Financial Advice Market Review: Call for Input

RESPONSE FROM ICAS TO HM TREASURY AND THE FCA

18 December 2015
Introduction

The ICAS Pensions Committee welcomes the opportunity to respond to the joint call for input, from HM Treasury and the Financial Conduct Authority, to their Financial Advice Market Review (FAMR) (October 2015).

Our CA qualification is internationally recognised and respected. We are a professional body for over 20,000 members who work in the UK and in more than 100 countries around the world. Our members represent different sizes of accountancy practice, financial services, industry, the investment community and the public and charity sectors.

Our Charter requires ICAS committees to act primarily in the public interest and our responses to consultations are therefore intended to place the public interest first. Our Charter also requires us to represent our members' views and to protect their interests, but in the rare cases where these are at odds with the public interest, it is the public interest which must be paramount.

Our response to the review is focused on the market for independent financial advice on pension decumulation options: we also highlight that consumers may require advice on pensions taxation in circumstances where they do not require financial advice.

We believe the concurrent reviews of the provision of independent financial advice and public financial guidance are timely. We acknowledge that the reviews are broad in scope; however, with the pensions freedoms recently implemented, these reviews are particularly welcome.

Now that major reforms to our pensions system have been implemented, we believe it is an appropriate time for the government to consider setting up an independent pensions/retirement savings commission as a standing advisory body which seeks to achieve long-term stability for the UK pensions system and cross-party consensus. Long-term stability in pensions policy is relevant to the provision of independent financial advice and public financial guidance as it would help to build consumer confidence in these services.

We have not responded directly to the review questions but rather set out our detailed comments below.

Any enquiries should be addressed to Christine Scott, Assistant Director, Charities and Pensions, at cscott@icas.com.

Detailed comments on the review

The advice gap
While the majority of consumers are likely to seek public financial guidance about their pension options, rather than advice, the extension of pension freedoms from April 2015 has increased the likelihood that consumers will also seek independent financial advice. However, following the implementation of the Retail Distribution Review (RDR), there has been consolidation in the advice market, with the number of firms with the capacity to give advice on pensions expected to continue to reduce further.

We believe that the combination of increased demand and market consolidation has created an advice gap in respect of pension decumulation. The recent announcement that the tax restrictions on the sale of annuities belonging to individuals will be removed from 6 April 2017, will likely add to this gap.

We have the following suggestions which could help reduce the advice gap:

- Demand could be reduced by expanding the definition of guidance, and therefore the scope of public financial guidance, to a point which falls just short of recommending a particular decumulation product. This would involve publically supported guidance setting out the options available to the consumer in more detail along with the pros and cons of each option.

  In addition to creating a demand for guidance and advice, the pension freedoms create a need for consumer knowledge and also a better understanding of risk. Extending the definition of guidance would inevitably involve conversations with consumers about risk and probability.
The private sector is producing stochastic models and their use could be incorporated into guidance services. These models provide consumers with information at a point in time about the probability of achieving a particular outcome. The assumptions used in these models can change daily, therefore an understanding of risk is vital.

In our response to HMT on the provision of public financial guidance, we recommend extending the availability of the pension guidance guarantee to consumers at the start of their working life and mid-career. If the guidance could include information on probable outcomes; this could encourage further pension saving by confronting consumers at an early stage with how much they realistically need to save for retirement.

- Independent financial advice is perceived by consumers as being too expensive and therefore not providing value for money. If advice is not priced correctly then advisors will continue to leave the market. We therefore believe that the government needs to revisit the advice model created by the RDR. We recommend that consideration is given to permitting providers to give advice on their own products, rather than consumers having to receive a whole of market review. This model would require the regulation of price, the conduct of advisors as well as of the advice itself. While we fully appreciate that developing effective regulation around an advice model with these features would be challenging, such a model could encourage financial advisors into the market.

Retiring entirely on a defined contribution (DC) pension pot is not yet common but it will become increasingly so. Therefore, demand for both guidance and advice will grow and it is essential that the government has a long-term plan to ensure that this demand can be met.

With auto-enrolment, there are more pension savers than at any time in the past and ever growing master-trusts. However, master-trust providers may not have the appetite for providing continuity between pension accumulation and decumulation. This may be another area which will increase pressure on the provision of guidance and advice in the long-term. We support the concept of collective defined contribution and believe that if this model of pension provision could be taken forward, it would go some way to easing future demand for financial advice by providing continuity between pension accumulation and decumulation.

**Advice on pension taxation**

We have a concern that insufficient attention has been given by government to how consumers access advice on pensions taxation in tandem with accessing public financial guidance, prior to making a decision on how to approach pension decumulation. We understand that pension providers have to give their customers risk warnings but we are not convinced these will be sufficiently timely in a person’s decision-making process or well enough understood.

