



Institute
and Faculty
of Actuaries

CP 15/7 Proposed changes to our pension transfer rules

IFoA response to the Financial Conduct Authority

15 April 2015

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.



Donald Cranswick
Strategy and Competition Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS

15 April 2015

Dear Mr Cranswick

IFoA response to CP15/7 Proposed changes to our pension transfer rules

The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the Financial Conduct Authority's (FCA) consultation paper on the pension transfer rules. The IFoA's Pensions Board has led the drafting of this response.

General comments

The IFoA is generally supportive of the proposals; however, there are a number of specific areas where we would welcome further clarification of, or amendments to, the proposed rules. The IFoA has commented previously that there are circumstances where pension transfers would be in the interest of the transferring members; however, it is important that individuals are fully aware of the consequences of taking transfers of safeguarded benefits.

The IFoA would also encourage the FCA to comment on the monitoring of transfers that may be undertaken following advice from a regulated adviser after the pension freedoms take effect. Such monitoring would enable a better understanding of how individuals may face specific risks. Therefore, we would welcome any analysis the FCA would develop in relation to:

- Transfers by advisor;
- Transfers in excess of those anticipated;
- Transfers by product type; and
- Transfers by receiving firm.

Q1: Do you agree that, in general, we should require that advice under the new specified activity be provided by, or checked by, a Pension Transfer Specialist?

1. The IFoA supports the proposal. We welcome the requirement that advice is required in all circumstances where safeguarded benefits are converted into flexible benefits. As noted in our general comments, the IFoA would support work undertaken to identify specific areas where transfers of safeguarded benefits are more prevalent
2. We would welcome clarity from the FCA/tPR that they will take a consistent approach and will issue clear communications about the specific responsibilities of all parties within the retirement income market, including advisers, firms, employers and trustees. In particular, we would encourage the FCA/tPR to recognise the possibility of member detriment where safeguarded benefits are converted to flexible benefits within the same trust.

Q2: Do you have any comments on the proposed new definition of pension transfer and subsequent requirements?

3. The new definition will allow the provision of advice in respect of transfers, or conversions, where individuals may not be fully aware of the risks they face by transferring their benefits.
4. However, it appears inconsistent to include transfers of benefit without safeguards from occupational money purchase schemes to contract-based money purchase arrangements, whilst excluding transfers between contract-based money purchase arrangements. From the IFOA's perspective, the similarities between these two types of transaction would suggest they should be treated in a similar manner from a regulatory perspective.
5. In addition this causes concern about how an occupational scheme wind up (or other bulk transfer) could be efficiently handled where a new contract-based DC arrangement has been put in place.

Q3: For future consideration, do you have views on whether or not we should continue to include transfers from occupational DC schemes without safeguards in our definition of pension transfer?

6. Please refer to our response to Q2.

Q4: Do you have any comments on the proposed new definition of pension conversion and subsequent requirements?

7. We understand, and support, the legislative requirement for advice to be provided on conversion of safeguarded benefits into flexible benefits or UFPLSs. Such pension conversions can involve the member foregoing extremely valuable benefits. However, the possibility remains that members could convert safeguarded benefits into another form of safeguarded benefits (e.g. the conversion of an increasing annuity into a level annuity), but such conversions would lie beyond the reach of current legislation.
8. On one level, there is no theoretical difference between:
 - a) An individual at the point of crystallisation giving up safeguarded benefits in favour of flexible benefits and/ or UFPLSs; and
 - b) An individual with money purchase or flexible benefits at the point of retirement electing to take an UFLPSs and/ or to use drawdown, rather than purchasing an annuity.
9. In considering current market values, there is a clear distinction between 8a and 8b. The cost of purchasing an annuity is much greater than the CETV in respect of safeguarded benefits. The conversion of safeguarded benefits does allow for individual members to have poorer outcomes than could otherwise be the case. There is a greater requirement for members considering 8a to receive advice on the conversion.
10. In both cases, the individual is giving up a known, guaranteed income for life and, in so doing, risks running out of money in retirement. Indeed, it can be argued that the guaranteed income is more valuable in (b) than in (a) since, generally speaking, the covenant of the annuity provider under (b) will be stronger than that of the corporate entity funding the safeguarded benefits under (a). In the future this would equally apply to members selling their annuity in any secondary market.

