



# **Standards for the provision of pensions guidance by designated guidance providers: cost benefit analysis**

February 2015

In this cost benefit analysis we assess the costs and benefits arising from Policy Statement 14/17 *Retirement Reforms and the guidance Guarantee*, including feedback on CP14/11.

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Abbreviations in this document

<b>DC</b>	Defined contribution
<b>DGPs</b>	Designated guidance providers
<b>FCA</b>	Financial Conduct Authority
<b>TPAS</b>	The Pensions Advisory Service

# 1 Overview

## Introduction

- 1.1 In the 2014 Budget the Government announced reforms to retirement options including a proposal that all consumers with Defined Contribution (DC) pensions should be entitled to access free impartial guidance at retirement about their options when accessing their pension savings– the 'Guidance Guarantee'. This has recently been launched under the brand Pension Wise and will take effect from 6 April 2015.
- 1.2 In November, we (the FCA) published near final rules<sup>1</sup> requiring firms to direct consumers to the new service and to set standards for the Treasury's designated guidance providers<sup>2</sup> to meet in delivering Pension Wise. The Department for Work and Pensions (DWP) has introduced similar requirements for trust-based pension schemes.
- 1.3 In addition following a Dear CEO letter in February we are making rules to require firms to give appropriate personalised retirement risk warnings to consumers seeking to access their pension savings.
- 1.4 We are also required to monitor the designated guidance providers' compliance with these standards and to make recommendations to the designated guidance providers and the Treasury, where necessary, when providers have breached our standards. In the Policy Statement in November we outlined our proposed approach to monitoring and said we would consult on a policy on recommendations.
- 1.5 The Treasury is responsible for the overall design of the guidance service, and will lead on the digital element of delivering it, but will not be a designated guidance provider (and so not formally subject to the standards).
- 1.6 We published our near final standards in PS 14/17. The Pensions Bill also requires us to publish a cost benefit analysis. We didn't publish the cost benefit analysis at the time of the publication of the near final standards as we were keen to ensure that the cost benefit analysis reflected the final development of the guidance service itself. We are now publishing the cost benefit analysis. We are happy to receive comment but are not consulting on this cost benefit analysis. Annex A contains our compatibility statement outlining our reasons for concluding that the standards we have set for designated guidance providers are compatible with certain requirements under FSMA.

## Who does this affect?

- 1.7 This cost benefit analysis will be relevant to all those with an interest in the pensions and retirement space, including:
  - Providers of pensions and retirement products.
  - Designated guidance providers.

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<sup>1</sup> [www.fca.org.uk/your-fca/documents/policy-statements/ps14-17](http://www.fca.org.uk/your-fca/documents/policy-statements/ps14-17)

<sup>2</sup> Designated guidance providers are delivery partners appointed by the Treasury to give pensions guidance. At commencement there will be 4 designated guidance providers appointed by the Treasury being the Pensions Advisory Service (TPAS) which will provide a telephone service and the three Citizens Advice Bureaus of England and Wales, Scotland and Northern Ireland which will provide a face to face service.

- Trustees of Defined Contribution (DC) pension schemes (and schemes with a DC element).
- Employer sponsors of DC schemes (and schemes with a DC element).
- Providers of other financial services products that play a role in consumers' retirement planning.
- Those providing advice and information in this area already.
- Distributors of financial products, in particular retirement income products.
- Trade bodies representing financial services firms.
- Consumer representative bodies.
- Charities and other organisations with a particular interest in retirement and/or financial services more generally.
- Individual consumers.

## **Is this of interest to consumers?**

- 1.8 The standards and rules will affect all consumers who have DC pension funds, and those who will have these pensions in the future. They will play a key role in determining the way in which consumers interact with the pensions and retirement markets in future.

## 2 Market failure analysis

- 2.1 Given the complexities associated with the new pension flexibilities, the guidance service was established to provide consumers with a free service to give them the tools to help them to make an informed choice about what to do with their pension saving at retirement.<sup>3</sup> The objective of the FCA's standards is to set an appropriate level of quality to which the guidance service should adhere, and ensure that this level is maintained. Poor quality guidance could also result in poor consumer outcomes.<sup>4</sup>
- 2.2 There are a number of reasons why in the absence of high quality guidance consumers may make poor decisions and suffer negative outcomes. In this section we discuss these negative outcomes, their implications for what good quality guidance should look like, and identify potential market failures that may undermine the quality of the guidance service.<sup>5</sup>

