers are most engaged at the point of opening their NWP or making an investment choice. We think offering the default option at other points risks requiring providers to ask for an active decision outside of a natural decision point in time and consumers might not respond. It would also require providers to develop a process for asking the question and a process for consumers who do not respond. Our rules do not prevent the default option from being offered at other stages of the journey as well if providers decide to do so.

If a firm offers menus of investments or decision tree tools, then the default option should be presented alongside those. That should benefit existing non-advised customers who are reviewing their investments or deciding where to invest a new contribution, as well as new non-advised customers investing for the first time if they find they are unable to choose from the investments offered. Consumers who are engaged with their investment strategy can choose to ignore the default option, so there is no need to offer them an opt-out.

Consumers transferring in investments they already hold elsewhere and who already have an investment strategy do no need to be offered the default option.

How a default option would be offered

2.35 When offered upfront, we proposed that the default option should be presented prominently and on a stand-alone basis. When offered in menus of investments, it should be presented with at least equal prominence to other investments. When offered alongside a pre-purchase questioning or filtering tool, it should be presented with at least equal prominence to that.

2.36 We proposed to require firms to label their default option as the 'standardised investment strategy' for non-advised consumers. We considered the label 'default option' but the word 'default' may have negative connotations and might imply (even with 'option') that consumers will be automatically invested in it should they make no choice.

2.37 We asked:

> **Q7:** ***Do you agree with our proposals for how a default option would be offered?***

Feedback and our response

2.38 Respondents broadly agreed with proposals to ensure the default option is displayed with at least equal prominence to other investment options.

2.39 One respondent raised concerns that prominently displaying the default option could lead to inertia, with consumers opting for the default option rather than considering other investment options.

2.40 A number of respondents disagreed with our requirement to label default option as the 'standardised investment strategy'. One respondent said the label was not consumer friendly and would not aid consumer understanding. A number suggested alternative names or that we carry out further consumer testing to decide on an alternative name, while others argued that the naming should be left to providers to decide what works best for their consumers, based on their own consumer testing.

Our response

It is important that consumers are aware of the existence of the default option at key decisions points such as at the point of purchase or making investment choices otherwise they may be discouraged from getting an NWP. As set out above, many non-advised consumers are unable or unwilling to engage with investments and are likely to remain less engaged throughout their pension journey in any case.

We proposed a consistent naming convention for the default option because we thought it would help consumers more easily identify the default option and its purpose. Following feedback and further consideration, we agree that there are likely to be negligible differences in consumer understanding between different headline default option names. Rather, we think the best way to help consumers understand the default fund is via a simple description of the default option.

We have changed the final rules to allow firms flexibility in naming the default option. This is consistent with the approach taken in the Consumer Duty, where we expect firms to support their customers by helping them make informed decisions about financial products and services. To support this, we have amended the rules we consulted on to remove prescription and will instead require that any name used should be sufficiently clear to give an indication of the nature of the default option and also to distinguish it from the firm's other offerings.

Governance and design

2.41 We proposed extending the application of the Product Intervention and Product Governance Sourcebook (PROD) 4 so that it also applies, for the manufacturing or distributing of default options, to the providers of arrangements that do not take the legal form of an insurance contract.

2.42 We proposed additional requirements in our product governance rules to reflect our expectation that firms consider:

- the likely characteristics and needs of consumers using the product
- an appropriate and diversified allocation of assets, to manage risks while seeking investment growth
- an appropriate and competitive price for the product, which bears a reasonable relationship to the services being provided

2.43 Firms with existing standardised solutions may choose to adapt one of these as their default option. A firm may continue to offer a number of standardised solutions, for example as end points for decision trees or tools but, as explained above, the default option would always be presented at the point of entry.

2.44 We asked:

> **Q8:** ***Do you agree that we should extend our product governance rules in PROD 4 to all manufacturers and distributors of default options?***

Feedback and our response

2.45 No respondents disagreed with our proposals, although one questioned how PROD 4 would apply to a default option as it cannot be considered as an individually tailored solution.

2.46 One firm suggested that when replacing a default option, consumers using the previous default option should be given the option to remain in the existing option or be transferred to the new one, rather than be automatically transferred to the new one.

Our response

Given the feedback, we are proceeding with the rules as consulted on.

We expect the distributor of the default option, if different from the manufacturer, to review their choice of default option at least every 3 years and transfer consumers to a new default option if necessary to prevent harm. This is to ensure the design, performance and investment strategy of the default option remains appropriate for the target market.

We do not think it is feasible to require an active decision when replacing the default option. Many consumers using the default option are likely to be unengaged and firms may struggle to get them to confirm whether they want to remain in the current default option, rather than be transferred to the new one. In addition, such consumers may struggle to actively make an informed choice between remaining in the current default option or being moved.

Models of default option

2.47 Some firms or groups of firms may operate different businesses with different target markets. Our proposed rules did not require the same default option to be offered across these. But a firm would not be able to offer an individual more than one default option, nor could a firm offer a default option that depends on that individual's answers to a decision tree or tool.

2.48 Many workplace default arrangements include 'lifestyling' in the years before a target retirement date, to de-risk investments towards an investment portfolio appropriate for how consumers are likely to want to use their pension savings. While we expect firms to include lifestyling where this meets the needs of their target market, our existing rules and pensions legislation do not require it. We proposed to require firms to include lifestyling in the design of a default option, unless the needs, objectives and characteristics of consumers in the target market for the default option are incompatible with lifestyling.

2.49 Our proposed rules enabled the use of target date funds for default options. For both target date funds and lifestyling, we think that firms should assume pension access at state pension age unless an individual has stated otherwise.

2.50 We asked:

> **Q9:** ***We have sought to enable different models of default option while ensuring that firms take account of ESG risks and the need for lifestyling. Do you think we have provided sufficient flexibility? Alternatively, do you think we should be more prescriptive?***

Feedback and our response

2.51 Twenty-four respondents answered this question, with an almost equal split between those who supported the proposals and those who did not.

2.52 Fourteen respondents agreed with the proposals, with most of them supporting the flexibility provided and noting that they did not see the need to be more prescriptive. One respondent argued that lifestyling or the use of target date funds should be mandatory as consumers who chose the default option are unlikely to be sufficiently engaged or informed such that they would personally act to make lifestyling inappropriate. One respondent said that providers should not be obligated to offer an explicit ESG fund as a default option, as unengaged investors are unlikely to have a view on ESG issues.

2.53 Ten respondents disagreed with our proposals. The majority disagreed with our proposals on the basis that the decision to include lifestyling should be at the discretion of the provider, while our current proposals would make it difficult to avoid lifestyling, even if it was not the right approach.

Our response

We proposed that firms build lifestyling into the design of the default option so that investments are de-risked automatically in the run up to a target date of retirement unless it is incompatible with the needs of the target market.

We are aware that some market commentators consider our use of the term lifestyling to mean a specific type of lifestyling towards purchase of an annuity. To be clear, our use of the word lifestyling is much broader and is consistent with industry usage. By lifestyling we mean any automatic and pre-determined change in the investment mix that involves an appropriate level of de-risking in the years before target retirement age. The aim is to ensure that the investment mix at target retirement date is consistent with how consumers invested in the product are expected to use their pension savings. In today's market, lifestyling can be towards income drawdown where the consumer would expect to stay invested, for example.

We expect firms to be mindful of the needs of and objectives of their consumers. As mentioned above, PROD 4, which requires identification of a target market, the design of a product that is compatible with the needs, characteristics and objectives of consumers in that target market, and product testing, will apply to the manufacture and distribution of a default option. The lifestyling built into the design of the product should be with good customer outcomes in mind, for a given target market and should not automatically lead to full disinvestment from growth assets.

