Consultation Response

Pension reforms – proposed changes to our rules and guidance, CP 15-30

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About this consultation

Following the introduction of the pension flexibilities in April 2015, where consumers no longer have to annuitise their pension savings and can instead choose from a range of options, the decumulation product marketplace has seen a considerable amount of change. This consultation by the Financial Conduct Authority (FCA) is looking at how to appropriately amend the rules and guidance that providers must follow.

Key points and recommendations

- We are concerned that people with pension pots below £10,000 may no longer receive the full retirement risk warnings. Many people with savings at this level will depend upon their pension savings, and they could still face increased tax liabilities or reduced means-tested benefit payments if they do not use their savings appropriately. It could also leave lower net worth individuals vulnerable to being scammed or making inappropriate investments. The FCA should continue to protect all consumers with the full retirement risk warnings. If it does allow a less intensive regime for small pots, we think a threshold of £10,000 is too high.
- As decumulation product decisions are no longer a one-off, the FCA needs to ensure that people receive information and risk warnings at the appropriate points and at the appropriate frequency. Age UK is concerned that for customers making withdrawals, either through drawdown or uncrystallised pension lump sums, receiving a statement once every 12 months may not be frequent enough.
- The FCA should work towards introducing cancellation rights in all cases without exception, and in the meantime require all firms to issue risk warnings in instances where cancellation rights do not apply.
- The at-retirement product marketplace is more complex than ever, and is likely to become even more so. It will require constant monitoring and probing to make sure consumers are getting a fair deal, as well as timely action to resolve arising issues.
- Most savers are invested in the default fund, and many could be described as ‘disengaged’. As such, the FCA needs to think carefully about how to work with firms to ensure appropriate ‘lifestyling’ decisions are taken.
- We strongly support the FCA’s proposal to ensure that debtors are protected from being pressured into using their pension savings inappropriately to repay debt.
- We agree that there is a potential issue with non-advised annuity sales. The FCA should examine this specific marketplace in more detail.

1. Introduction

The introduction in April 2015 of increased pension flexibilities has created a profound change in the decumulation product market, and one which is constantly evolving. As changes occur, Age UK believes it is vital that consumer protection is placed at the forefront of policy-making.

The regulatory rules that govern providers are an essential part of the protection landscape, and the FCA must continue to ensure that they fully serve all consumers, including those with lower value savings.

We have some concerns that people with small pots might be ‘ineligible’ for the full range of risk warnings and protections, even though for many smaller pot-holders their decision has every bit as much impact on their future lifestyle as for higher value pot-holders.

Over the coming years the FCA should keep the market under review with this in mind, and in the meantime ensure that the baseline protections are sufficient to meet customer needs.

2. Consultation questions

Question 1 – Do you agree with the proposal to add these application and purpose provisions in COBS 19.4?

Question 2 - Do you agree with our proposal to add guidance on communications about retirement options?

Question 3 - Do you agree with our proposed rule to prevent application forms being sent in wake-up packs and reminders?

We agree that these application and purpose provisions should be added to COBS 19.4. They are necessary for empowering consumers in the contemporary marketplace. However, the complexities introduced by the freedom and choice agenda – where many people will not just make a single one-off decision but may well be repeatedly interacting with the marketplace throughout their later life across a range of options – mean that shopping around is likely to become more difficult for a typical consumer.

‘Adequacy of information’ might be a more difficult issue to determine when the possible pathways for utilising pension funds have increased. This will be dependent on a customer’s intentions, and a generic statement to be applied at a firm level may not deliver the best outcome to many customers within a firm.

We agree that the ability to shop around – across all product options – should be made absolutely clear at all times, regardless of the communication method used by the provider; and that application forms should not be sent out with wake-up packs.

However, the provision in COBS 19.4.2: that the firm needs to provide an open market options statement with any communication “unless the firm has given the client such a statement in the last 12 months” should be reconsidered. Some customers who are making complex decisions, especially those who make ad-hoc cash withdrawals, and approach their provider on more than one occasion in a 12 month period might well benefit from receiving more than one statement. The FCA should consider revising this to a shorter period.

Question 4 - Do you agree with our proposal to restrict when firms can send illustrations?