### Negative outcomes from poor quality guidance

- 2.3 There are a number of potential negative outcomes associated with the options for accessing pensions if consumers make wrong decisions. We have highlighted those which we believe are the most significant.<sup>6</sup> Consumers might:
- cash in the whole pot/smaller lump sums over time and run out of money during retirement
  - buy an income drawdown product and run out of money unexpectedly or have uncertain and fluctuating income
  - delay drawing benefits and have uncertain and fluctuating income and incur unexpected losses
  - buy an annuity and choose the incorrect product/rate
- 2.4 Cashing in the whole pot/smaller lump sums may lead to consumers running out of money unexpectedly if, for example:
- they underestimate their longevity or health care needs and do not invest or adjust spending accordingly
  - tax implications reduce their expected pot
  - having released the money they make poor investment decisions such as placing their funds in scams
  - by increasing their assessable income they reduce their access to means tested benefits.
- 2.5 Equally they may suffer if their remaining pension pot reduces unexpectedly in value, or they are unable to continue to pay into their pot at the rate they expected to. Additionally, consumers may incur unexpected charges from their providers. Finally, consumers making this wrong choice could lose simply out on better options, such as:

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<sup>3</sup> The ultimate choices are up to the consumer and the objective of the guidance service is not to steer consumers to particular options, but rather ensure that they make their decision based on the correct information relevant to their circumstances.

<sup>4</sup> We define a negative outcome of poor guidance as a consumer choosing an option that does not yield the expected value because the decision was made in the absence of good information at the time.

<sup>5</sup> At the time of this analysis, a market for guidance does not yet exist, and therefore our analysis considers *potential* market failures.

<sup>6</sup> As set out previously, whether or not an option is the best for the consumer will depend on the consumers' circumstances and preferences, which we cannot judge.

- delaying withdrawing if they expect to be on a lower tax band in the future
- benefiting from future fund growth potential
- benefiting from tax benefits upon death
- buying an annuity if they prefer secured income.<sup>7</sup>

2.6 If an individual chooses to buy an income drawdown product they may run out of money unexpectedly or have uncertain and fluctuating income. As with the options above, consumers may fail to consider all the factors that could affect their reliance on and source of income and buy a drawdown product that does not cover their needs. Consumers may underestimate the need for ongoing engagement<sup>8</sup> with income drawdown and so:

- make poor investment decisions
- suffer from unexpected fluctuating income
- be forced to pay for financial advice that they did not anticipate
- get poor value for money if they fail to shop around for drawdown products.

2.7 Alternatively, consumers may choose to delay drawing benefits and have uncertain and fluctuating income and incur unexpected losses. Consumers may not understand that this option is not merely a continuation of a status quo, but may incur penalties or losses. Deferring may:

- affect the ability to continue to pay into the pension
- have implications for the fund in which the money is held (the levels of risk and return may no longer be appropriate or the provider could switch funds)
- incur charges from the provider
- lose guarantees.

2.8 Buy an annuity and choose the incorrect product/rate. Negative outcomes could arise if consumers are not aware of all the factors that determine their annuity rates. They could

- lose out on higher rates from an enhanced annuity if they are unaware they qualify
- not get the best structure of payments
- suffer unexpected tax implications
- get poor value for money if they fail to shop around for annuities.

2.9 The likelihood of consumers making wrong decisions about their pension pots and suffering any of the above negative outcomes is influenced by many different factors, including information asymmetries facing consumers and biases that affect their decision-making.

## **Negative outcomes: information asymmetries**

2.10 The options available to consumers on how they can access their pension pots are complex, and the outcomes of each option depend on a number of external considerations (such as tax implications) as well as consumers' individual

<sup>7</sup> The opportunity cost of forgoing better options applies in all cases where consumers make the wrong decision.

<sup>8</sup> Income drawdown generally involves some ongoing involvement from the consumer, such as deciding where the pot is invested and whether the amount being drawn down and remaining will be enough to live on.

circumstances. If consumers lack information about the options, or the skill to link this information to their own situations, they can make poor choices.

- 2.11 In addition, consumers may not be aware of their need for, or the availability of, other services such as regulated financial advice or debt advice that would help them make good decisions about their pension pots.<sup>9</sup> They may also not be aware of the importance of shopping around for pension products and could lose out on associated benefits.<sup>10</sup>

## **Behavioural biases**

- 2.12 Behavioural insights show that consumers often simplify decisions, which could lead to errors.<sup>11,12</sup> Consumers may overvalue the present over the future (present bias) and may place a greater value on the use of their pension pot now, or underestimate how much they will need to draw on in the future (including underestimating how long they will live, or being over-confident about their future health status).
- 2.13 In addition, when evaluating a product or future prospects, people's assessment can be influenced by 'loss aversion', whereby they can strongly prefer avoiding losses to acquiring gains. This may manifest as a preference for the status quo – staying with a known option in preference to choosing an unknown, even if a potentially more beneficial, one. Consumers facing complex decisions about their pension pot may leave their pension invested without further thought, or choose a de facto status quo like buying an annuity, which may not be the best option for them.

