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# Defined benefit transfers

*Defined benefit (DB) transfers remain topical and the Financial Conduct Authority (FCA) recently published its latest policy statement introducing new rules and guidance. Rory Percival provides an update on some of the key aspects of this year's policy developments.*

## Policy Statement PS18/6 (March)

PS18/6 introduced the appropriate pension transfer analysis (APTA) which includes the transfer value comparator (TVC) and additional guidance on assessing suitability.

### APTA/TVC

The APTA can best be described as a 'suitability pack' which encompasses all the analyses you undertake to assess the suitability of the transfer. The key point is that it is personalised to the client and hence is not an old-style TVA with the TVC added.

The mandatory part of the APTA is the TVC. This is a heavily prescribed bar chart comparison between the cash equivalent transfer value (CETV) and the fund required to buy a comparable annuity. The 'loss' shown on TVCs is proving to be 30 – 50% or more. This is likely to put some clients off. Also, it is likely to influence FOS decisions (I am less concerned about the FCA) and it will be looking at the file to see if the advantages outweigh these significant 'losses'. Consequently, you need to be really clear on file about the client's objectives – with adequate colour and detail – and also about the client's strength of feelings.

### Assessing suitability guidance

#### The client's intentions for accessing pension benefits

Suitability is all about meeting the client's objectives and hence understanding about the client's intentions for accessing pension benefits is fundamental. Files which record the client's objective of 'flexibility' without any colour and detail are simply inadequate. They do not clearly demonstrate that the transfer is in the client's best interests and hence do not meet FCA requirements.

#### The client's realistic retirement income needs

This is a key area and touches on the importance of what I refer to as 'core secure income'. Core secure income includes state pension, DB benefits, annuities, guaranteed third way products and, possibly, good quality rental income.

When establishing the client's realistic retirement income needs, I suggest establishing their fixed outgoings and discretionary spending plans. Although this may involve some discussion and assistance to the client with calculating this, it is essential to obtain this information for two key reasons: in order to meet the requirements of COBS 19 to consider how the income needs can be met and also to assess whether the recommendation meets the client's capacity for loss.

You then need to consider how this income is going to be met. Having adequate core secure income at least to cover the client's fixed outgoings – but preferably their discretionary spending as well – puts the client in a very secure financial position. They know that, whatever happens, they have enough money to live on.

My interpretation is that the FCA considers core secure income to be an important factor in suitability. If the DB scheme is needed to provide part of this core secure income, then this is significant factor to take into account when assessing the suitability of the transfer.

#### Considering alternative courses of action to meet the client's objectives

The FCA expects advisers to consider other ways of meeting the client's objectives and maintaining the DB scheme. In essence, the DB transfer should be the last resort to meet the client's objectives.  The file should demonstrate that alternative options have been considered – and considered genuinely – not just going through the motions and ticking the box.

## Policy Statement PS18/20 (October)

This second PS introduced some additional rules and guidance such as the requirement for a suitability report but I want to focus on two main areas – triage and attitude to transfer risk.

### Triage services

Many firms use a triage process where some clients, for whom the full advice process is not necessary or worthwhile, are filtered out. The FCA is concerned that sometimes this might be inappropriately straying into giving advice. The FCA is bringing in guidance to help clarify how triage services might work – by being an educational process – without straying into advice.

An FCA supervisor expressed this very well by saying 'triage is not the firm filtering the client out, but rather giving the client generic information so that he/she can filter themselves out'. The guidance suggests that the generic information can explain 'the features of pension schemes with flexible benefits and pension schemes with safeguarded benefits that make them more or less suitable for general groups of people'. This means the information can be more helpful than simply explaining how the respective pension arrangements work.

### Attitude to transfer risk

This is a new expression and is entirely separate from the client's attitude to (investment) risk (ATR). You should therefore treat it separately from your risk profiling process. The attitude to transfer risk is about the client's attitude towards the features of the DB scheme benefits and certainty of income versus the flexible benefits approach. The list of issues raised in this section of the Handbook (COBS 19.1.6G(4)(b)) should be turned into a series of questions to ask the client at the fact-finding stage. I suggest also summarising these in the suitability report (perhaps under the heading 'Security versus flexibility').

Overall, the policy changes are wide-ranging but sensible, but they do involve changes to your advice process.

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