Question 5 - Do you have any proposed alternatives?

Question 6 - In what ways would the alternative be more beneficial for firms and consumers?

We agree the FCA’s proposals to restrict illustrations are logical and Age UK supports them. We have nothing further to add at this point.

Question 7 - Do you agree with our proposal to require firms to make customers aware of key factors relevant to the product the customer is seeking information for?

Question 8 - Do you agree with the factors we propose these are likely to be in relation to this rule?

The key aspect of this is developing a link between a customer request for product information and independent advice or guidance. We believe that it will always be in the customer’s best interest to understand and consider the full range of options before making a decision, therefore any rule created aimed at raising awareness should also direct customers to either Pension Wise or, if appropriate, paid-for advice.

It is unclear from the consultation paper whether the list of suggested topics for drawdown customers (3.48) is in addition or exclusive to the three factors suggested for annuity customers (3.47). Drawdown customers would also benefit from a risk warning about protecting spouses and dependents in particular. A good model to follow in terms of the wording and portrayal of these alerts would be the retirement risk warning rules, as this new rule will address similar issues at an earlier point in the cycle – consistency would be beneficial for consumers.

Question 9 - Do you agree with our proposals for providing product disclosures and information when accessing pensions flexibly? If not, what alternatives would you suggest?

We agree that the FCA should not prescribe firms' precise wording or forms of communication, but the FCA will need to monitor communications carefully and should consider how it can act quickly to stop any poor practice.

There is also a risk that information could be presented in a way that frightens consumers into acting rashly and against their best interests. For example, if firms sent a poorly worded letter explaining that a customer's fund value had declined due to stock market falls (para 3.70), the customer may be tempted to cash in their remaining fund, even though this would not necessarily be in their best interest.

A similar approach should be applied when informing drawdown or UFPLS customers at what age their money is projected to run out (para 3.64). Here, an explanation of life expectancy would be important if consumers are to optimise the use of their fund. People often under-estimate how long they are likely to live for, and if told their pension/drawdown fund will run out at age 78, many people will consider this to be at or close to their life expectancy when in reality they might live for a much longer period.

Question 10 - Do you agree with our proposals for extending the rules and guidance in COBS 9 to UFPLS? If not, please explain why you consider this is not appropriate.

We strongly support proposals to extend the requirement on suitability reports and personal recommendations to UFPLS .

Question 11 - Do you agree with our proposal to clarify that SIPP retained interest charges should be included in projections and charges information? If not, how would you suggest we level the playing field for disclosing charges between SIPP and other pensions?

We support this proposal.

Question 12 - Do you agree with our proposal not to add guidance at this stage to support firms in meeting their obligations to review the operation and distribution of their products over time?

The at-retirement product marketplace is likely to continuously evolve. The FCA needs to take a highly proactive approach in monitoring and regulating this environment, and should plan to conduct regular reviews of the marketplace. We are pleased that FCA is reminding firms of the importance of good governance in product design, but would like to see further details of how this will be monitored.

The vast majority – over 80 per cent – of pension savers are invested in the default fund, and this is likely to increase up to 90 per cent by the mid-2020s.[i] While some default fund members do take an active decision to save in this fund, many people do not and could be classed as 'disengaged savers' – FCA should not rely on communication alone to help them reach better outcomes (para 4.13).

This is particularly true for savers in master trusts, of whom 91 per cent already save in the default fund. Master trusts need to be particularly aware of the importance of communications on investment issues.

Question 13 - Do you agree that the rules in PS 15/4 should be retained? If not, please explain what change you would propose and why?

Age UK agrees the Retirement Risk Warning rules should be maintained. They are an essential protection for the majority of consumers, and should be given as much prominence as practically possible. With fewer people than expected (or hoped) using Pension Wise,[ii] these rules are crucial for informing people about the potential pitfalls.

Question 14 - Do you agree with our proposal to remove the requirement on firms to go through step 2 of the risk warning process where the consumer's pension pot is

below a minimum level and where there are no safeguarded benefits but that firms should still give the consumer relevant risk warnings? If not, why not and what alternative would you propose?

Question 15 - Do you agree that the minimum level should be set at £10,000 or less? If not, what level do you think the minimum should be set at and why?