## **The importance of good quality guidance**

- 2.14 The above discussion highlights the important role of guidance in mitigating behavioural biases associated with complex decisions it can also reduce information asymmetries by providing consumers with the necessary information to make good decisions.
- 2.15 Poor quality guidance – which the FCA standards seek to prevent – that is unclear or overwhelms the consumer with information will not be effective in reducing the complexity of the options and may not address decision-making biases (or indeed may exacerbate them).
- 2.16 In addition, if the content of the guidance session does not contain all the necessary information about the option, or if the guider lacks the professional skill to link this information to the consumer's situation, then information symmetries will not be adequately addressed. This includes highlighting the relevance of other services such as debt advice, and the importance of shopping around.
- 2.17 If the quality of the guidance is low (including both the content and the user experience), it could undermine the reputation of the service and reduce take-up by consumers, limiting the extent of the benefits of the service.

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<sup>9</sup> For example, the implications for debt repayments of taking a lump sum from the pension.

<sup>10</sup> There is evidence that consumers currently do not shop around for retirement products. The FCA's Thematic Review of Annuities (TR14/2 February 2014), for example, found that around 80% of consumers who purchase their annuity from their existing provider could get a better deal on the open market. See <http://www.fca.org.uk/static/documents/thematic-reviews/tr14-02.pdf>

<sup>11</sup> This is particularly the case where decisions are complex, emotional, and undertaken infrequently with little opportunity for learning – all characteristic features of decisions about accessing pensions upon retirement.

<sup>12</sup> Such insights are discussed in depth in: FCA (2013) 'Applying behavioural economics at the Financial Conduct Authority', Occasional Paper 1, [http://www.fca.org.uk/static/documents/occasional\\_papers/occasional-paper-1.pdf](http://www.fca.org.uk/static/documents/occasional_papers/occasional-paper-1.pdf)

## **Potential market failures leading to poor quality guidance**

- 2.18 There are a number of factors that present a risk, such that the quality of the guidance service may not be sufficient to address all the above issues. These are only potential failures, as the market is not yet in operation, but nevertheless they provide a rationale for the setting and monitoring of standards by the FCA.

## **Potential market failures: information asymmetries**

- 2.19 There are likely to be information asymmetries between consumers and the DGPs, and consumers are unlikely to be good judges of the quality of the guidance. Guidance can be seen as a 'credence' good, with its quality difficult for customers to assess even after purchase. For example, outcomes from the guidance will only become apparent a long time after the event.<sup>13</sup> Furthermore, even if consumers were able to identify poor quality, they cannot discipline the providers by accessing an alternative service. This creates the need for an external body to provide quality assurance of the guidance service to protect consumers.
- 2.20 Further, the DGPs are currently independent organisations that together will need to provide a single guidance service. There is a risk that, in the absence of an external set of standards, the consistency of the quality and professionalism of the service may be compromised. There is also a possibility that the DGPs may underestimate the levels of cooperation and coordination required to deliver a consistent service across the delivery channels.

### ***Externalities arising from the interaction of the DGPs***

- 2.21 As the guidance service will be under a single brand, any failure on the part of one provider is likely to undermine the whole service. This in turn may damage the reputation of the service and its take-up among consumers.

## **Summary of the FCA's standards and monitoring approach**

- 2.22 The above discussion identifies a number of potential market failures that present a risk to the quality of the guidance service and provide a rationale for the setting and monitoring of standards. It also considers specific areas where poor quality guidance could lead to negative consumer outcomes, such as:
- professional skill of guiders to link consumer circumstances to options
  - sufficient information about options in the content of the guidance session
  - establishing appropriate links to wider markets, e.g. access to other services and shopping around
  - overall clarity of guidance, including consistent delivery across providers and channels
  - user experience and service take-up.

- 2.23 The FCA's standards seek to maintain the quality of the guidance service and address all the above areas. The standards cover:

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<sup>13</sup> Of course, some aspects of quality will be observable by consumers, such as practical details of the service, but others like the quality of the content of the guidance less so.

- delivery of the guidance service
- professional standards
- communications
- systems and controls
- complaints management
- content of the guidance session
- next steps, including record of the session.

2.24 We expect our monitoring to ensure compliance with these standards to include the following activities with the DGPs:

- annual self-assessment forms and gathering associated evidence
- reporting of other data not included in the self-assessment
- site visits / assessments
- ongoing ad hoc interaction with the FCA.

