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**Consumer and Retail Policy**  
Financial Conduct Authority  
12 Endeavour Square  
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20 September 2022

Dear Consulting Team

**SPP response to FCA Consultation Paper: Calculating redress for non-compliant pension transfer advice**

We welcome the opportunity to respond to this consultation. We have focused our response on those questions that primarily impact on our members and consequently have not responded to those questions where we have no comment.

**Key Messages**

The key points that we wish to make are:

- Whilst reinstatement of affected consumers into their original scheme would be the ideal solution, we agree that in practice it is unlikely to be an option for most affected consumers.
- Treating redress as an augmentation in the receiving DC scheme is not necessarily straightforward either and there are several potential issues, mainly revolving around the tax treatment of the augmentation, that we suggest need further consideration.
- We do have concerns about the payment of a one off lump sum which is deemed to be 'sufficient' to put consumers back in the position they would have been in if they had not transferred out. The amount of money that is deemed to be sufficient will vary depending on the date on which it is calculated (especially in the current high inflation environment) and consumers are expected to invest it 'prudently', however there is no guidance as to 'prudent' investments might be and they may well vary depending on the age of the member.
- From our experience with pension scams, the consumers most likely affected by this issue will be less sophisticated investors, who may not have access to, or the resources for, independent financial advice.
- Finally, the levels of redress being paid in these cases will commonly be of such a level as to automatically cause net relevant earnings and/or annual allowance issues, i.e. unless

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redress can be paid without being subject to the current pensions legislation, in practice, many customers will receive lump sum payments. If the FCA really wants to ensure consumers get the right outcome, it must engage with His Majesty's Treasury and Revenue & Customs and repeal current pensions legislation in these circumstances.

## **Response to consultation questions**

**Q1: Do you agree that we should consolidate the pension transfer redress methodology as a new appendix in the Dispute Resolution: Complaints sourcebook covering pension transfer redress cases within the current scope of Finalised Guidance 17/9? If not, what alternative approach would you propose?**

If the FCA want the methodology to be applied and followed consistently, then our view is that it should be included in the Handbook.

**Q3: Do you agree with our proposal that firms should continue to calculate redress as the difference between the estimated value of the benefits given up in the defined benefit scheme and the current value of the consumer's defined contribution pension and pay that redress as a lump sum? If not, what alternative approach would you propose?**

We broadly agree with the proposal as it likely to be the only viable option for the majority of affected consumers in practice. However we do think that the redress should be paid to a registered pension scheme and not paid as a lump sum to the affected consumer directly, except in very limited circumstances.

**Q5: Do you agree with our proposal that all valuations of benefits must be undertaken on a same date basis, referred to as the 'valuation date'?**

Yes, we agree that the valuations should have the same date.

**Q6: Do you agree with our proposal that firms should issue calculations within three months of the valuation date? If not, what timeframe would you propose for issuing calculations to consumers and why?**

Yes, we agree that three months is a reasonable timeframe for firms to issue calculations to the affected consumers.

**Q7: Do you agree with our proposals for actuarial oversight of redress calculations? If not, what alternative approach would you propose?**

Yes, we consider this is essential.

**Q9: Do you agree with our proposed approach to requesting information from consumers, including what should happen if consumers do not respond to reasonable requests? If not, what alternative approach would you propose?**

Yes, we agree with the proposed approach.

**Q11: Do you agree with our proposed approach to keeping the methodology under review? If not, do you have any other suggestions for how we could ensure the methodology and individual assumptions remain appropriate?**

Yes, the methodology should be reviewed and we agree with the proposed approach.

**Q45: Do you agree that firms should pay as much of the redress as possible directly into the consumer's defined contribution pension by augmentation? Do you also agree that payment should only be by cash lump sum where augmentation is likely to mean consumers incur a tax charge or where the consumer specifically requests that redress is provided in this way? If not, how do you think redress should be provided to consumers and why?**

Paying redress as an augmentation and tax issues

We agree that redress should be paid directly into the consumers defined contribution pension arrangements and that should be the default option. The redress is intended to put the consumer in the position they would have been in if they had not transferred out of their defined benefit pension scheme. Consequently, the redress payment should be used to provide pension benefits rather than a cash lump sum.

However we think there are challenges with paying the redress as an augmentation and consider that there is further work to do to ensure this is a viable option to be used in the majority of cases. To simply say firms should augment as default completely ignores so many of the individual complexities associated with pension contributions. Firms would have to gather some really detailed information from the affected consumers and in doing so would have to get into complex areas of pension rules (annual allowance, tapered annual allowance, carry back/forward, lifetime allowance etc.) and risk breaching the advice boundary.

