

Briefing

# The defined benefit pension transfer process

RISK | PENSIONS | INVESTMENT | INSURANCE



The current market for members transferring their benefits from a defined benefit (DB) scheme to a defined contribution (DC) arrangement does not work particularly efficiently for many members. We believe that DB scheme sponsors and trustees should look to put in place a process to support members who want to investigate whether transferring is in their best interests.

## Transform your members' experience

We believe scheme sponsors and trustees can transform the DB transfer process in three areas. This will minimise the risks to the scheme of facilitating poor outcomes and give all members – whether transferring or not – a vastly improved experience.

Do nothing	Provide full support
<b>1. Finding good quality advice</b>	
Difficult to find an IFA – “unbiased.co.uk is not unbiased.”	Partner with a specialist IFA vetted by sponsor and trustees
Member will pay a large, contingent fee on the ‘high street’	Fixed fee, regardless of outcome
Higher risk of unsuitable advice and poor outcome	Robust advice process
<b>2. Educating members about their options</b>	
No personalised support or guidance	Access to engaging online tools that provide personalised modelling capabilities
Transfer value looks large out of context	Transfer value put into context of retirement objectives
Lack of awareness of the options available	Member makes informed decisions
<b>3. Minimising the administrative burden</b>	
Administration team dealing with ad-hoc IFA requests	IFA provided with all relevant information in advance
IFA will struggle to advise in 3-month guarantee window	Process that completes well within statutory and best practice timescales
All parties frustrated at difficulties of just ‘doing their job’	Streamlined advice process, including pre-populated online APTA analysis for IFAs

## Background

Since the pension freedoms were introduced in April 2015, The Pensions Regulator (TPR) estimates there have been more than 180,000<sup>1</sup> transfers from DB schemes. The vast majority of these will have been initiated by the members; we estimate that less than 15% of these transfers were as a result of sponsor or trustee-led transfer exercises where member advice was given by specialist IFA firms.

Virtually all members are required by law to take advice from an suitably qualified adviser with the relevant regulatory permissions in order to transfer. Members with benefits worth less than £30,000 are not required to take advice but, in practice, few retail DC providers are now prepared to accept an unadvised transfer meaning that many of these members also have to take advice.

### The IFA market

Members currently face some challenges in finding an IFA to advise them on a DB to DC transfer:

- As a result of increasing FCA focus and regulation on DB to DC transfers, there are reducing numbers of IFAs with the necessary FCA permissions to give this advice;
- IFA firms are finding it increasingly harder, and more expensive, to get professional indemnity (PI) cover for DB to DC advice; and
- The traditionally suggested route of using [www.unbiased.co.uk](http://www.unbiased.co.uk) to find an IFA has been criticised by the Rookes<sup>2</sup> review into the British Steel Pension Scheme (BSPS) member transfer problems.

There are around 10-15 IFA firms who specialise in pension transfer advice and who predominately advise members as part of a bulk transfer exercise or an ongoing business as usual transfer option. These firms have robust processes in place and are heavily monitored by the FCA.

## Member advice charges

One of the most contentious areas of the DB advice market is member charges. Once a member has engaged with their own IFA, the charges for the advice are commonly structured in the following ways:

- A contingent charging basis – which means the IFA is remunerated by a deduction from the transfer value, usually on a percentage basis and which can be as high as 4% but typically 1% to 2%.
- A hybrid basis whereby the member pays a charge for the advice and a contingent fee is deducted from the transfer value for implementation of the transfer (although in some cases with the advice fee also being rolled into the contingent fee)

### Advantages of contingent fees

- 👉 Enables members who do not have the cash resources to pay the IFA's advice fees to receive advice
- 👉 Prevents the DB advice market only being available to the wealthy
- 👉 Member is not under pressure to transfer in order to pay for the cost of advice

### Disadvantage of contingent fees

- 👎 Conflict of interest for advisers who are incentivised to recommend a transfer
- 👎 Cross-subsidies between members – effectively members who transfer subsidise the costs for those who take advice but do not transfer
- 👎 Higher charges for transferring members than in a non-contingent structure
- 👎 Not consistent with most other fee structures for professional services that members may use (conveyancing, tax returns etc)
- 👎 Lessens the member's appreciation of the value of advice not to transfer

## Charges under the spotlight

The FCA have contingent charging high on their agenda (and reviewed it in detail in late 2018<sup>3</sup>) but have not yet banned the practice. They have stated that it is difficult to establish a causal link between contingent charging and unsuitable transfer advice but acknowledge the potential is there. Further investigation by the FCA will take place in 2019. Ahead of this, Frank Field and the Work and Pensions Committee ran an inquiry into this topic in January 2019<sup>4</sup> after calling for the practice to be banned.

These charging structures contrast with the approach taken by the specialist pension transfer IFA firms who provide advice in bulk transfer exercises and ongoing business as usual cases. In these cases, an advice fee is charged on a fixed fee basis regardless of the advice given. In bulk exercises this must be paid for by the company but in business as usual cases, the company, members or trustees can pay the advice fees.