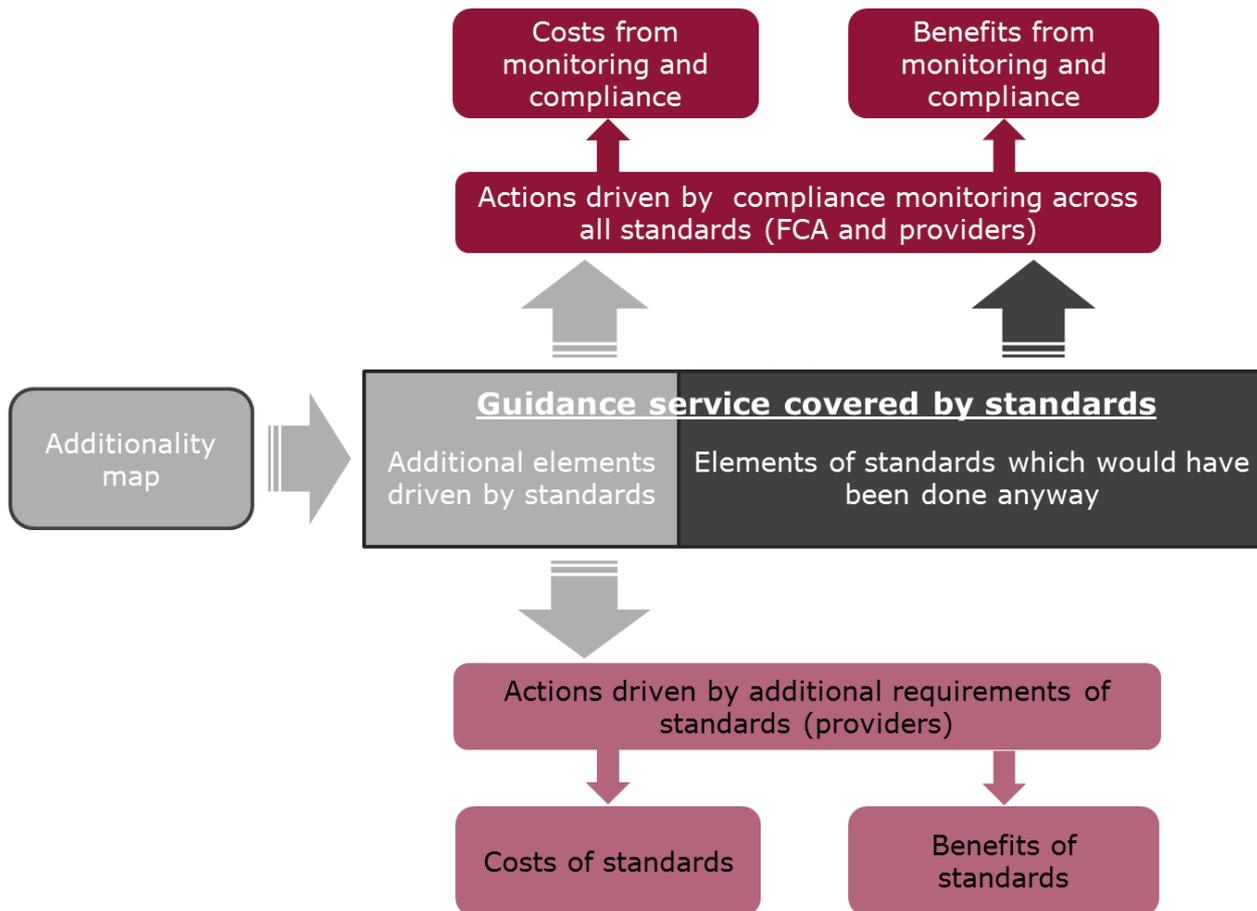
# 3 Approach to cost benefit analysis

- 3.1 It is necessary to establish a baseline, or counterfactual, against which to assess the costs and benefits of an intervention to ensure that only those attributable to the intervention are considered. The relevant counterfactual here is the provision of the guidance service in the absence of the FCA's standards and monitoring.
- 3.2 Our analysis therefore seeks to consider the additional costs and benefits arising from DGPs' compliance with the standards over and above what they would have done otherwise in delivering the guidance service. Implicit in this are the additional costs and benefits stemming from the FCA's monitoring role.<sup>14</sup>
- 3.3 As the standards have been developed at the implementation stage of the guidance service, there is no clear picture of how the DGPs would have delivered the service in the absence of the standards. To address this, we have developed an 'additionality map' to identify the specific standards that are most likely to affect the DGPs' implementation and delivery of the guidance service. The incremental costs and benefits will stem from these additional elements.
- 3.4 Costs and benefits will also stem from the FCA's role in monitoring compliance with the standards (both with respect to those standards that are additional for the DGPs and those which they would have implemented anyway).
- 3.5 The diagram below summarises our approach to analysing the costs and benefits of the standards.

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<sup>14</sup> The FCA's monitoring role is an inherent part of the standards and so we do not consider a situation in which we set standards but do not monitor DGPs' compliance.

**Figure 1: Approach to analysing costs and benefits**



3.6 Our cost benefit analysis has been developed using input from the Treasury and some of the DGPs as well as wider information and our own modelling and analysis. As the implementation of the guidance service and the development of our monitoring process are still underway, this analysis is based on the information available to date.