Q5: Do you agree that we should not require a Pension Transfer Specialist for advice on the conversion or transfer of benefits from pension policies with a GAR?

11. We understand the cost and capacity challenges with requiring a Pension Transfer Specialist to advise on the conversion or transfer of benefits from pension policies with a GAR. Nonetheless, in the current low-interest rate environment the GAR may be extremely valuable, possibly more so than a DB benefit. The IFoA considers that it is not clear that attaching a GAR to a money purchase benefit makes it a safeguarded benefit in accordance with the legislation. If the policy intent had been to include GARs as safeguarded benefits, we would encourage the required changes to legislation. Consequently any transaction involving a GAR would be subject to advice and analysis from a Pension Transfer Specialist.
12. In this context, we would note that transactions involving GARs could subject an individual to considerably more risk than transfers from other trust-based DC benefits without GARs to contract-based DC arrangements. If the FCA proposes the involvement of a Pension Transfer Specialist in the latter as important, we would urge it to reconsider the involvement of a Pensions Transfer Specialist in the former. The IFoA would support any efforts the FCA would make to include GARs within the definition of safeguarded benefits. This would address the issue of the advice requirement not applying to money purchase benefits with GARs, if legal advice supports the view that such benefits are not 'safeguarded'.

Q6: Do you have any comments on our proposed approach to permissions and grandfathering firms?

13. Given the requirement for DB trustees to confirm that appropriate advice has been received, easy access to the relevant data is important. Anything that allows a smooth transition post 5 April is welcome, provided controls are in place. The grandfathering seems a reasonable course of action to follow. We would encourage the FCA to ensure that a robust process is put in place to monitor those advisers who are able to qualify under the grandfathering system.
14. We would also encourage the FCA to ensure that the register that trustees will access is clear, easy to use and in plain English. We note the suggestion under 2.42 that trustees will be able to easily ascertain that there is no limitation 'excluding activity under Article 53E'. As this language will be new to many trustees, we would hope that the actual text in the register would be straightforward.

Q7: Do you agree with our proposal that all advice on DB to DC pension transfers – including any provided for the purpose of crystallising the benefits being transferred – must be carried out or checked by a Pension Transfer Specialist?

15. The argument set out in 3.9 is one the IFoA has highlighted previously and we strongly support the conclusion that advice is important. We also support the requirement for Pension Transfer Specialists to at least check all such advice and relevant circumstances around that advice.
16. However, we refer you to our response to Q4 on the potentially inconsistent treatment between members crystallising safeguarded benefits and those crystallising flexible benefits.

Q8: Do you have any comments on our cost benefit analysis?

17. As the consultation paper observes, it is very difficult to predict the number of individuals who will exercise (or consider exercising) the new flexibilities. Our members have been involved

in a material number of exercises over the past few years in which trustees or employers alerted members approaching retirement in DB arrangements to the option to transfer their benefits to a DC arrangement. Significant numbers of members have found this to be an attractive proposition, even after taking financial advice. There are various possible reasons for this.

- They value the higher amount of tax free cash generally available;
- They appreciate the opportunity to forgo pension indexation and/ or dependants' benefits in favour of a higher starting pension;
- They are in poor health; or
- They are concerned that the employer covenant is weak.

18. The results of these exercises suggest that the number of individuals who will exercise (or consider exercising) the new flexibilities may be rather higher than the cost benefit analysis assumes. Nonetheless, this is unlikely to change the overall conclusions of the analysis.

Should you wish to discuss any of the points raised in further detail please contact Philip Duggart, Technical Policy Manager (Philip.duggart@actuaries.org.uk / 0131 240 1319) in the first instance.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Nick Salter', written in a cursive style.

Nick Salter,
President, Institute and Faculty of Actuaries