## Impact on members

For a member, the difference in fees paid can be large. Whilst charges for financial advice vary considerably across different IFAs, the example below sets out an example based on anecdotal evidence of the charges paid under a contingent model compared to our experience of what is typically paid under a 'bulk' arrangement made with a pension scheme or sponsor. Additionally, not only will the initial advice and implementation fee be much cheaper, the ongoing charges for those transferring to drawdown will be cheaper too.

	Contingent charging	Bulk advice model	Difference
Transfer value	£200,000	£200,000	
Advice fee	Nil	£900	
Implementation fee if transfer	£4,000 (2%)	Nil	
Total fee	£4,000	£900	£3,100
Ongoing drawdown charges	c. 1.5% - 2% a year	c. 0.75% to 1.5% a year	0.5% - 0.75% a year
(platform, fund management and ongoing advice)	£3,000 to £4,000 a year	£1,500 to £3,000 a year	£1,000 to £1,500 a year

## Helping members overcome these challenges

Scheme sponsors and / or trustees are increasingly appreciating the challenge that members who wish to investigate transferring face. It is a topic that is gathering increasing attention from the press<sup>5</sup>, the Work and Pensions Select Committee, the FCA and TPR.

TPR's 2018 annual funding statement<sup>6</sup> stated that "The combination of accurate and timely information from trustees to members and their advisers, and good advice from a regulated financial adviser, will help members to make informed decisions that suit their personal aims and circumstances".

Following that, and in response to the criticisms that the various government organisations with an interest in this area have not taken a co-ordinated approach, the FCA, TPR and TPAS released a 'joint protocol'<sup>7</sup> setting out how they will work together to "enable early intervention... to help pension schemes and trustees ensure that their members are adequately and fully informed when considering transferring their DB pensions".

## Providing support

We believe that schemes will increasingly be expected to provide more support for members considering transferring than has historically been the case. There are varying degrees of support that can be provided. At a minimum we see it as important that schemes help their members find good quality advice, normally from a specialist IFA firm.

Area of support	Minimum	Mid-level	Full
Partnering with a specialist firm, or panel of firms, of IFAs (having carried out suitable due diligence)	✓	✓	✓
Including IFA contact details in member transfer and retirement statements	✓	✓	✓
Implementation fees paid for by the company or trustees	✓	✓	✓
Members pay advice fees	✓	✓/x	x
Company or trustees pay advice fees	x	✓/x	✓
Streamlined online process to provide access to transfer quotation, education material, modelling tool and link to IFA contact details	x	✓/x	✓
Allow the IFA to access an online Appropriate Pension Transfer Analysis (APTA) tool pre-populated with the members' scheme data	x	✓/x	✓
Online process for the IFA to notify the scheme administrator of the member's decision for action accordingly	x	✓/x	✓

## How we can help companies and trustees facilitate transfers

We can help companies and trustees establish a support framework for members at a level that they feel comfortable with.



### IFA due diligence

We have carried out due diligence on the specialist IFA firms that advise members in bulk transfer exercises. We regularly refresh this information to capture updates and changes



### IFA market knowledge

We speak regularly with the specialist firms to keep up to date with their experiences and identify market trends. We monitor the market to identify new entrants and carry out due diligence on them



### Communications

Our specialist communication team can provide engaging member communications and transfer packs



### Online portal

Our BWebstream online portal allows members to request transfer quotes and can provide a link to our educational tool Me2



### Me2

Our Me2 tool enables members to look at the potential for reshaping their retirement income by comparing their scheme pension with flexible drawdown (and other options) if they transfer. Me2 allows members to input other pensions, streams of income and expenditure and assets and obligations in order to get the full picture



### APTA tool

We already provide several of the transfer specialist IFAs with the APTA modelling support they are required to obtain in order to advise the members. As part of a streamlined process we can provide the APTA tool to the IFA based on information from the administration system