# 4 Analysis of benefits

4.1 The incremental benefits of the standards for DGPs are expected to flow through the following transmission mechanisms:

- additional elements of the standards lead DGPs to undertake actions they would not otherwise have done. The FCA’s monitoring role ensures compliance with the whole set of standards
- this leads to a better quality guidance service compared to a situation without the standards
- consumers are less likely to make poor decisions about their pension pots, leading to improved consumer outcomes
- adjacent to this, the increased quality of the service also encourages customer take-up, which extends the benefits of the guidance service to more consumers. Regulated financial firms (e.g. financial advisers) also benefit from greater take-up.

4.2 These transmission mechanisms are illustrated in the diagram below.

**Figure 2: Benefits transmission mechanisms**



4.3 The scale of the benefits will depend on the size of each link in this chain, that is the extent to which:

- FCA’s standards and monitoring role change the behaviour of DGPs
- these behaviour changes improve the quality of the guidance service
- a better quality guidance service improves consumers’ ability to make good decisions about their pension pots, and leads to improved consumer outcomes
- a better quality service encourages customer take-up.

4.4 It is not feasible to assess the potential size of every link in the chain. For example, to assess the extent to which good quality guidance would improve consumers’ decision-

making ability and lead to better consumer outcomes, we would need a view on how likely, and to what extent, consumers are to make poor decisions in the absence of good information, and what types of poor decisions concerning the use of their pension pots they are likely to make (i.e. what ultimate outcomes they would experience). As the market for guidance does not yet exist, a robust *ex ante* assessment of these potential failures is not feasible.<sup>15</sup>

- 4.5 Given these limitations, we do not consider it reasonably practicable to quantify the benefits arising from the standards.
- 4.6 However, we are able to form a judgement on the extent to which the standards and the FCA's monitoring role are likely to improve the quality of the guidance service over time, based on our additionality assessment and on the content of the standards (i.e. the first two links in the chain).

### **Incremental benefits from specific standards**

- 4.7 As the guidance service has been developed largely concurrently with the development of the standards, identifying clear areas of additionality from the FCA's standards is not straightforward. It is likely that many areas of the service have been influenced by the standards; however, we focus on those elements that are clearly additional, as highlighted through our discussions with the Treasury and the providers, and our own assessment. Feedback from the DGPs to whom we spoke indicated that many areas covered by the standards were either already part of their current service, which they planned to extend to the guidance service (for example, quality assurance processes and complaints handling); or, related to processes they would expect to have implemented even without the standards, such as recruiting sufficiently skilled personnel.
- 4.8 The table below summarises the elements that were identified as additional, and the associated benefits. We include our assessment of the likely scale of the impact of each element; i.e. the extent to which the standard is likely to change or reinforce DGPs' behaviour.

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<sup>15</sup> We cannot make *ex ante* assumptions about consumers' preferences and what pension options would be of more value for which consumers. An *ex post* assessment could, for example, collect information on consumers' satisfaction with their decisions regarding their pension pots and use this to estimate the level of harm in the guidance market.

**Table 1: Impact of additional elements of FCA standards**

<b>Elements of the standards (standard no.)</b>	<b>Likely scale of additional impact</b>	<b>Assessment</b>
Sufficiently skilled guiders (10, 11)	Medium-high	These standards are likely to lead to significantly greater emphasis on the recruitment and training of individuals with the skills required to link specific aspects of an individual's circumstances to the options they have in retirement. This is likely to increase the value to the individual of the guidance service.
Cooperation between providers to deliver service in accordance with standards (2), and consistent delivery of service across channels, including content (3, 19, 20)	Medium-high	These standards are likely to require significantly more coordination between providers than anticipated on a number of levels (e.g. operational, planning, content, and any ongoing changes). DGPs would have coordinated to some extent anyway, but the standards elevate this from a 'nice to have' to a focused requirement. Added benefit from coordination and consistent service is particularly important considering the large number of individual Citizens Advice bureaux.
Content of the guidance session (20)	Medium-high	The FCA's standards have been instrumental in informing the content of the guidance session, in particular the need for the guider to specifically relate the information about the options to consumers' circumstances. This will increase the value and impact of the guidance.
Service available in a timely manner (4)	Medium	DGPs would have an incentive to provide a timely service anyway, but this may be difficult to achieve from the outset. The standard raises the importance of this and will ensure focus is maintained on this requirement as the service develops.
Systems, controls and records to ensure and demonstrate compliance (14, 15)	Medium	DGPs already have quality assurance and controls. However, the standards' record-keeping period is longer than anticipated by some providers; this will provide the FCA with greater scope to monitor the long-term performance of the providers. The format of records and reports is likely to entail tailoring to facilitate the FCA's monitoring, and some additional compliance oversight by DGPs will be needed to ensure compliance with standards.
What the providers cannot do (9)	Low	The standard emphasises the boundaries between guidance and advice and maintains the impartiality of the service. Already part of providers' considerations, but the more rigorous

		definition in the standards will increase their focus on this.
Access to complaints management and record keeping (16, 18)	Low	Providers would have complaints systems regardless, but the format of the system will need to be tailored to facilitate reporting to the FCA.

