

# Delivering the RDR: Corporate pensions

Retail Distribution Review 14

February 2010

## Introduction

The Financial Services Authority (FSA) published its RDR consultation paper 09/31, *Delivering the RDR*, on 16 December 2009. This contains proposals for enhancing professionalism, applying RDR to corporate pensions and initial thoughts on applying elements of the RDR to advice on pure protection products.

We've been following the emerging position on corporate pensions very closely and, while we welcome most of the FSA's proposals, we're very concerned that the proposed factoring ban will lead to real consumer detriment.

The FSA will publish its main RDR policy statement containing final rules in the spring. For the corporate pensions market, we expect a policy statement and final rules in the third quarter of 2010.

Here, we give our views on the FSA's detailed proposals for the corporate pensions market, which covers group personal pensions, group stakeholder pensions and group self-invested personal pensions (all referred to here as GPPs). We also consider the proposed extension to occupational defined contribution schemes.

## The main points

The FSA proposals include:

- a ban on commission for GPP products and sales, for both advised and non-advised services
  - the ban on commission is tentatively extended to all group stakeholder pensions, whether sold through 'basic advice' to employees or by other means
- allowing 'consultancy charging' (the new name for 'arranger charging') from GPP contributions and/or members' accounts, as agreed between employers and advisers
  - the consultancy charge can include a separate member advice charge when (and only when) members accept individual advice
- a proposal that the ban on provider factoring (already proposed for individual investments) should extend to consultancy charging under GPPs
- allowing commission to continue on existing GPPs set up before the ban on commission is implemented, including those for new members and increases in contributions for existing members
- requiring disclosure by advisers to employers of the total potential adviser remuneration
- extending the ban on commission to investment products linked to occupational pension schemes sold as alternatives to GPPs



## Ban on commission for new GPP schemes

The FSA is proposing to ban commission for new GPPs set up after 2012, in line with the corresponding ban for the individual retail investment market. Instead, consultancy charging will operate. The FSA argues the way this market operates isn't sustainable – highlighting unnecessary re-broking of schemes and the lack of transparency of commission, particularly at employer level.

The FSA also hopes that removing commission will address the problem of commission creating provider bias and may enable providers to enter or get back into the GPP market.

## Consultancy charging

The FSA has renamed 'arranger charging' as 'consultancy charging' and this will apply regardless of whether the end investor (the employee) receives advice.

Consultancy charging applies whenever a firm is giving advice, or providing services, to an employer in connection with a GPP scheme, a group stakeholder scheme or a group self-invested personal pension scheme. The FSA defines this as:

- giving advice or assistance to an employer on the operation of such a scheme
- taking, or helping the employer to take, the steps that must be taken to enable an employee to become a member of such a scheme, and
- giving advice to an employee, following an agreement between the employer and the adviser, about the benefits that are, or might be, available to the employee as an actual or potential member of such a scheme

This appears to extend the scope of FSA regulation around 'advice' to employers.

We agree there are benefits in applying consultancy charging to the corporate market. These include:

- greater transparency through separate product and advice services costs
- increased employer engagement with their pension scheme and the services provided to them in the running of their scheme
- improved persistency
- more emphasis on advisers providing ongoing advice to the schemes they set up


A number of issues arise in the way that consultancy charging may be allocated fairly to members of a GPP. For example, how it may be applied across members with different contribution levels and different potential lengths of service, and to members who join the scheme at the time it's set up and to those who join later. In addition, whether charges will be applied to employer contributions, member contributions, or both.

The FSA expects HM Revenue & Customs will regard reasonable consultancy charges as 'scheme administration member payments' and therefore not as unauthorised payments incurring tax charges. Here 'reasonable' means on a commercial basis relating only to the GPP scheme in question.

## Existing schemes

The FSA said there's no need to disturb any commission-based arrangements already in place for existing GPPs, as it's more concerned about the setting up of new schemes, including those re-brokered and switched to new providers.

We welcome the FSA's intentions to leave existing schemes to operate on a commission basis. This avoids having to operate two adviser charging methods – one for the existing membership, and a consultancy charging basis for increments and subsequent (post-RDR) joiners.



The FSA intends to monitor the market closely to mitigate the risk that commission-based GPPs will be recommended where the NEST scheme (National Employment Savings Trusts – formerly personal accounts) would be better.

## **Factoring ban**

The FSA wants to ban provider factoring not just for individual business, but also for corporate pensions, as it sees a danger this may become a basis for competition among scheme providers, rather than a market characterised by competition around product terms and quality of service. It has also dismissed factoring on a standard basis in line with an industry code on the basis this is likely to infringe competition law.