We think that lifestyling will be appropriate in most cases but recognise there may be certain target markets for which it is not appropriate. We do not think that lifestyling should be mandatory. Having considered the feedback, we have amended the rules so it is clear that we require lifestyling unless the needs of the target market make it inappropriate to offer lifestyling.

Our proposed rules did not require providers to offer an ESG fund as a default option. However, we remain of the view that providers should take proper account of climate change and other ESG risks and opportunities in their design of the default. Our existing guidance at SYSC 3.2.23G and SYSC 4.1.15G will apply to default options.

We have also added to COBS 19.12.21G to clarify that where manufacturing of the default option is carried out by a third party, the operator retains the responsibility to offer the default option in line with the requirements in the new rules in COBS 19.12.

Governance

2.54 We did not propose to extend the remit of Independent Governance Committees (IGCs) and Governance Advisory Arrangements (GAAs) to default options and did not propose a charge cap. We expect providers to consider their obligations under our product governance rules and under our Consumer Duty.

2.55 We asked:

> **Q10:** ***Do you agree that we should not extend the remit of IGCs/ GAAs or cap the charges of default options at this time?***

Feedback and our response

2.56 The majority of respondents agreed with our proposals, while 2 disagreed. One individual supported the introduction of a charge cap, while 1 firm supported a role for IGCs/GAAs to provide independent review and reduce the need for additional regulation to ensure consumer protection.

Our response

Given the feedback that we received, we are proceeding with our rules as consulted on. As mentioned in CP21/32, we expect providers to consider their obligations under our product governance rules and under the Consumer Duty.

Implementation timeline

2.57 We proposed that providers be given 12 months to implement these proposals from the date we publish our final rules and guidance.

2.58 We asked:

> **Q11:** ***Do you agree with our proposed implementation timeline for the default option?***

Feedback and our response

2.59 Fifteen respondents disagreed with the proposed implementation period, with a number preferring an 18-month implementation period due to the number of regulatory initiatives during this period, while one individual preferred a shorter implementation period of 6 months.

2.60 Seven respondents agreed with our proposal. One respondent said 12 months was a reasonable implementation period if there was no requirement for providers to auto-invest on behalf of investors or present the default option with investment tools.

Our response

We have retained the 12-month implementation period. We are conscious that firms must implement the Consumer Duty and other regulatory initiatives in this period, in a challenging economic climate. However, this must be balanced against the ongoing harm to consumers who may be struggling to make an investment choice. The default option rules are consistent with the principles of the Consumer Duty, which come into force 6 months before these rules (for products open to sale), so firms should already be considering how to support such consumers. We think the current implementation time achieves a fair balance between protecting consumers and taking into account the burden on firms.

Our final rules do not require providers to auto invest on behalf of investors, although the default option will have to be presented alongside investment tools and decision trees.

3 Cash warnings

3.1 This chapter summarises the feedback we received on our proposal to require firms to send a notification (a 'cash warning') to consumers with a significant and sustained proportion of their NWP assets invested in cash, with annual cash warnings thereafter.

Our proposal for a cash warning

3.2 We consulted on a requirement for the providers of NWPs to send cash warnings to consumers with significant and sustained cash holdings.

3.3 A consumer who has been given a cash warning and continues to meet the conditions would be sent ongoing cash warnings. We proposed that providers have up to a year before they must resend a cash warning. We think it is important that consumers who receive a cash warning and do not act on it continue to receive cash warnings.

3.4 We asked:

> **Q12:** ***Do you agree with our proposals for cash warnings to be given to consumers with significant and sustained cash holdings in their NWPs?***
>
> **Q13:** ***Do you agree that we should make cash warnings mandatory up to the proposed age limit, with guidance that providers should consider giving cash warnings beyond that age limit?***

Feedback and our response

3.5 All respondents agreed with the intention of our policy proposals. They noted the adverse impact significant and sustained cash holdings can have on retirement outcomes. One respondent did not think there should be prescriptive rules around when and how consumers are warned about their cash holdings and it should be left to providers to decide how best to communicate with their customers about their cash holdings.

3.6 Views differed on the appropriate threshold level before a cash warning was required. A number of respondents said the thresholds of 25% of NWP assets or £1000 in cash for a cash warning was too low a threshold and suggested higher figures. One respondent argued that 6 months was not a long time to hold cash and could be the result of an active decision. A few respondents suggested aligning the requirements with those of drawdown funds.

3.7 Thirteen respondents agreed that cash warnings should be mandatory up to 5 years before the normal minimum pension age. A number of respondents thought an age limit should not apply, and cash warnings should be sent up to the expected pension age. A few respondents thought there should not be an age limit and firms should be able to decide whether it is appropriate to send a cash warning based on a consumer's intentions.

Our response

We are proceeding with our proposals as consulted on. As set out in CP21/32, we sought to align our proposals, where appropriate, with existing cash warnings for non-advised consumers entering or transferring into a drawdown fund. The objective of issuing a cash warning remains the same throughout the saving journey and we do not see a reason to change the way they are issued during the accumulation phase by having less prescriptive rules.

We think the lower proposed threshold for NWP cash warnings, rather than the 50% threshold for cash warnings under our existing rules for drawdown is appropriate because consumers in the accumulation phase generally have a longer investment timeframe, so the harm is greater and are less likely to have a good reason to be invested in cash.

Cash warnings will be mandatory up to 5 years before the normal minimum pension age. However, providers can continue to give cash warnings after this, since many consumers retire at or around state pension age. Our rules enable providers to tailor triggers for non-mandatory cash warnings to the characteristics and likely needs of their consumers. For example, a provider might choose to set a higher cash threshold for consumers closer to retirement. The provider could also take into account how their customers are likely to access their pension savings.

The Consumer Duty requires providers to consider what support consumers need, and in some cases, it may be appropriate to continue sending cash warnings.

For advised as well as non-advised consumers

3.8 We proposed to require providers to give initial and ongoing annual cash warnings to all their NWP consumers who meet the conditions, including existing and advised consumers.

3.9 We asked:

> **Q14:** ***Do you agree that we should require cash warnings for all consumers who meet the conditions, including advised consumers?***

Feedback and our response

3.10 Almost all respondents agreed with our proposals, with some noting that while it was a different approach to drawdown funds, it was a simpler approach.

3.11 Two respondents argued that advised consumers could be holding cash based on a recommendation from an adviser. In such cases, a cash warning could undermine the advice received and create confusion and complexity.

Our response

We think it is simpler and of relatively small marginal cost to require cash warnings for all consumers who meet the conditions.

Few consumers receiving ongoing advice should be significantly invested in cash for a sustained period, up to the age limit for mandatory cash warnings. For those who are not clear why they are significantly invested in cash for a long period, a cash warning may prompt a conversation with their adviser.

Active decision

3.12 Having considered the evidence available, we did not propose to require providers to ensure an active decision from consumers to hold cash. We proposed consumers would receive a cash warning once cash has built up to a significant level and has not been invested in growth assets for a sustained period.

3.13 We asked:

> **Q15:** ***Do you agree that we should not at this time require providers to ensure an active decision to hold cash in an NWP?***

Feedback and our response

3.14 The majority of respondents agreed with our proposals, with only 2 respondents disagreeing.

3.15 One respondent thought there should be a different, higher threshold at which an active decision to hold cash should be sought. Another respondent said that firms should ask whether cash is an active choice at the point of making an initial investment to align requirements in the accumulation and decumulation phases.