## Incremental benefits from the FCA’s compliance monitoring

4.9 The market failure analysis highlights the key elements of a guidance service necessary for good consumer outcomes. Table 2 shows how the FCA’s standards uphold these areas.

**Table 2: Elements of good quality guidance and corresponding FCA standards**

Areas necessary for a good quality guidance service	Corresponding FCA standards
Professional skill of guiders to link consumer circumstances to options	Sufficiently skilled guiders (10, 11)
Sufficient information about options in the content of the guidance session	Appropriate content of guidance sessions, developed by sufficiently skilled personnel (10, 11, 12, 20, 21) Particularly important considerations consumers should be aware of (21)
Establishing appropriate links to wider markets	References to other good quality services / organisations (8, 21, 22)Emphasis on shopping around (21) Respect boundary with other services and retain impartiality (7, 9)
Clarity of the guidance, and consistent delivery of quality.	Consistent delivery of a free service across delivery channels and providers (1, 2, 3 and 19) Clear and fair information communication (13) Delivery of a good quality service with care and diligence (5, 6, 10, 22)
User experience and service take-up	Timely provision of the service (4) Appropriate complaints management (16 and 17) and appropriate systems and controls (14 and 15) Record of the guidance session for effective follow-up by customer (23, 24)

4.10 The FCA’s role in monitoring and ensuring DGPs’ compliance with these standards as a whole (and not just those with additional implications) will uphold the overall quality of the service and ensure that the service meets the objectives for which it was created. This will bring about incremental benefits if it increases the likelihood that the DGPs will comply with the standards compared to a situation with no standards or monitoring. There are a number of reasons why we consider this incremental benefit likely.

4.11 The DGPs’ accountability to the FCA is likely to increase their incentives to comply with the standards. As consumer-focused organisations, the DGPs should already have strong incentives to comply and provide a good-quality service. However,

'unintentional' failure to comply may still occur (i.e. where necessary processes are not all in place to ensure compliance, even though at a high level the organisation wishes to be compliant). Being held accountable to the FCA as a formal oversight body is likely to focus the providers' efforts on compliance and may encourage them to examine their services with a greater degree of scrutiny than before.

- 4.12 The role of the FCA may also act as a deterrent to non-compliance. In the event of non-compliance, we will be able to make recommendations to the providers and to the Treasury.<sup>16</sup> This should deter non-compliance, although the FCA's enforcement powers in this context are not as extensive as those it has over other supervised firms.
- 4.13 We will be able to identify and address issues with the service before they become problems. This will be achieved through proactive monitoring and interaction with the providers (for example, gathering and analysing data on a continual basis, and annual assessments), combined with a clear idea of the desired outcomes of the service.<sup>17</sup> As an external body, we will have an advantage over individual providers in identifying issues that might affect the service as a whole.
- 4.14 The ability of the FCA to undertake event-driven research, and its in-house expertise, will also enable it to identify potential issues that may necessitate amendments to the service or to the monitoring approach over time. Inevitably the Pension Wise service will develop from its initial start. We will be able to set targets to address areas where we have concerns and monitor DGPs to ensure these are not neglected.
- 4.15 The oversight role of the FCA will increase in importance in the future if more providers are included in the delivery of the service that have not been involved in the initial set-up. Having an external set of standards may also help providers to hold contractors to account and ensure consistent levels of quality across all involved in the delivery of the service.
- 4.16 The above assessment indicates that having the FCA set, and monitor compliance with, the standards will improve the extent to which DGPs maintain a good quality guidance service. The incremental benefit of our role is, however, likely to be moderate if as we expect they would've complied with most of the standards in any event. Table 3 below summarises our assessment of the extent to which our monitoring role is likely to increase DGPs' compliance with the standards over and above what would have occurred anyway.

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<sup>16</sup> There is extensive literature about the deterrence effect of regulation, although usually applied in stronger contexts than this.

<sup>17</sup> The FCA's monitoring role is also enhanced by the specific standards around compliance and record-keeping.

**Table 3: Summary of the incremental impact of the FCA’s role on DGPs’ compliance**

Feature of FCA role	Likely incremental impact on compliance
Proactive monitoring against standards and identification of problems	Medium
Increased accountability to an external oversight body	Medium-low
Deterrence effect	Low

### Assessment of increased quality of guidance service

4.17 We combine our assessments of the additional elements of the standards and the FCA’s overall compliance monitoring role judge the extent to which these are likely to improve the overall quality of the guidance service compared to a situation without FCA standards. Table 4 presents this assessment.