## What is APTA and why do IFAs need to do one?

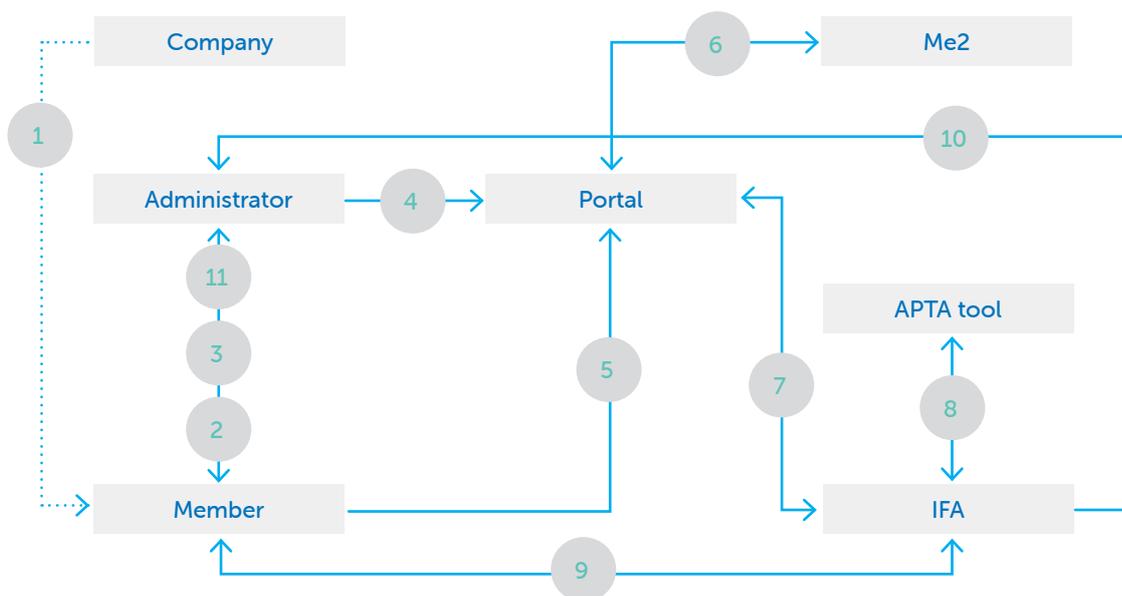
APTA is an "Appropriate Pension Transfer Analysis". It is an analysis that IFAs are required to carry out every time they advise an individual on a DB to DC transfer. The analysis must take into account a number of factors specific to the individual, such as the DB benefits they would get if they were to remain in the scheme. It also needs to include a Transfer Value Comparator (TVC) which places an actuarial value on the DB benefits being given up, assuming the individual were to replicate them by purchasing an annuity. This will virtually always be higher than the transfer value being offered.

Because of the complex, and often unique, nature of most DB schemes' benefits, and the actuarial nature of the TVC calculation, the bulk of the quantitative analysis in an APTA is outsourced to a small number of specialist firms, including Barnett Waddingham. Where there are delays in an advice process, it is typically due to the time taken for the APTA and TVC calculations to be done where this has not been streamlined in advance.

1. OPTIONAL: Company makes offer to member
2. Member requests early retirement or transfer value quote or receives the usual scheme benefits pack in advance of reaching normal retirement age
3. Administrator calculates figures and sends pack to member
4. Administrator sends locked data to Portal
5. Member accesses Portal and agrees to release data to Me2
6. Data unlocked on Me2 and member self-triages
7. Member contacts IFA for advice (and agrees to release unlocked data to APTA tool) via the portal
8. IFA uses APTA tool to advise member
9. Member receives personal recommendation, makes decision and notifies IFA
10. IFA informs the Administrator of member response
11. Normal administration processing of selected benefit option (do nothing, transfer or retire)

## An example of a full support process

The graphic below illustrates a full member support framework.



## Summary

We believe that scheme sponsors and trustees should put in place a support framework for members who wish to investigate their retirement options, including transferring out of their DB scheme. In the area of partnering with an IFA to provide members access to good quality advice, we firmly believe that the risk of doing nothing is greater than the risk of doing something. There are many steps that scheme sponsors and trustees can take to facilitate a better process for members.

Barnett Waddingham has the market knowledge, expertise and tools to enable a suitable framework to be designed and implemented.



1. [www.thepensionsregulator.gov.uk/en/about-us/freedom-of-information-\(foi\)/number-of-transfers-out-of-db-schemes-in-2017-18](http://www.thepensionsregulator.gov.uk/en/about-us/freedom-of-information-(foi)/number-of-transfers-out-of-db-schemes-in-2017-18) and [www.thepensionsregulator.gov.uk/en/about-us/freedom-of-information-\(foi\)/recently-released-information/number-of-people-who-transferred-out-of-their-db-schemes-last-year](http://www.thepensionsregulator.gov.uk/en/about-us/freedom-of-information-(foi)/recently-released-information/number-of-people-who-transferred-out-of-their-db-schemes-last-year)
2. [www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/rookes-review-british-steel-pension-scheme-members.ashx?la=en&hash=449D61E290965BB5B2F4DE15AA5171427F134E96](http://www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/rookes-review-british-steel-pension-scheme-members.ashx?la=en&hash=449D61E290965BB5B2F4DE15AA5171427F134E96)
3. [www.fca.org.uk/publication/policy/ps18-20.pdf](http://www.fca.org.uk/publication/policy/ps18-20.pdf)
4. [www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/inquiries/parliament-2017/inquiry13](http://www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/inquiries/parliament-2017/inquiry13)
5. [www.pensions-expert.com/Comment-Analysis/Trustees-must-go-the-extra-mile-for-their-members-on-transfers](http://www.pensions-expert.com/Comment-Analysis/Trustees-must-go-the-extra-mile-for-their-members-on-transfers)
6. [www.thepensionsregulator.gov.uk/en/document-library/statements](http://www.thepensionsregulator.gov.uk/en/document-library/statements)
7. [www.thepensionsregulator.gov.uk/en/media-hub/press-releases/regulatory-and-consumer-bodies-welcome-review-of-pension-scheme-communications-provided](http://www.thepensionsregulator.gov.uk/en/media-hub/press-releases/regulatory-and-consumer-bodies-welcome-review-of-pension-scheme-communications-provided)

Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail. Alternatively get in touch with one of our experts:

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