Our response

As set out in CP21/32, we considered whether to require an active decision to hold cash at some point, such as when a consumer meets a certain threshold of investable assets in cash or at the point of making an initial investment choice. We decided not to require providers to get an active decision, as they would have to ask for this outside of a natural decision point and consumers might not respond. It would also require providers to develop a process for asking the question and a process for consumers who do not respond. There would be a cost to industry that ultimately consumers may end up paying.

Having considered the feedback received, on balance, we maintain our position and think our final rules address the harm of consumers holding significant cash for sustained periods while avoiding unnecessary cost and complexity so we are proceeding with our proposals as consulted on. Our rules do not prevent providers from deciding on additional thresholds at which to warn consumers about their cash holdings if they think it is necessary.

The providers covered by our proposals

3.16 Our proposed rules for cash warnings apply to providers operating NWP schemes such as insurers, platform providers and SIPP operators. Some providers operate schemes that, at an HMRC registration level, encompass both workplace and non-workplace arrangements. Our proposed rules would apply for the non-workplace arrangements within the overarching scheme.

3.17 We do not see the need for a cash warning in relation to NWP assets where a consumer has contracted with a third party, for example discretionary investment management services, to manage and invest the assets on their behalf, on an ongoing basis.

3.18 We did not exempt bespoke SIPP operators from the requirement to give cash warnings to all their consumers, including advised consumers, who meet the conditions, as we consider it unlikely there be good reason for remaining invested in cash to a significant extent over the longer term.

3.19 We asked:

Q16: ***Do you agree that we should not exempt bespoke SIPP operators from the proposed requirement to give cash warnings?***

Feedback and our response

3.20 Twenty-four respondents answered this question. Only one respondent disagreed with our proposal, arguing that discretionary investment management services should not be exempted from giving cash warnings unless providers are also exempted from having to give cash warnings to advised consumers.

Our response

The need for a cash warning is excluded where the consumer has appointed an investment manager (including discretionary investment management services) because consumers who have appointed an investment manager will rarely have a significant amount invested in cash over a long period of time because their investments will be actively managed on an ongoing basis.

However, some advised consumers may be overly invested in cash for reasons such as having received historic advice, not acting on advice received or the investments originally advised on maturing and defaulting to cash. Where the conditions set out in COBS 19.12.23R are met, advised consumers will receive a cash warning. This may prompt a discussion with their adviser as a result.

What a cash warning would say

3.21 We proposed that the cash warning must:

- inform the consumer that more than a quarter of their NWP assets is invested in cash or investments that are similar to cash
- say that their NWP is at risk of being eroded by inflation
- include a generic illustration that clearly shows how erosion by inflation would affect a £10,000 pot over 10 years, assuming 0% interest and using the Consumer Prices Index (we propose 10 years rather than the 5 years for investment pathways cash warnings because consumers have longer to be invested when building a pension)
- inform the consumer that they should consider whether their current investments are likely to grow sufficiently to meet their objectives

3.22 Our proposals included guidance that the provider should also:

- explain in plain language or illustrate that different types of investment have a different balance of risk relative to potential gain
- inform the consumer that the provider offers other investments including the default option, where the provider offers one, and the consumer is not advised (a firm may also wish to inform advised consumers about its default option)
- make clear the warning is not advice and that the value of investments can fall as well as rise

3.23 We asked:

> **Q17:** ***Do you agree with our proposals for the content of a cash warning?***

Feedback and our response

3.24 Most respondents agreed with our proposals on the content of a cash warning, noting the consistency with drawdown.

3.25 A few respondents suggested our proposals were too prescriptive on the content of the cash warning and it should be left to firms to decide on the content. Some argued that as proposed, this would lead to a lengthy document, while others argued that it would stifle innovative ways of communicating with consumers.

3.26 Some firms suggested alternatives names for the notifications. They argued that calling the notifications 'cash warnings' gave the impression that something was wrong and suggested alternative names such as 'cash alerts'.

3.27 A few firms suggested that cash warnings should be sent alongside annual benefit statements (ABS) or as part of the ABS. They argued that it would make the process of sending cash warnings simpler or that consumers were already familiar with ABS and would be more likely to engage with that.

Our response

We agree that to be effective, a cash warning should have a clear and simple message presented in a way that is likely to engage consumers. While we have not mandated the precise wording, we have prescribed what the content must include. We think this achieves a balance between allowing firms to find innovative ways of communicating with consumers, while ensuring that key information is provided. This is consistent with our expectations for firms under the consumer understanding outcome of the Consumer Duty.

As mentioned above, where appropriate, we have tried to align our NWP rules with cash warning rules for non-advised consumers entering or transferring into a drawdown fund. 'Cash warning' is a term already in use to describe similar notifications and we think it would be confusing to consumers to introduce a different term at this point.

While initial assessments may not allow cash warnings communications to be aligned with ABS timings, our rules do not prevent firms from conducting future assessments at a time that allows the communication of a cash warning to be aligned with other client communications, such as the ABS. However, to ensure that the message on cash holdings is sufficiently clear, the warnings should be in a separate document that does not include unrelated information. As mentioned in response to questions 18 and 21 below, firms can carry out their own assessments on the need for cash warnings and send cash warnings before the implementation date of our rules if they are able to. Firms can also choose to send an additional cash warning once our rules are implemented if they think it is beneficial for a consumer.

When the need for a cash warning would be assessed

3.28 We proposed that providers must, for each of their consumers, determine the proportion invested in cash at least once every 3 months.

3.29 To determine whether the holding has been sustained, a provider must consider all assessments conducted over the preceding 6 months, for example the 2 previous assessments. If, in addition to the current assessment, more than 25% was invested in cash in each of the previous assessments, the requirement to notify the consumer would be triggered.

3.30 We proposed providers would not have to assess the cash investments of all their NWP consumers in each assessment, although they may choose to do so. Our proposed requirement for an assessment at least once every 3 months applies at the consumer level.

3.31 We asked:

> **Q18:** ***Do you agree with our proposals for when the need for a cash warning would be assessed?***

Feedback and our response

3.32 Twenty-seven respondents answered this question. Most respondents disagreed with 3-month assessments of cash holdings.

3.33 Respondents suggested that the same policy intention could be achieved via 6-monthly or annual assessments.

3.34 Other respondents argued that it should be left to firms to decide how to conduct the assessments, which would allow them to develop their own on-going measures.

3.35 Many respondents argued that while our proposals were one way of delivering our policy intent, they felt that they were unduly burdensome.

Our response

We are proceeding with our proposals as consulted on. We recognise that cash holdings could be assessed in a number of ways. However, we think 3-monthly assessments allow timely cash warnings to be sent to consumers, reducing the potential for harm. Increasing the period between assessments means a consumer could have significant and sustained cash holdings for a longer period before they receive a cash warning. Under our rules, the maximum period a consumer could have significant and sustained cash holdings before receiving a cash warning will be 12 months. Increasing the time between assessments would increase the time a consumer can have significant and sustained cash holdings to over a year before they are prompted to take action to address the harm caused by holding cash.

To reduce the administrative burden, our rules do not require providers to continuously monitor a consumer's NWP assets or assess the cash holdings of all their NWP consumers in each assessment. This flexibility allows providers to consider a consumer's holdings at a point in time, and to spread assessments and the issuance of cash warnings throughout the year or do them in batches, depending on what is easier for the provider operationally.

We acknowledge that some firms can develop complementary measures to identify consumers who are invested in cash alongside our proposals. This would be in line with the consumer support outcome of the Consumer Duty and our rules do not prevent this.