**Table 4: Incremental improvement in the quality of the guidance service arising from the FCA’s standards**

Areas necessary for a good quality service	Added value from:		Incremental improvements in quality of the service
	Specific standards	Monitoring	
Professional skill of guiders	✓✓	✓✓	Medium
Sufficient information about options in the content of the guidance session	✓✓	✓✓	Medium
Clarity of the guidance and consistent delivery across providers and channels	✓✓	✓	Medium-low
User experience and service take-up	✓	✓✓	Medium-low
Establishing appropriate links to wider markets	✓	✓	Low

Note: For *Specific Standards* score: ✓✓ = additional impact from Table 1 is ‘medium’ or above; ✓ = additional impact is less than medium. For *Monitoring* score, ✓✓ = particular risk identified in market failure analysis addressed by monitoring; ✓ = general monitoring benefits.

### Summary of benefits

4.18 This analysis has identified a number of potential market failures that may undermine the quality of the guidance service provided by the DGPs. These include:

- the inability of consumers to judge the quality of the guidance they receive and discipline providers for poor quality
- the historical operational scope of the DGPs and the risk that they may lack the full skills and expertise required to provide the service, and
- the knock-on effects that any failures by one provider will have on the quality and reputation of the service as a whole, given the interconnectedness of the providers.

- 4.19 The FCA's standards address key areas of the guidance service where poor quality is most likely to lead to negative consumer outcomes. These are summarised in Table 4 above and include, for example, ensuring there is sufficient information in the content of the guidance sessions, and that guiders have the necessary professional skills to apply various options to consumers' individual circumstances.
- 4.20 Our discussions with DGPs and the Treasury, and our own assessment, have identified elements of the standards that are likely to be additional to what the DGPs would have implemented otherwise. These, combined with our monitoring role to facilitate compliance with all the standards, are likely to lead to an increase in the quality of the guidance service compared to a situation with no standards. The overall improvement in quality will most likely be moderate.
- 4.21 Improvements in quality are likely to lead to some improvement in consumers' ability to make good decisions when accessing their pension pots. We therefore expect some material benefits from our standards in the form of improvements in overall consumer outcomes. As set out previously, it is not reasonably practicable to quantify this benefit.

# 5 Compliance costs to firms

- 5.1 Designated guidance providers (DGPs) will incur costs in implementing specific elements of the standards that they would not otherwise have done, and in complying with the FCA's monitoring and reporting requirements more generally. Our cost model is based on discussions with providers and benchmarking against similar regulatory changes.
- 5.2 The incremental costs of the standards are related to the additional elements of the standards as set out in Table 1 in the benefits section. However, not all additional elements imply incremental compliance costs. As the standards have been developed at the implementation stage of the guidance service, DGPs may have been able to adjust their plans to incorporate some of the standards in a cost-neutral way, i.e. by replacing one set of planned actions with another. The key additional elements of the standards for the DGPs that have cost implications are:
- greater levels of cooperation and coordination between the different providers, driven by Standards 2 and 3
  - more focused processes and systems to ensure compliance with the standards, driven by Standard 14. Providers already have in place quality assurance processes, which would need to be aligned to these purposes
  - longer periods for record-keeping than originally envisaged, and tailoring of reporting systems to enable FCA monitoring, driven by Standard 15.
- 5.3 In addition, DGPs will incur costs related to the FCA's compliance monitoring role, such as setting up systems to enable appropriate data gathering for the purposes of self-assessments, and more focused compliance functions.
- 5.4 The associated incremental one-off costs for DGPs include:
- time spent on coordination and cooperation with other providers
  - time spent on familiarisation with the standards and developing policies and protocols to ensure appropriate oversight of compliance within each organisation
  - time to align quality assurance processes and record-keeping/reporting to ensure compliance with standards
  - staff training on compliance with the standards (e.g. on policies and protocols)
  - IT costs of keeping records for longer time periods than envisaged. This largely affects TPAS as storing telephone records requires significantly more server space than documents
  - tailoring complaints systems to enable record-keeping and reporting to FCA.
- 5.5 The ongoing costs related to these elements are significantly less material than the one-off costs. As the providers currently undertake (or were planning to) most of the requirements implied by the standards, the greatest additional effort will be involved in tailoring these processes to have a greater focus on compliance with the standards. Ongoing costs will largely be aligned with business as usual costs. The ongoing costs will consist of:
- ongoing compliance and senior management time to ensure appropriate cooperation and coordination with other providers
  - standards-specific training elements for new staff (assuming an indicative 10% churn per year)
  - gathering data and reporting as part of the monitoring process.

- general compliance oversight and interactions with the FCA as part of the monitoring process.

5.6 The tables below summarise the one-off and ongoing compliance costs across all four providers (TPAS and the three Citizens Advice organisations). We note that some of the costs, such as guider training, also cover the individual Citizens Advice membership bureaux. We present the costs across three main areas:

- ensuring coordination and consistency
- systems and controls, which includes IT for record-keeping. These costs are purely one-off in nature
- overall compliance function, which includes training across all providers and bureaux.