The tax implications of decisions about pension decumulation are taken into account by Independent Financial Advisors (IFAs) in the advice they give. However, the freedom and choice reforms mean that those accessing guidance only, may not fully recognise when they need to seek advice on the tax aspects of their decumulation decision. In our response to HM Treasury on public financial guidance we highlight the need for guidance services to sign-post consumers to the appropriate tax advice.

It may not be necessary to seek pensions tax advice along with independent financial advice and it is important that consumers understand this.

Tax advice is not a regulated activity and therefore can be delivered by unregulated advisors. Therefore, care will need to be taken if pension guidance services of the future sign-post consumers to tax advice. If sign-posting occurs, we recommend that consumers are directed to tax advisors who have signed up to the Professional Conduct in Relation to Tax guidance published in May 2015 by ICAS, the Association of Accounting Technicians, the Association of Chartered Certified Accountants, the Association of Taxation Technicians, the Chartered Institute of Tax, the Institute of Chartered Accountants in England and Wales and the Society of Trust and Estate Practitioners.
Advice on DB to DC transfers
At present there is a requirement for individuals to receive appropriate independent financial advice on DB to DC transfers, where safeguarded benefits have a cash equivalent transfer value of £30,000 or less, but this advice can be ignored. The responsibility of pension scheme trustees or LGPS board members is to check that the advice has been received before releasing funds from the pension scheme: however, the content of that advice is not made available to the trustees. We are not proposing a change in these arrangements but there is a risk that at some point in the future, perhaps having ignored the advice received, individuals may conclude that they have made the wrong decision and seek recompense. Consequently, we believe this is an area where regulatory arrangements surrounding advice must be sufficient to ensure that both the advice itself and accompanying risk warnings are of sufficiently high quality. Without advisor confidence in both the advice structure and regulatory arrangements, there will be an increased reluctance to provide advice and an upward pressure on the cost of advice reflecting the perceptions of risk held by advisors and their insurers.

In our response to the HM Treasury consultation on “Freedom and choice in pensions” (June 2014), we set out our reasons for supporting the flexibility of DB to DC transfers in respect of private sector DB schemes and the challenges for advisors operating in this space:

“This is a difficult issue given the potential for damage to private sector defined benefit schemes. However, we believe that it would be untenable to prohibit DB to DC transfers as doing so may be discriminatory and could be challenged from a human rights’ perspective. Therefore, we would support leaving the existing flexibilities in place.

There are circumstances where a DB to DC transfer is the most appropriate option for an individual, for example, for someone who is terminally ill and/or has no dependents. Therefore, making transfers subject to trustee approval could have consequences for the trustee body or the PPF. For example, if a transfer was refused by the trustees, what would happen if the scheme entered the PPF and the individual’s retirement income was reduced as a result? Would there be a potential liability arising in relation to any loss suffered and where would it lie?

The complex rules around transfers mean that it is already difficult for individuals to find an independent financial advisor who is willing to recommend that an offer is accepted on the basis that it is difficult to assess whether the cash transfer value represents a good offer.”

Use of technology
Greater use of technology, ‘robo’ advice, has the potential to make financial advice more accessible and may also fill part of the advice gap. Technology can be used to deliver information through different media and could sign-post the consumer to more tailored on-line resources or to face-to-face advice. As the consumer journeys through the technology, he or she would need to indicate after each section that they have understood the information received.

The interaction of the consumer with the technology will create a verifiable audit trail which the advisor can rely on to demonstrate what has been delivered to the consumer. This approach could reduce the risk of mis-selling, although we recognise a cultural shift towards greater personal responsibility for decisions taken would need to occur.

We are still in the early days of pensions freedom in the UK and as products develop there may be scope for technology to deliver market comparisons which consumers are sufficiently confident to rely on.

However, both technological change and cultural change will take time with perhaps cultural change taking longer. The existence of new pension freedoms could provide an impetus for cultural change but the complexity of pensions does not favour the individual consumer, especially as the quality of the outcome may not be assessed for a considerable period of time. In monitoring the impact of pension reform on levels of pension saving and pension outcomes, the government will need to consider at regular intervals whether public financial guidance and independent financial advice are meeting consumer needs. A failure to do so could ultimately undermine the pension reform agenda.
In conclusion

We have recommended that the definition of guidance is extended so that the scope of public financial guidance can be extended to address the advice gap. Also, we recognise that our views on the use of technology by advisors would involve their relationship with consumers beginning with guidance and ending in advice. This would likely mean that there is some unavoidable duplication of provision even in an environment where demand is high and resources are scarce. We see duplication as unavoidable as seamless provision between guidance and advice would in practical terms be difficult to implement and may not always be in the interests of the consumer.