We think it is important to warn consumers with significant and sustained cash holdings in a timely manner but recognise that there may be some consumers who do not take action. Firms will not have to send a consumer another cash warning for a year once they have sent one, which further reduces the burden.

Overall, we think our rules achieve an appropriate balance to deliver good outcomes for consumers.

When a cash warning must be sent

3.36 We proposed that if the conditions are met in an assessment, the cash warning must be sent within an appropriate timeframe after the date of the assessment, likely to be within 3 months. At times of high market volatility, when markets may fall substantially, a cash warning may not be appropriate. We do not want to prompt consumers to consider growth investments at just the wrong time so we proposed that in such circumstances, a longer timeframe before sending a cash waring may be appropriate.

3.37 We asked:

> **Q19:** ***Do you agree with our proposed timeframe for sending cash warnings? If not, what would you suggest?***

Feedback and our response

3.38 Twenty-five respondents answered this question. About half of the respondents agreed with our proposals.

3.39 Most of those who disagreed raised concerns that firms should not have to decide when market conditions meant that it was not appropriate to send a cash warning. They argued that this could lead to different thresholds of when not to send a cash warning and could lead to complaints or inconsistent treatment of consumers. As a solution, they suggested we give a clearer indication of what market conditions meant it was not appropriate to send a cash warning.

Our response

We acknowledge that firms' approaches to deciding whether market conditions make it inappropriate to issue a cash warning may differ.

The range of market conditions that may make it inappropriate to issue a cash warning is broad. We think firms, responding to real time market conditions, using their professional judgement, and knowledge of their consumers are better placed than relying on a pre-set threshold by the FCA to decide when to temporarily stop sending cash warnings. We acknowledge that firms may choose different thresholds for when to suspend cash warnings, but we think the overall risk to consumers will be low as firms will still need to act to deliver good outcomes for consumers as required by the Consumer Principle in the Consumer Duty.

Record keeping

3.40 In addition to existing rules and guidance on record-keeping set out in our Handbook at SYSC 9.1, we proposed a list of other areas where we think it is important that NWP providers keep good records for cash warnings. Examples included:

- dates of assessments, with the number of consumers assessed and the number of consumers who meet the conditions
- a breakdown of the above numbers between advised and non-advised consumers, and a further breakdown between consumers who were customers before and after these requirements come into force
- of those consumers who meet the conditions, the number who continue to meet the conditions in subsequent assessments, to track how consumers move out of significant cash holdings over time

3.41 We asked:

> **Q20:** ***Do you agree that we should provide guidance on the data we would expect providers to retain? Are there other data you think important?***

Feedback and our response

3.42 Twenty-five respondents answered this question, with all agreeing on the need to keep data.

3.43 Some respondents asked whether it was necessary to retain data on customers before and after implementation of our proposals, while others suggested we simplify the data we require providers to retain.

Our response

We will proceed as consulted on. As set out in CP21/32, good record keeping will help providers show that they have met all their requirements, particularly around communicating with consumers and. It will also help them show that they are complying with product governance rules. The data we have requested will enable us to identify changes that have happened because of our proposals.

Implementation timeline

3.44 We proposed that providers be given 12 months to implement these proposals from the date we publish our final rules and guidance,

3.45 We asked:

> **Q21:** ***Do you agree with our proposed implementation timeline for cash warnings?***

Feedback and our response

3.46 Ten respondents agreed with our proposed implementation timeline.

3.47 As with the implementation of the default option, the majority of respondents who disagreed requested an 18-month implementation period due to the number of regulatory initiatives that had to be implemented during this period.

Our response

We have retained the 12-month implementation period for cash warnings. As mentioned in response to Q11, we are conscious that firms must implement the Consumer Duty and other regulatory initiatives in this period, in a challenging economic climate. However, this must be balanced against the ongoing harm to consumers. We think a 12-month implementation period achieves a fair balance between protecting consumers and taking into account the burden on firms.

In the current environment, with elevated levels of inflation, we encourage firms that are able to send out cash warnings before the 12-month period to do so to support those consumers who may be invested in cash.

4 Cost benefit analysis

4.1 We published a cost benefit analysis (CBA) of our proposals in Annex 2 of CP21/32.

4.2 We asked:

> **Q22:** ***Do you have any comments on our cost benefit analysis?***

Feedback and our response

4.3 The majority of respondents said they had no further comments on the CBA. Nine respondents thought we had over-estimated the benefits of our proposals but did not quantify the extent to which we had done so.

4.4 A few respondents suggested that take up of the default option may be lower than the figures in the CBA. This was based on observations of the take up of investment pathways.

Our response

Respondents did not provide detailed evidence or data that could be taken into account to produce an updated CBA. We consider that the targeted amendments we have made to our rules in response to consultation feedback have an insignificant effect on the breakeven position between costs and benefits overall – therefore we have not updated the CBA in this Policy Statement.

Annex 1
List of non-confidential respondents

Association of British Insurers

Abrdn

Aegon

AJ Bell

Association of Member Directed Pension Schemes

atSIPP

Capita Life & Pensions Regulated Services

CMC Markets Investments Ltd

Curtis Bank

Dentons Pension Management Limited

Digital Moneybox Limited

Financial Services Consumer Panel

Gaudi Ltd

Hargreaves Lansdown

Institute and Faculty of Actuaries

Investment and Life Assurance Group

Interactive Investors

James Hay Administration Company

John Griffiths

Legal and General

M&G

NFU Mutual

Phoenix Group

Quilter plc

Scottish Widows

St. James's Place

The Society of Pension Professionals

The Investing and Saving Alliance

Vanguard

Annex 2
Abbreviations used in this paper

Abbreviation	Description
ABS	Annual Benefit Statement
CBA	Cost Benefit Analysis
COBS	Conduct of Business Sourcebook
CP	Consultation Paper
DP	Discussion Paper
ESG	Environmental, Social and Governance
FCA	Financial Conduct Authority
FS	Feedback Statement
GAA	Governance Advisory Arrangement
HMRC	Her Majesty's Revenue and Customs
IGC	Independent Governance Committee
NWP	Non-workplace pension
PERG	Perimeter Guidance Manual
PROD	Product Governance Sourcebook
PS	Policy Statement
SIPP	Self-Invested Personal Pension
SYSC	Senior Management Arrangements, Systems and Controls
TPR	The Pensions Regulator

All our publications are available to download from www.fca.org.uk. If you would like to receive this paper in an alternative format, please call 020 7066 7948 or email: publications_graphics@fca.org.uk or write to: Editorial and Digital team, Financial Conduct Authority, 12 Endeavour Square, London, E20 1JN

Sign up for our **news and publications alerts**

Appendix 1
Made rules (legal instrument)

NON-WORKPLACE PENSIONS INSTRUMENT 2022

Powers exercised

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

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

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

Commencement

C. This instrument comes into force on 1 December 2023.

Amendments to the Handbook

D. The modules of the FCA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below.

(1)	(2)
Glossary of definitions	Annex A
Conduct of Business sourcebook (COBS)	Annex B
Product Intervention and Product Governance sourcebook (PROD)	Annex C

Amendments to material outside the Handbook

E. The Perimeter Guidance manual (PERG) is amended in accordance with Annex D to this instrument.

Notes

F. In the annexes to this instrument, the "notes" (indicated by "*Editor's note:*") are included for the convenience of readers, but do not form part of the legislative text.