**Table 5: Estimated one-off compliance costs across providers**

	FTE low	FTE high	Cost low (£000s)	Cost high (£000s)
Coordination and consistency	1.8	2.8	112	189
Systems and controls	0.7	1.0	82	131
Overall compliance function	2.1	3.0	100	148
<b>Total</b>	<b>4.6</b>	<b>6.8</b>	<b>295</b>	<b>468</b>

**Table 6: Estimated ongoing compliance costs across providers per year**

	FTE low	FTE high	Cost low (£000s)	Cost high (£000s)
Coordination and consistency	0.5	0.9	30	51
Systems and controls	-	-	-	-
Overall compliance function	0.5	1.0	25	47
<b>Total</b>	<b>1.1</b>	<b>1.8</b>	<b>56</b>	<b>98</b>

## 6 Direct costs to the FCA

- 6.1 The FCA will incur costs of monitoring the DGPs' compliance with the standards. Our envisaged monitoring approach set out in PS14/17 forms the basis of our cost benefit analysis. The monitoring approach will combine a number of tools to establish appropriate baselines of compliance and assess DGPs' ongoing performance against these baselines. These tools include:
- collecting and analysing monitoring data provided by DGPs on a regular basis
  - developing and carrying out an ongoing self-assessment process with DGPs
  - visits/assessments of DGPs
  - consumer research (e.g. mystery shopping, user experience)
  - detailed reviews of specific issues (similar to the thematic supervision approach)
  - developing action plans and recommendations where necessary.
- 6.2 The FCA will incur one-off costs in the first year of the guidance service of setting up these tools and establishing the relevant baselines. Ongoing costs will be incurred through the regular activities associated with the tools and more general activities such as internal reporting and governance and day-to-day interactions with the providers.
- 6.3 The costs will stem from FCA staff resources, based on a blend of junior and management time. We estimate that a team of between 3 and 4.5 full time equivalent (FTE) staff will be required in the first year, with an ongoing requirement of between 2 and 3 FTEs per year. We have also made an indicative allocation for external consumer research, but note that this allocation will depend on the extent to which DGPs conduct consumer research themselves and our final overall monitoring approach.
- 6.4 The ranges of one-off and ongoing cost estimates are presented in Table 7 below.

**Table 7: One-off and ongoing monitoring costs to the FCA**

Cost area	One-off (£000s)		Ongoing (£000s p.a.)	
	Low	High	Low	High
FCA staff costs	275	412	183	275
Research budget	100	150	80	120
<b>Total</b>	<b>375</b>	<b>562</b>	<b>263</b>	<b>395</b>

# 7 Summary of costs and benefits

- 7.1 The FCA's standards for designated guidance providers introduce some requirements for implementing and delivering the guidance service that the providers would not have undertaken otherwise. The FCA's role in monitoring compliance with the standards will also result in some behaviour changes on the part of DGPs.
- 7.2 However, the extent to which the requirements of the standards and the FCA's monitoring role are incremental to what DGPs would have done anyway is limited, given the nature of the providers and the services they currently provide, and their perceptions of what is necessary for a good quality guidance service.
- 7.3 We therefore expect moderate incremental costs and benefits from the standards. One-off and ongoing costs to providers are estimated at around £300,000 to £470,000 and £60,000 to £100,000 respectively; and one-off and ongoing costs to the FCA at around £380,000 to £560,000 and £260,000 and £400,000 respectively. While it is not reasonably practicable to quantify the benefits of the standards, they are likely to materially increase the quality of the guidance service and lead to improved consumer outcomes through better decision-making.

## Compatibility Statement

This annex explains our reasons for concluding that the standards we have set for designated guidance providers are compatible with certain requirements under FSMA.

The Pension Schemes Act 2015 modifies section 138I (2)(d) of the Financial Services and Markets Act 2000 so that the FCA must, upon the making of the Standards under our new statutory powers, publish an explanation of our reasons for believing that setting the standards will secure an appropriate degree of protection for recipients of pensions guidance from designated guidance providers. The following is our statement of compatibility with this consumer protection aim.

The standards for delivery providers were proposed in anticipation of new duties and powers that have been given to us through the Pension Schemes Act 2015 to set and monitor standards on the delivery partners involved in the Guidance Service.

The standards aim to:

- ensure that the guidance is impartial, consistent, of good quality and engaging across the range of delivery channels.
- create consumer trust and confidence in the delivery partners and content of the guidance so that consumers actively use the service.
- ensure that the framework works for both contract-based and trust-based pension schemes.
- deliver helpful guidance for consumers that considers their retirement

The standards we have made set the framework within which the pensions guidance service must be delivered. The Treasury and the designated guidance providers will work together on the operational detail of the pensions guidance service and the designated guidance providers must deliver this in accordance with the standards.

We are satisfied that this approach provides an appropriate degree of protection for those receiving pensions guidance from designated guidance providers.