Institute and Faculty of Actuaries

CP19/5 Retirement Outcomes Review: Investment pathways and other proposed changes to our rules and guidance

IFoA response to the Financial Conduct Authority

05 April 2019

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We strive to act in the public interest by speaking out on issues where actuaries have the expertise to provide analysis and insight on public policy issues. To fulfil the requirements of our Charter, the IFoA maintains a Public Affairs function, which represents the views of the profession to Government, policymakers, regulators and other stakeholders, in order to shape public policy.

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Financial Conduct Authority
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1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to this consultation. The FCA's Retirement Outcomes Review project has identified a number of potential pitfalls for savers in the complex defined contribution (DC) pensions landscape. Any initiatives that help savers to avoid these pitfalls and make informed decisions by better understanding their retirement options are welcome. The IFoA is generally supportive of the development of investment pathways; they are a step in the right direction in helping to facilitate better decision-making by DC savers. However, we continue to have some concerns about specific aspects of the consultation which we set out below.

General comments

2. In our response to CP18/17[1] we recommended that the overarching policy aim for investment pathways should be to help customers manage the number of risks they are asked to shoulder in the current DC environment, in particular investment and longevity risk. We are therefore pleased that the FCA has included an investment pathway linked with an annuity purchase which goes some way to addressing the potential mismanagement of longevity risk.

3. However this will not be sufficient to mitigate the risk entirely. Those entering drawdown still face a risk that they will run out of money in retirement. More must be done to highlight this. Below we suggest some additional wording to sit alongside Option 3 in the investment pathways, which might help bring this to the fore. Firms should ensure they make clear to customers entering drawdown that their savings could be adversely affected by the investment climate, and that they could run out of money if they withdraw money from their pot too quickly

4. In addition, investment pathways should form part of a broader strategy by the FCA and the government to help customers engage with and understand their financial situation. We are keen to understand in more detail how the investment pathways would be supplemented with other help and tools. This may become clearer as the role of the Single Financial Guidance Body (SFGB) is developed. We would hope for example that industry initiatives on simple,

[1] IFoA response to FCA CP 18/17 Retirement Outcomes Review: Proposed changes to our rules and guidance, questions 1-33 and 47-49, https://www.actuaries.org.uk/documents/ifoa-response-fca-cp-1817-retirement-outcomes-reviewproposed-changes-our-rules-and-guidance

plain-English communication are incorporated into the descriptions sitting alongside the investment pathways.

5. We are supportive of the proposed direction of travel, which builds on the use of nudge theory in other areas. Over time we would hope that providers are given flexibility to construct more customised pathways, by building on the initial requirements. This could them become an area where providers can add value and differentiate themselves in the market, more likely making use of innovations in robo-advice to allow high quality solutions to be constructed at low cost.

Answers to specific consultation questions:

Q1: Do you agree with our proposed rules on when a consumer must be offered investment pathways, including how consumers who enter drawdown in stages should be treated, and that those who take an UFPLS are not included?

6. We agree with the approach for consumers who enter drawdown in stages. We do not agree that those who take an UFPLS should be excluded, because most consumers are put into default investment strategies in the accumulation stage and these may not be appropriate for decumulation purposes. Furthermore, UFPLS is a potential alternative to drawdown for taking a pension income and so there is logic in treating them in a consistent manner.

Q2: Do you agree with our proposal that all providers of drawdown to non-advised consumers should be covered by our requirements on investment pathways, including SIPP operators?

7. Yes. Many consumers nowadays regard SIPPs as mainstream products in place of other types of personal pensions, and so this is an important segment of the non-advised market.

Q3: Do you agree with our proposed 4 objectives, and mandating all providers to use our prescribed wording when presenting these objectives?

8. Generally yes. We are pleased to see the FCA include an option for customers who might wish to purchase an annuity in the future. We remain concerned that those entering drawdown do not understand and are not sufficiently protected against longevity risk and this is likely to become a growing concern over time as retirees become more reliant on DC pots to fund their retirement. Therefore a prompt to think about this could be extremely helpful. As the FCA has acknowledged in the consultation, the proportion of customers with larger DC pots for whom it may be advisable to consider some form of annuitisation at some stage in their retirement, is growing. We expect to see this become increasingly important in the future. Our 2018 research in this area demonstrated the potential for customers to benefit from this type of arrangement, allowing them to balance flexible access with a guaranteed income and protection against longevity risk[2].

9. The consultation states that customers were more likely to make an appropriate choice when provided with additional text, and we feel this extra information is particularly important for

[2] Institute and Faculty of Actuaries Policy Briefing, *Can we help consumers avoid running out of money in retirement?*, April 2018, https://www.actuaries.org.uk/news-and-insights/public-affairs-and-policy/ageing-population/defined-contribution-pensions

Option 3, where customers are beginning to draw down on their pot. Whilst we feel the additional text offers welcome additional clarity, we do not think the concept of the money not being a 'guarantee' is sufficient in explaining the risk that the customer may exhaust their savings too quickly. Specifying 'There is a risk that I will run out of money if I withdraw it too quickly', would help to remedy this. We would like to see firms asked to make this risk clear to customers when entering drawdown.

Q8: Do you agree with our proposed rules requiring larger providers to provide pathways solutions for at least 2 of the 4 objectives and to refer consumers to another provider's pathways solutions for any objectives where they don't provide a pathways solution?

10. We agree with this in principle. It is important that customers receive appropriate signposting and are encouraged to shop around for the most appropriate product for their needs. This is, after all one of the key pillars of the freedom and choice agenda. Small firms could obviously only refer customers to a larger, FCA authorised firm with suitable commercial due diligence, and it is not yet clear how this would work in practice. We are encouraged by the SFGB's announcements on its drawdown comparator which should act as a useful tool for customers. We recommend that the design of the comparator tool include strong controls on what products can be included from providers, including those submitted being 'primary' products on sale which are available to clients without any material restrictions and offering all appropriate features.

11. In order to remove any undue complexity and potential friction to the customer journey, the process should be designed in a way that is as smooth as possible for the consumer. Incorporating the drawdown comparator tool within the SFGB's version of the pensions dashboard could be a way to do this, and we would hope that the FCA is considering future changes such as this when designing the rules applicable today.

Q11: Do you agree with our proposed approach for ongoing information to consumers using investment pathways? Do we go far enough, or is there anything further that providers could do to ensure that consumers carefully consider their investment choice on a periodic basis?

12. Timely reminders to consumers could be vital to ensure they review their circumstances. We are concerned though that statements, especially if in a prescribed format, may not receive due attention. It will be important to ensure that the key messages are conveyed in a prominent and engaging manner and market research might be helpful to establish what works best in this regard.

13. We recommend that the FCA engage with industry to create common protocols to communicate key information to consumers, not only around things like the value of their investments, but also the purpose for which they were taken out. From this data standards for communicating this might develop to enable interoperability of providers with the evolving technology e.g. consumer portals, dashboards and aggregators'. This will help the industry move towards a more consumer-outcome data driven framework (from the current technical, valuation driven framework which is less engaging and intuitive for clients).

Should you wish to discuss any of the points raised in further detail please contact Catherine Burtle, Senior Policy Analyst (catherine.burtle@actuaries.org.uk / 0207 632 1471) in the first instance.