Citation

G. This instrument may be cited as the Non-Workplace Pensions Instrument 2022.

By order of the Board
24 November 2022

Annex A

Amendments to the Glossary of definitions

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

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

cash-like investments	*cash* or *near cash*, units in a *regulated money market fund*, or units in a fund authorised as a money market fund for the purposes of the *UK* version of Regulation (EU) No 2017/1131 of the European Parliament and the Council of 14 June 2017 on money market funds, which is part of *UK* law by virtue of the *EUWA*.
default option	an *investment* or group of *investments* offered for inclusion in a *non-workplace pension* and designed to meet the needs, objectives and characteristics of a typical *non-advised client* in the target market.
lifestyling	an investment strategy that aims, as the *member of a pension scheme* approaches retirement, progressively to reduce the potential for significant variation caused by market conditions in the value of the member's accrued rights.
non-advised client	(in *COBS* 19 and *PROD* 6) a *retail client* in relation to whom a *firm* has not been able to determine, on reasonable grounds, that the client has received, or will receive, a *personal recommendation* or investment management services for the purposes of *COBS* 19.12.5R.
non-workplace pension	the individual arrangements of a member of a *non-workplace pension scheme* who is a *retail client* with the scheme's *operator*.
non-workplace pension scheme	a *personal pension scheme* or *stakeholder pension scheme*, in situations where the scheme will be used to provide members with benefits other than employment benefits.
target date fund	a *fund* whose investment strategy is adjusted over time based on when investors in the *fund* are expected to access their investment.

Amend the following definitions as shown.

distribute	…
	(3) (in relation to *PROD* 1.4.3AG, 1.4.3BR and 1.4.3CG, *PROD* 1.6.1R and *PROD* 6) *arranging* a *pathway investment* <u>or a *default option*</u>.

manufacture …

(3) (in relation to *COBS* 19, *PROD* 1.6 and *PROD* 6) creating, developing, designing, issuing, operating and/or underwriting a *pathway investment* or a *default option*.

…

manufacturer …

(5) (in relation to *COBS* 19, *PROD* 1.6 and *PROD* 6) a *firm* which creates, develops, designs, issues, operates and/or underwrites a *pathway investment* or a *default option*.

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

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

19 Pensions supplementary provisions

…

19.10 Drawdown, investment pathways and cash warnings

Definitions

19.10.1 R In *COBS* 19.10:

(1) ~~“cash-like investments” includes *cash* or *near cash*, units in a *regulated money market fund*, or units in a fund authorised as a money market fund for the purposes of the UK version of the European Parliament and Council Regulation on money market funds (2017/1131/EU), which is part of UK law by virtue of the *EUWA*;~~ [deleted]

…

…

Purpose

…

19.10.6 G This section specifies the circumstances where a *firm* dealing with a non-advised *retail client* in relation to the investment of the sums or assets in their drawdown fund must:

(1) …

…

(3) ensure that *retail clients* investing wholly or predominantly in ~~cash-like investments~~ *cash-like investments* make an active decision to do so; ~~and~~

(4) provide warnings to *retail clients* investing wholly or predominantly in ~~cash-like investments~~ *cash-like investments*;

…

…

Information, including cash warnings, for clients who have not decided to invest at least 50% of their drawdown fund in pathway investments

…

19.10.30 R Before carrying out the *retail client's* request referred to in *COBS* 19.10.8R, the *firm* must:

(1) …

(2) subject to *COBS* 19.10.32R, if carrying out the *retail client's* request referred to in *COBS* 19.10.8R would result in more than 50% of the *retail client's* drawdown fund being invested in ~~cash-like investments~~ *cash-like investments*:

(a) ensure that the *retail client* has made an active decision to invest in ~~cash-like investments~~ *cash-like investments*; and

…

…

19.10.31 G A *retail client's* signature on a pre-populated form, whether in paper or electronic format, is not, by itself, sufficient evidence of an active decision to invest in ~~cash-like investments~~ *cash-like investments*.

19.10.32 R (1) …

(2) When ascertaining whether more than 50% of the *retail client's* drawdown fund is invested in ~~cash-like investments~~ *cash-like investments*, a *firm* may ignore sums or assets in relation to which a *discretionary investment manager* or a financial advisor has permission to *execute* investment decisions. A *firm* exercising this option must take the steps in *COBS* 19.10.30R(2) if the client's decision would result in more than 50% of the remainder of the drawdown fund being invested in ~~cash-like investments~~ *cash-like investments*.

(3) If it is not possible for the firm to identify the assets in a *retail client's* drawdown fund, despite making all reasonable efforts, a *firm* may take into account all investments in the *retail client's personal pension scheme* or *stakeholder pension scheme*. In such a case, a *firm* must take the steps in *COBS* 19.10.30R(2) if the client's decision would result in more than 50% of the value of the client's *personal pension scheme* or *stakeholder pension scheme* being invested in ~~cash-like investments~~ *cash-like investments*.

19.10.33 G To ascertain whether more than 50% of a *retail client's* drawdown fund is invested in ~~cash-like investments~~ *cash-like investments*, a *firm* should take reasonable steps to obtain up-to-date information, and should use the most recent information it has access to.

…

Cash warnings

…

19.10.38 R The cash warning must:

(1) …

(2) using plain language, warn the *retail client* that:

(a) more than half of their eligible drawdown fund is invested in ~~cash-like investments~~ *cash-like investments*; and

…

…

…

Record keeping

…

19.10.47 G A *firm* to which the record-keeping rules in *SYSC* 3 (Systems and controls) or *SYSC* 9 (Record-keeping) apply should maintain a record of its compliance with the requirements in this section including:

(1) …

…

(16) evidence of how each *retail client* who received an initial cash warning made an active choice, in accordance with *COBS* 19.10.30R(2)(a), to invest more than 50% of their drawdown fund in ~~cash-like investments~~ *cash-like investments*;

…

…

After *COBS* 19.11 (Pensions dashboards), insert the following new section. The text is all new and is not underlined.

19.12 Non-workplace pensions: default options and cash warnings

Definitions

19.12.1 R In *COBS* 19.12:

(1) 'cash warning' is the warning in *COBS* 19.12.31R;

(2) 'distributes' includes having an arrangement with a third party to arrange an *investment,* or to promote *platform services* that distribute *investments*;

(3) 'filtering tool' means a tool whereby a *firm* makes the list of the *investments* it sells easier to search by allowing the *customer* to filter products based on factors presented by the *firm* and selected by the *customer*, and showing to the *customer* the *investments* that meet the factors selected by the *customer*; and

(4) 'pre-purchase questioning tool' means a tool which involves putting a sequence of questions in order to extract information from a *person* to help them best select an *investment* that meets their needs. A decision tree is an example of a pre-purchase questioning tool. The process of going through the questions will usually narrow down the range of options that are available.

Application of default option rules

19.12.2 R *COBS* 19.12.10R to *COBS* 19.12.22G apply to an *operator* of a *non-workplace pension scheme* that:

(1) offers, distributes or promotes *investments*, or promotes *platform services* that distribute *investments*, in relation to their inclusion in a *non-workplace pension* of the *operator*; or

(2) accepts, for inclusion in a *non-workplace pension*, *investments* which are offered, distributed or promoted by another *person* where that other *person*, or another *person* connected to it, also arranges for the *retail client* to enter into the *non-workplace pension* with the *operator*.