We're very disappointed that the FSA continues to intend to ban provider factoring and would reject its concerns. We don't agree that limited factoring, possibly with industry standard terms, conflicts with FSA aims, and believe any competition concerns can be addressed.

We believe it's especially important to allow provider factoring for the corporate pensions market, as it provides a solution to resolving two conflicting desires with least disruption to the market. One desire is from advisers, who'll want to be paid around the time they carry out the initial work. A factoring ban means charges to cover this also need to be deducted upfront, resulting in reduced or nil allocation in the early months, which will put many members off saving. The other is from the scheme member, who'll want to see their contribution allocation maximised.

Some employers will be willing to pay a fee, which resolves the above difficulties. But not all will be able or willing to pay an up-front fee. Equally, some advisers will be unable or unwilling to have the consultancy charge paid over time through deductions from members' funds. So there are huge risks to the market if the FSA sticks with the factoring ban. We continue to believe a limited form of factoring, which spreads up-front consultancy charging over the first five years of contributions, strikes the right balance.

Introducing measures which focus on removing possible bias doesn't benefit consumers if at the same time they discourage saving. The benefit of more people buying protection appears to have been taken into account in the proposal to retain commission for pure protection. We think similar arguments apply to allowing provider factoring in the corporate pensions market.


GPP schemes often include very low contributions, much lower than is typical in the individual market. The impact of a factoring ban will particularly affect these GPP members – possibly causing them to opt out of their pension scheme. The FSA has previously admitted that banning factoring is most likely to adversely affect modest and low regular savers. This is precisely the market GPPs serve. We will continue to lobby against this proposal.

## **Occupational pension schemes**

In last June's consultation paper, there was a suggestion that advisers wanting to avoid the new rules for the GPP market might recommend occupational defined contribution pension schemes instead. To counter this, the FSA is proposing to ban commission on investment products linked to such schemes (which could be used as alternatives to GPPs). While it doesn't intend to extend its regulatory scope at this stage, the FSA will revisit this if it sees any worrying developments in the occupational pension market.

## **Basic advice models**

In its June 2009 consultation paper on the individual retail investment market, the FSA proposed allowing commission on sales of stakeholder products made through the basic advice model. However, in the December paper the FSA says it will consider the potential for increased use of this method of distributing stakeholder pensions and that, for the time being, draft rules will prohibit the payment of



commission on group stakeholder pension schemes, including those sold through basic advice. It will revisit this by March 2010 (in line with the timing of the policy statement).

## Next steps

Responses to this consultation paper are requested by 16 March 2010 and we expect the FSA to publish a policy statement, containing final rules for consultancy charging, during the third quarter of 2010.

However, as this consultation is effectively building on the main proposals, we'll get further insight into the likely direction of travel when the FSA publishes its final rules for the individual retail market in March 2010.

The FSA intends for any rules for the corporate pensions market to take effect at the end of 2012, in line with the main RDR rules.

## What this means for you?

We have less than three years to go before all the RDR rules are implemented. The FSA's intentions regarding the corporate pensions market are now much clearer and this consultation period gives the industry its last chance to influence the FSA.

To prepare for the changes to the corporate pensions market, advisers should now be considering:

- how the ban on commission will affect their business model
- for adviser remuneration, what consultancy charging tariff to adopt for different forms of advice – providers will have no influence over adviser remuneration
- how a sustainable remuneration basis can be established for both initial and ongoing advice
- how the firm can best position consultancy charging with its clients
- how the proposed ban on provider factoring may affect the firm's ability to advise on smaller schemes and employers unwilling to pay a fee
- what the firm's strategy is alongside pensions reform, in particular the new employer responsibility and the NEST scheme

If you have any concerns with this consultation paper, you need to respond to the FSA by 16 March. You can find the full consultation paper at [www.fsa.gov.uk/pubs/cp/cp09\\_31.pdf](http://www.fsa.gov.uk/pubs/cp/cp09_31.pdf)

Our respected team of industry experts analyse new legislative and regulatory developments affecting financial services.

One of the ways the team regularly shares its thinking is through the industry lobbying blog on the AEGON UK website. To find out about the latest developments, go to [www.aegon.co.uk/how/industryblog.htm](http://www.aegon.co.uk/how/industryblog.htm)

This communication is directed at professional financial advisers. It shouldn't be distributed to, or relied upon by, private customers.