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Sixty second summary

FCA proposals on pension transfer advice & contingent charging

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18 months on from their last consultation, the FCA remains highly concerned that the practice of contingent charging, where advisers only get paid if the transfer takes place, creates a conflict of interest that might incentivise poor advice. Under pressure from the industry, including the Work and Pensions Committee, and clearly concerned about a mis-selling scandal brewing, the intent of this latest FCA consultation feels far stronger. We'd be highly surprised not to see a ban on contingent charging applying from early next year.

Backdrop to the proposals

The proposals have been triggered by an ongoing FCA review of the DB financial advice market. The review found an alarmingly high proportion (69%) of advice recommendations to transfer out. Against a backdrop of repeated warnings by the FCA that advisers should start from the position that a transfer is not suitable, these findings came as a huge surprise. Although the FCA isn't able to directly evidence that contingent charging is to blame for the huge volumes of assets leaving DB pensions, there is no evidence to suggest it hasn't contributed.

Given the potential mis-selling scandal brewing, the FCA is putting consumer outcomes at the heart of these proposals. There will be knock on impacts on the costs and availability of advice, however, the FCA seem happy to live with these consequences.

What is the FCA proposing?

The proposals would mean that advisers would need a single pounds and pence upfront charging structure for advice, regardless of the advice recommendation. There are however limited exemptions where contingent charging could still apply. This includes where it can be evidenced that a member is in serious ill-health or financial hardship, for whom a transfer is more likely to be in their best interests.

Although the ban on contingent charging has rightly grabbed the headlines, the FCA is making several other proposals as part of this consultation:

- To address the conflict of interest that can arise when advisers recommend transfers resulting in high ongoing charges, advisers will need to demonstrate why the recommended scheme is more suitable than a workplace scheme.
- To introduce '*abridged advice'* as a new approach to filter out consumers for whom a pension transfer would be unsuitable, at a low-cost alternative to full advice. Abridged advice can only result in a recommendation not to transfer.
- To improve charge disclosure at the start and end of the advice process, with guidance on how advisers should check consumers' understanding of the risks of proceeding with a transfer.

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Our views on the proposals

Many of the broader proposals feel like good common sense and something that good advisers should already be doing.

Abridged advice

Abridged advice is designed to make advice less costly where it is highly unlikely to be in a member's interests to transfer. Abridged advice will require advisers to filter out members who are highly unlikely to benefit from a transfer value. To deliver abridged advice properly and to protect against future claims risk, advisers will need to undertake elements of the full advice process and demonstrate robustness of process. We therefore expect to see technology playing a greater role in delivering abridged advice well at a price point the market would be willing to pay.

If it can be delivered cost effectively, abridged advice can have a valuable role to play in preventing DB members sleepwalking into retirement in the DB scheme. However, members may struggle somewhat with the concept of abridged advice – i.e. paying to go through what is ultimately an advice process only to be told that they can't transfer. Advisers will therefore have a key role to play in ensuring members understand the purpose and value of abridged advice.

A ban on contingent charging

Given the levels of transfers from DB schemes since the introduction of the Freedom & Choice reforms in 2015, we welcome the ban on contingent charging to support improved overall confidence in the market and importantly in member outcomes.

However, the proposed ban on contingent charging is expected to reduce the number of advisers in this market and hence the availability of quality advice. This will compound wider supply issues, including the recent withdrawal of a major provider of DB financial advice, and other firms leaving the market having been unable to secure affordable Professional Indemnity insurance. This clear gap in the market could however present a material opportunity for advisers – those who can adapt quickly whilst demonstrating quality of process should be in high demand.

Payment of a material upfront advice cost could mean that those most in need of advice (and who don't meet the limited circumstances where contingent charging can still apply) can't afford it. The threshold for which transfer advice must be taken is currently £30,000. In current market conditions, small pensions exceed this limit. To help those most in need who are likely to have smaller pension amounts, we'd be keen to see debate around increasing this limit in conjunction with lighter touch advice (delivered at lower cost) to apply to more modest pension amounts.

A ban on contingent charging won't remove conflicts for advisers completely – advisers will still receive ongoing revenues for those who transfer. Greater transparency around both the costs and value of ongoing advice will be key.

The role of trustees and sponsors

We continue to advocate pension scheme trustees and sponsors doing more to help their members with one of the key financial decisions they'll ever take. Through sustained education and engagement with members, trustees have a valuable role to play in ensuring members are adequately equipped to fully explore their choices. We also expect to see a further increase in trustees and sponsors facilitating access to quality financial advice for their members. This approach already offers members access to quality advice at a transparent and competitive cost and is key to protecting member outcomes.