19.12.3 G The effect of *COBS* 19.12.2R is that *COBS* 19.12.10R to *COBS* 19.12.22G:

(1) do not apply where an *operator* only *arranges* an *investment* for inclusion in, or the provision of *platform services* in respect of, a *retail client's non-workplace pension*, at the request of the *retail client*. In these circumstances, therefore, the *operator* does not offer, distribute or promote any *investments*, nor does it promote *platform services* that distribute *investments.*

(2) apply where an *operator* accepts, for inclusion in a *retail client's non-workplace pension,* an *investment* offered, distributed or promoted by a third party, including a *platform services provider* or an introducer, where that third party or someone connected to that third party also arranges for the *retail client* to enter into the *non-workplace pension* with the *operator* unless the *retail client* has received or will receive, either as part of transactional or ongoing advice, a *personal recommendation* in relation to the *investment* of

their contributions to, or assets in, the *non-workplace pension* (see *COBS* 19.12.5R).

19.12.4 R *COBS* 19.12.10R to *COBS* 19.12.22G do not apply where an *operator* starts treating a *retail client's* workplace pension arrangements as a *non-workplace pension* after the *retail client* has become a deferred member of the relevant *qualifying scheme*, so long as the *firm* does not offer, distribute or promote to the *retail client* any *investments* or *platform services* other than those available in connection with the former workplace pension arrangements, including the *default arrangement* and any *investments* available on a self-select basis.

Exclusion from default option rules in relation to advised clients

19.12.5 R *COBS* 19.12.10R to *COBS* 19.12.22G do not apply in relation to a *non-workplace pension* where the *firm* has determined, on reasonable grounds, that the *retail client*:

(1) has received or will receive, either as part of transactional or ongoing advice, a *personal recommendation* in relation to the investment of their contributions to, or assets in, the *non-workplace pension*; or

(2) has appointed an *investment manager* in relation to the investment of the *retail client's* contributions to, or assets in, the *non-workplace pension*.

19.12.6 G A *firm* will not have reasonable grounds to determine that a *retail client* has received, or will receive, a *personal recommendation* for the purpose of *COBS* 19.12.5R(1) if the determination is based solely on information that:

(1) is over 12 *months* old;

(2) the *retail client* is in, or transferring from, an advised product; or

(3) the *retail client* provides *remuneration* to an *adviser* in relation to other *investments*.

Application of cash warning rules

19.12.7 R *COBS* 19.12.23R to *COBS* 19.12.33G apply to an *operator* of a *non-workplace pension scheme*.

19.12.8 R *COBS* 19.12.23R to *COBS* 19.12.33G do not apply in relation to a *non-workplace pension* where the *firm* has determined, on reasonable grounds, that the *retail client* has appointed an *investment manager* in relation to the investment of their contributions to, or assets in, the *non-workplace pension*.

Purpose

19.12.9 G (1) The purpose of this section is to specify the circumstances where a *firm* must:

(a) offer a *default option* to a *non-advised client* in connection with their *non-workplace pension*; and

(b) provide warnings to a *retail client* who has invested, for a sustained period of time, over a certain percentage of their *non-workplace pension* in *cash-like investments.*

(2) The *default option* rules in *COBS* 19.12 are designed to help *non-advised clients* who are generally unable or unwilling to engage with *investment* decisions, or find it difficult to identify appropriate *investments* for inclusion in their *non-workplace pensions*, including where questionnaires or filtering tools are used. The purpose of the rules in *COBS* 19.12 is to help these *non-advised clients* to choose an appropriate *investment* option.

Requirement to offer a default option

19.12.10 R *A firm* must offer its *retail clients* a *default option* for inclusion in the *non-workplace pensions* it operates for those clients.

19.12.11 R A *firm* must not:

(1) offer more than one *default option* to each *retail client*; or

(2) make the decision as to which *default option* to offer to each *retail client* by depending on the *retail client's* answers to questions set out in a pre-purchase questioning tool or a filtering tool.

19.12.12 G A *firm* may, as a single *default option*, offer a series of different *target date funds* that depend on *retail clients'* target retirement dates.

When and where to offer a default option

19.12.13 R A *firm* must offer the *default option*:

(1) at the time the *retail client* enters into the *non-workplace pension* operated by the *firm* (regardless of whether an initial cash contribution is made at this stage); and

(2) again at the time the *retail client* makes their initial cash contribution (if one has not already been made on entry) into the *non-workplace pension*,

unless the *retail client* is, at the point of entry into the *non-workplace pension* with the *firm*, only transferring in *investments* they already hold elsewhere and will continue to use the investment strategy associated with those *investments* when making requests of the *firm*.

19.12.14 G Where a *retail client*:

(1) makes their initial cash contribution at the point of entry into the *non-workplace pension* with the *firm*, the *firm* will need to bring the existence of the *default option* to the attention of the *retail client* at that stage; and

(2) makes their initial cash contribution after the point of entry into the *non-workplace pension* with the *firm,* the *firm* will need to comply with *COBS* 19.12.13R by offering the *default option* both at the stage at which the *client* enters the *non-workplace pension* and again at the point they make their initial cash contribution.

19.12.15 R Additionally, where a *firm*, or any other *person* involved in the offer, distribution or promotion of *investments* for inclusion in a *non-workplace pension* of the *firm*:

(1) sets out, in menus or otherwise, the other *investments* available to the *retail client* for inclusion in their *non-workplace pension*, the *firm* must set out the *default option* in a location most likely to bring it to the attention of that *retail client*;

(2) makes available pre-purchase questioning tools or filtering tools that enable a *retail client* to select *investments* for inclusion in their *non-workplace pension*, the *firm* must set out the *default option* alongside those tools.

19.12.16 G It is unlikely that complying with *COBS* 19.12.15R(1) would require a *firm* to set out the *default option* in every menu, or in every level of a menu, where other *investments* are set out.

How to present the default option

19.12.17 R A *firm* must present a *default option*:

(1) when complying with *COBS* 19.12.13R, prominently and on a standalone basis; and

(2) when complying with *COBS* 19.12.15R, with at least equal prominence to any other *investment*, pre-purchase questioning tool or filtering tool made available to *retail clients* alongside the *default option*.

19.12.18 R When complying with *COBS* 19.12.13R and *COBS* 19.12.15R, a *firm* must ensure that it:

(1) labels a *default option* in a sufficiently clear way to give an indication of the nature of it and also to distinguish it from the *firm's* other offerings;

(2) sets out, in a clear and prominent way, the aims of the *default option*, explains that the *default option* has been designed to meet the needs, objectives and characteristics of a typical *non-advised client* in the target market for the *default option*, and sets out what the *manufacturer* considers those needs, objectives and characteristics to be; and

(3) makes it clear that the *default option* is not tailored to the specific needs, objectives or characteristics of each *retail client*, and that if the *retail client*:

(a) considers that their needs, objectives and characteristics may fall outside those of the typical *non-advised client* in the target market as described by the *firm*, they may wish to consider other investment options;

(b) wishes to ensure that the *non-workplace pension* and any *investments* included in it (including the *default option*) are suitable for them, the *retail client* should consider seeking *investment advice*.

Preparing to offer a default option

19.12.19 R A *firm* must be in a position to offer a *default option* in good time before it has to offer the *default option* pursuant to *COBS* 19.12.10R, in order to allow for sufficient internal product governance.

19.12.20 G The *default option* may be *manufactured* by either the *operator* alone, by another *firm*, or by both, and *distributed* by either the *operator* alone, or by the *operator* and another *firm*.

19.12.21 G *Manufacturers* and *distributors* of *default options* must comply with the applicable product governance requirements in *PROD*. Where the manufacturing is done by another *firm* (either alone or with the *operator*), the *operator* is still responsible for the obligations under *COBS* 19.12.10R to *COBS* 19.12.18R.