We do not agree with the proposals to remove step 2 of the risk warnings for people with pots below £10,000. This is an important – and in many cases the only – form of protection for consumers and is necessary for helping them make the right decisions.
For example removing these warnings could increase peoples' risk of falling victim to a scam. There appears to be no evidence provided to back up the statement that 'firm experience has been that the benefit to consumers from receiving risk warnings is lower for those consumers with smaller pension pots'. As the early evidence on how consumers are accessing their pension savings indicates that many smaller pot holders are taking cash, it is crucial that sufficient protection is in place for this scenario in particular.

Therefore we believe the most appropriate action is to retain the protection in its current form. If this is not the case, then an alternative process must be developed including clear and prominent warnings that must be given about the potential short and long-term issues that can arise from taking the pot as a lump sum, and especially highlighting the risk of scams. If compliance costs are a genuine concern for providers, the FCA could consider reverting to a more standardised risk warning approach for consumers with lower value savings.

We also believe that £10,000 is too high. Increasingly (and even more so in the future as automatic enrolment is expanded) consumers are likely to have a higher number of low level pots. By the point of retirement, people could have amassed a significant amount of savings spread thinly across several different providers, and not be eligible for any risk warnings. This could leave even 'average' level savers exposed to unnecessary risk. If there must be a threshold for differentiated treatment, it should be set at a much lower level, although Age UK is opposed in all circumstances.

Question 16 - Do you consider our cancellation rules expose some consumers to a risk that is not mitigated by any other measures? In what other ways might we reduce that risk and improve consumer outcomes?

As the consultation paper explains, the majority of consumers are covered by existing statutory or contractual cancellation rights. However, it seems that 14 per of drawdown and 50 per cent of UFPLS customers do not require a change of contract to access these options and so are not covered by the statutory mechanism, and while many of those who miss out on statutory protection may be covered by their contracts, this number is not known. This means a significant minority may have no protection. Rectifying this might require a change in law or the FCA regulations, but we believe would be worthwhile.

Also, with more people using the freedoms to cash in their pension saving, the FCA should act to ensure that firms who may not offer cancellation rights as specified in paragraph 5.9 for this option do so in future, or many people risk being exposed to irreversible decisions. Until a universal cancellation regime is in place the FCA should require an additional set of risk warnings issued where consumers may lack protection.

Question 17 - Do you agree that monitoring the evolving environment is an appropriate and proportionate FCA response in the pursuit of consumer protection? If not, what action do you think we should take and how would this alter consumer outcomes?

Monitoring the marketplace is clearly an important activity for the FCA. However on its own it does not necessarily improve consumer protection, so the FCA will need to consider how best to use its findings to implement appropriate measures to reduce consumer detriment, and in a timely manner. In addition a transparent approach where market updates are regularly published for scrutiny by organisations similar to ourselves, as well as the industry, is essential.

Question 22 - Do you agree with our proposal to add guidance to make explicit the application of existing rules on debt collection in relation to pension savings and remind both debt collection and advice firms that advising on conversion or transfer of pension benefits is a regulated activity?

Yes. This is an issue of some concern to Age UK and one that we raised in our eight point plan published in December 2014.[iii] While we have not seen evidence of creditors pressuring people into using their pension savings to repay debts when it may not be in the consumer's best interest, it is nonetheless a distinct possibility and one that may slip under the radar. The FCA should pursue this wholeheartedly.

A related issue is what regulation exists to prevent creditors who are not regulated by the FCA pressuring debtors to use their pensions. Clearly this is outside the scope of this consultation, and probably the FCA altogether, however there is a substantial reputational risk for the financial services industry if other creditors, for example local authorities, applied pressure in this direction. The FCA should consider what can be done to mitigate this risk.

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[i] Pensions Policy Institute Briefing Note (2015), Defined Contribution default funds and investment governance

[ii] http://www.ftadviser.com/2015/08/14/pensions/personal-pensions/pension-wise-take-up-only-around-of-clients-7C60vRa1xLounuQZI2sZlL/article.html

[iii] Available at: http://www.ageuk.org.uk/Documents/EN-GB/For-professionals/Policy/money-matters/getting_most_from_government_private_pension_reforms.pdf?dtrk=true