19.12.22 G (1) Where *firms* decide to replace a *default option*, they may need to consider whether it would be appropriate to transfer existing clients to the new *default option*.

(2) This may be the case, for example, if the transfer is required to prevent consumer harm and avoid risking non-compliance with our *rules*, for example *Principle* 6. This could be the case where *firms* determine that the *default option* no longer meets the applicable product governance requirements in *PROD* and existing clients are likely to suffer harm as a result.

(3) If *firms* decide to transfer existing clients to a new *default option*, they will need to consider the information needs of their clients, and

communicate to them appropriately and in good time, in a manner that is clear, fair and not misleading.

(4) *Firms* are required to have appropriate contractual arrangements in place (including contractual powers that are fair and transparent and comply with the *CRA*) to enable them to transfer existing *clients* to a new *default option* and to comply with their obligations under the *regulatory system*.

Cash warnings: conditions

19.12.23 R At least once during every 3-*month* period, for each of the *non-workplace pensions* that *retail clients* have entered into with the *firm*, the *firm* must assess whether the following conditions are met at the time of the assessment:

(1) more than 25% of the *non-workplace pension* is invested in *cash-like investments*, excluding any *cash-like investments* held in connection with *lifestyling* or within a *target date fund*;

(2) the amount of the cash holding in (1) is greater than £1,000;

(3) the conditions in (1) and (2) were also met in all the other assessments carried out during the 6-*month* period preceding the day of the assessment; and

(4) the *retail client* is more than 5 years away from:

(a) normal minimum pension age, as defined in primary legislation from time to time; or

(b) if lower, a protected pension age.

19.12.24 R For the purposes of *COBS* 19.12.23R, the start of the 3-*month* period is:

(1) initially determined by reference to the date members enter into their *non-workplace pensions* with the *firm*; and

(2) after the initial 3-*month* period, by reference to the date when, for each *retail client*, the *firm* last carried out, or should have carried out, the assessment under the *rule*.

Cash warnings: timing

19.12.25 R If all the conditions in *COBS* 19.12.23R are met, the *firm* must provide the *retail client* with a cash warning within an appropriate timeframe after the date when the assessment in that *rule* was carried out.

19.12.26 G For the purposes of *COBS* 19.12.25R, an 'appropriate timeframe' is likely to be within 3 *months* of carrying out the assessment in *COBS* 19.12.23R, unless the current market conditions would make it inappropriate to warn the *retail client* about their cash holdings within that timeframe, although

providing the cash warning later than 6 *months* after the date of the assessment is unlikely to be appropriate.

19.12.27 R If a *firm* has provided a cash warning pursuant to *COBS* 19.12.25R, the requirement in *COBS* 19.12.25R does not apply again until after 1 year of the *firm* providing the previous cash warning.

19.12.28 G Notwithstanding *COBS* 19.12.27R, a *firm* can choose to provide a new cash warning during the year following the previous cash warning, in which case *COBS* 19.12.27R would apply from the date when the new cash warning is provided.

19.12.29 G Where the condition in *COBS* 19.12.23R(4) is no longer met, a *firm* should consider whether it would be appropriate to keep providing the cash warning up until the time a *retail client* accesses their pension.

19.12.30 G A *firm* may send the cash warning with other client communications, provided that the cash warning is included in a document separate to those other client communications.

Cash warning: form and content

19.12.31 R The cash warning at *COBS* 19.12.25R must:

(1) be provided in a *durable medium*;

(2) using plain language, warn the *retail client* that:

(a) more than 25% of their *non-workplace pension* is invested in *cash-like investments*; and

(b) the value of their *non-workplace pension* is at risk of being eroded by inflation;

(3) include a generic example (provided as an explanation, an illustration or both) of how inflation erosion would affect a £10,000 cash pot over 10 years, assuming 0% interest and using a measure of inflation generally accepted in the *United Kingdom*; and

(4) inform the *retail client* that they should consider whether their current investments are likely to grow sufficiently to meet their objectives.

19.12.32 G The *firm* should also:

(1) inform the *retail client* that:

(a) the cash warning is not advice or a substitute for it; and

(b) the value of any *investment* can fall as well as rise;

(2) explain to and/or illustrate for the *retail client* that different types of *investment* have a different balance of risk to potential gain; and

(3) include in the cash warning a statement to the effect that, where applicable, the *firm* makes available *investments* for inclusion in *non-workplace pensions*, including the *default option*.

19.12.33 G In the *FCA's* view, the Consumer Prices Index is a national index of retail prices and so may be used as a measure of the current inflation rate for the purposes of *COBS* 19.12.31R(3).

Record keeping

19.12.34 G A *firm* to which the record-keeping rules in *SYSC* 3 (Systems and controls) or *SYSC* 9 (Record-keeping) apply will need to maintain a record of its compliance with the requirements in this *COBS* 19.12 section including, where relevant, how it has determined on reasonable grounds (including records of the evidence it has relied upon) that, in accordance with *COBS* 19.12.5R, a *retail client* is not a *non-advised client*.

19.12.35 R A *firm* must also maintain a record of:

(1) the number of *non-advised clients* entering into a *non-workplace pension* with the *firm* each year;

(2) the number of those *retail clients* in (1) who chose the *default option*;

(3) the number of *retail clients* not included in (1) that choose the *default option* each year, distinguishing between *retail clients* who were *clients* of the *firm* before *COBS* 19.12.10R to *COBS* 19.12.22G came into force and those who became *clients* later;

(4) the volume of contributions made by *retail clients* to the *default option* each year;

(5) the volume of assets under management attributable to the *default option*;

(6) a description of the product approval process for the *default option* and of any reviews undertaken in compliance with *PROD* 6;

(7) in relation to cash warnings, differentiating between advised clients and *non-advised clients*, as well as between those *retail clients* who were *clients* of the *firm* before *COBS* 19.12.23R to *COBS* 19.12.33G came into force and those who became *clients* later:

(a) the dates when assessments were carried out, alongside the number of *retail clients* assessed on those dates;

(b) of the *retail clients* in 7(a), the number who met the conditions at *COBS* 19.12.23R; and

(c) of the *retail clients* in 7(b), the number who continue to meet the conditions at *COBS* 19.12.23R in subsequent assessments.

Amend the following as shown.

TP 2 Other Transitional Provisions

[*Editor's note:* TP 2 takes into account the changes made by FCA 2022/38, which comes into force on 30 March 2023.]

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
…					
2.45	…				
2.46	*COBS* 19.12.10R, *COBS* 19.12.15R	R	*COBS* 19.12.10R and *COBS* 19.12.15R do not apply in relation to a *firm's* existing *non-advised clients* as of 1 December 2023, provided the *firm* does not enter into new *non-workplace pensions* with *non-advised clients* after 1 December 2023.	From 1 December 2023 indefinitely	1 December 2023
2.47	*COBS* TP 2.46R, *COBS* 19.12.10R, *COBS* 19.12.15R	G	The effect of *COBS* TP 2.46 is that a *firm* will not be required to offer a *default option* in accordance with *COBS* 19.12.10R and *COBS* 19.12.15R where the *firm* has legacy only business. A *firm* has legacy only business for the purpose of *COBS* TP 2.46 where it does not enter into a new *non-workplace pension* with *non-advised clients* after 1 December 2023. For the avoidance of doubt, where a *firm* does not enter into new *non-workplace pensions* with *non-advised clients* after 1 December 2023, but still continues to	From 1 December 2023 indefinitely	1 December 2023

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			offer, distribute or promote new *investments*, or promote *platform services* that distribute new *investments* to (or top-up existing *investments* for) existing *non-advised clients* to include in their existing *non-workplace pension*, the *firm* will still be considered to have 'legacy only business'. As a result, it will not be required to offer a *default option* in that situation.		
2.48	*COBS* 19.12.23, *COBS* 19.12.24(1)	R	For the purposes of *COBS* 19.12.23R and 19.12.24(1), the start of the 3-*month* period is initially determined, in respect of existing members on 1 December 2023, by reference to that date, and not by reference to the date they entered into their *non-workplace pensions* with the *firm*.	From 1 December 2023 to 1 March 2024	1 December 2023

Annex C

Amendments to the Product Intervention and Product Governance sourcebook (PROD)

In this Annex underlining indicates new text, unless otherwise stated.

1		**Product Intervention and Product Governance Sourcebook (PROD)**
…		
1.3		**Application of PROD 3**
…		
		Manufacturing pathway investments and default options
1.3.16	G	A *firm* that is within the scope of *PROD* 3 (Product governance: MiFID) when it *manufactures pathway investments* or *default options* other than in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*, is also subject to *PROD* 6 (Product governance: additional provisions for pathway investments and default options) as *guidance* with respect to that *manufacturing* activity (see *PROD* 1.6.1R(3)).
…		
1.4		**Application of PROD 4**
…		
		Manufacturing and distributing pathway investments and default options
1.4.3A	G	A *firm* that is within the scope of *PROD* 4 (Product governance: IDD) when it *manufactures pathway investments* or *default options* other than in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*, is also subject to *PROD* 6 (Product governance: additional provisions for pathway investments and default options) as *guidance* with respect to that *manufacturing* activity (see *PROD* 1.6.1R(2)).
1.4.3B	R	Where a *firm*: (1) *manufactures* or *distributes pathway investments* or *default options* in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*; and (2) is not otherwise within the scope of the *rules* or *onshored regulations* in *PROD* in relation to that *manufacturing* or *distribution* activity, then *PROD* 4, *PROD* 1.4.4UK and *PROD*

1.4.10G, apply with respect to that *manufacturing* or *distribution* activity.

1.4.3C G The effect of *PROD* 1.4.3BR is to apply *PROD* 4 to any *firm*, such as a *SIPP* operator, which:

(1) *manufactures* or *distributes pathway investments* or *default options* in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*; and

(2) before the entry into force of *PROD* 1.4.3BR, was not subject to the *rules* or *onshored regulations* in *PROD*.

…

Effect and interpretation of PROD 1.4 and PROD 4 for certain manufacturers and distributors of pathway investments and default options

1.4.6A R A *firm* to which *PROD* 1.4.3BR applies must:

(1) comply with provisions marked "UK" in *PROD* 1.4 and *PROD* 4 as if they were *rules*; and

(2) read terms or phrases found in *PROD* 1.4 or *PROD* 4 as follows:

(a) terms referred to in column (1) of the table below have the meaning indicated in the same row of column (2) of the table;

(b) terms relating to insurance or insurance products have the meaning of the corresponding term relevant in the context of *pathway investments* or *default options*; and

(c) terms or phrases which are only relevant to *firms manufacturing* or *distributing* insurance products may be disregarded.

This table belongs to *PROD* 1.4.6AR(2)(a).

(1)	(2)
…	...
"insurance-based investment products"	*pathway investment* or *default option*
…	...
"insurance product"	*pathway investment* or *default option*

…	...

…

1.6 Application of PROD 6

1.6.1 R *PROD* 6 applies to a *firm*:

(1) that *manufactures* or *distributes pathway investments* or *default options* in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*;

(2) within the scope of *PROD* 4 when *manufacturing pathway investments* or *default options*, other than in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*, as *guidance* with respect to that *manufacturing* activity;

(3) within the scope of *PROD* 3 when *manufacturing pathway investments* or *default options*, other than in connection with its operating of a *retail client's personal pension scheme* or *stakeholder pension scheme*, as *guidance* with respect to that *manufacturing* activity.

…

6 Product governance: additional provisions for pathway investments and default options

…

After PROD 6.3 (Distribution of pathway investments), insert the following new sections. The text is not underlined.

6.4 Manufacture of default options

6.4.1 R When designing a *default option*, a *manufacturer* should take into account, among other considerations, the fact that *COBS* 19.12 requires *operators* to offer the *default option* to *non-advised clients* for inclusion in their *non-workplace pensions.* As a result, the *default option* must be designed to be compatible with the needs, characteristics and objectives of a typical *non-advised client* in the *default option's* target market.

6.4.2 R A *manufacturer* must also ensure that:

(1) when specifying the investment strategy of the *default option*, and its costs and charging structure, it takes into account what the *manufacture*r considers, on reasonable grounds, to be the likely needs, objectives and characteristics of a typical *non-advised client* in the target market;

(2) the investment strategy of the *default option*:

(a) takes into account the target retirement age of a typical *non-advised client* in the target market, and their likely strategy for accessing their pension;

(b) includes *lifestyling*, unless *lifestyling* is not appropriate for the needs, objectives and characteristics of the typical *non-advised client* in the target market or the *default option* is based on *target date funds*; and

(c) seeks growth, while managing risks, through an appropriate and diversified asset allocation; and

(3) the *default option* has appropriate and competitive price and charges, which bear a reasonable relationship with the services being provided.

6.4.3 G *Manufacturers* are expected to take reasonable steps to understand the likely needs, objectives and characteristics of a typical *non-advised client* in the *default option's* target market. This could include carrying out sufficient research and consumer testing in support of its conclusions. What amounts to a typical *non-advised client* may be based on the needs, objectives or characteristics that are most commonly seen among *non-advised clients* within the target market.

6.4.4 R *Manufacturers* must review their *default options* at least once every 3 years to ensure that they:

(1) remain consistent with the needs, characteristics and objectives of a typical *non-advised client* in the target markets; and

(2) are being *distributed* to their target markets.

6.5 Distribution of default options

6.5.1 R A *firm* must not *distribute* a *default option* unless it is compatible with the needs, characteristics and objectives of the *retail clients* to whom the *firm* distributes the *default option*.

6.5.2 R When carrying out the compatibility assessment in *PROD* 6.5.1R, a *firm* must also take into account:

(1) the *manufacturer's* compliance with the requirements in *PROD* 6.4; and

(2) the financial strength of the *manufacturer*.

6.5.3 R A *firm* must review the distribution arrangements for the *default options* it distributes at least every 3 years.

Annex D

Amendments to the Perimeter Guidance manual (PERG)

In this Annex, underlining indicates new text.

8 Financial promotion and related activities

…

8 Annex 1 Examples of what is and is not a personal recommendation and advice

…

(F) Miscellaneous		
(1) **Example**	**(2)** **Is there a personal recommendation?**	**(3)** **Is this regulated advice for someone other than a firm with an appropriate authorisation?**
…		
(36) A *firm* gives a cash warning to a *retail client* in accordance with the requirements in *COBS* 19.10.38R and the *guidance* in *COBS* 19.10.39G, or in accordance with the requirements in *COBS* 19.12.31R and the *guidance* in *COBS* 19.12.32G.	No. This is not a recommendation to *buy*, *sell*, subscribe for, exchange, redeem, hold or underwrite a particular *investment*; or exercise or not exercise any right conferred by such an investment to *buy*, *sell*, subscribe for, exchange or redeem such an *investment*.	No. This is not advice on the merits of *buying*, holding or *selling* a particular *investment*.

Pub ref: 007938

© Financial Conduct Authority 2022
12 Endeavour Square London E20 1JN
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk
All rights reserved