We also think that the receiving DC scheme should not be responsible for the costs it incurs in processing the augmentation this, unless there is a policy intention that the augmentation would potentially act as a further challenge to the DC schemes accepting transfers in?

As augmentation provisions will vary between DC schemes it is not clear if some overriding legislation would be needed to facilitate this or if each DC scheme would need to review its scheme documents and then consider if it can give effect to the policy of accepting such redress on the basis that it is an augmentation.

Has any thought been given to the circumstances where the consumer has transferred from the original DC scheme to another DC scheme – should the redress be paid to that scheme? What if the DC scheme is unwilling or unable to accept new transfer payments? Does that mean the consumer would have to establish another DC arrangement, possibly requiring financial advice, to receive the redress?

We consider that there are risks with paying redress directly to the consumers. It is unclear how firms will be able to judge that augmentation is likely to result in a consumer exceeding their annual or lifetime allowance or a contribution exceeding their available relevant earnings. It is possible that affected consumers may have unused annual allowance that could be carried forward, and thus no tax charge would then be payable (even though the amount of redress being paid might exceed the annual allowance in a particular year). How would firms judge when tax might become payable without obtaining all of the affected consumers' financial information? It is also unclear to what extent affected consumers will understand why this information is required and/or understand how to obtain the information or have it readily available.

With regard to tax, our view is that the consumer's tax position is key and any augmentation should not result in the member being liable for a substantial (or any) tax charge. If augmentation is the preferred default, then query whether the FCA has liaised with HMRC or other government bodies with a view to ensuring that redress is not treated as a tax relievable/taxable pension

contribution.

In the event that there is a tax charge, we note that where the tax charge is £2,000 or more, consumers should be able to use 'scheme pays' where the defined contribution pension scheme receiving the compensation payment would pay the tax charge on behalf of the consumer and the benefits (i.e. redress) would be reduced accordingly. Has this been considered as an option?

Even if it is possible to address the potential tax issues, then there is a significant work to be done on communications with consumers and who will bear the cost of this work? Would it be for the receiving scheme to engage with the consumer and gather data, issue information and tax warnings etc or would this be deducted from the redress payment as a cost which would then be borne by the consumer?

#### Redress as a lump sum to the consumer

We would not be in favour of consumers being able to specifically ask to receive the redress directly as a cash lump sum (except in circumstances where augmentation is not possible or practicable). This is because we consider that there are further risks to consumers in these circumstances. For example, we are aware, in the context of pension scams, of firms who 'offer' to seek redress for members who pension schemes who have (or may have bene) 'scammed'. These firms require the members to enter into formal agreements, the terms of which commonly require the member to pay the firm 20% or more of the compensation recovered from the transferring occupational pension scheme as a fee. We consider that these claims management firms would consider the redress scheme a potentially lucrative business opportunity. This is not in the interests of the affected consumers.

#### **Q46: Do you agree with the factors that are likely to be relevant in judging whether augmentation would result in a consumer exceeding their annual or lifetime allowance? If not, which factors do you think are likely to be relevant?**

We agree with the factors set out as being relevant when forming a judgment on whether the augmentation would result in a consumer exceeding their annual or lifetime allowance. We do query what hierarchy firms would be expected to apply when balancing the consumer's tax position and their entitlement to state benefits were the redress paid as a lump sum rather than an augmentation?

#### **Q.47 Do you agree with our proposal on how firms should allow for tax and means-tested state benefit entitlements on lump sum augmentation of redress payments? If not, what alternative approach would you propose?**

We agree with the proposal in principle but means-tested benefits are, again, a very complex area and put a burden on firms and their staff who should not be expected to be experts in that area.

#### **Q48: Do you agree with our proposal on how firms should allow for tax and means-tested state benefit entitlements on cash lump sum redress payments? If not, what alternative approach would you propose?**

We broadly agree with the proposal, but it is unclear how firms will know where the consumer may have a liability to CGT or income tax at the time they are calculating redress.

#### **Q49: Do you agree with our proposal that calculations should be valid for three months from date of issue to the consumer? If not, what alternative timeframe would you propose?**

We agree that three months is a reasonable period for the calculations to be valid.

**Q50: Do you agree that redress payments should be increased between the valuation date and the payment date using, as appropriate, the pre-retirement or post-retirement discount rate to compensate consumers for foregone investment returns? If not, what alternative approach would you propose?**

We agree that there should be some compensation for the loss of investment returns during that period, but we do not have a view on using the pre-or post-retirement discount rates to calculate that compensation. If the compensation is intended to be invested prudently, how do those rates compare with what might be the return on a 'prudent' investment for that particular consumer?.

**Q51: Do you agree with the proposed content of the calculation explanation? If not, what information do you think consumers should be given to help them understand their calculation?**

We note that firms may seek advice from HMRC under its non-statutory clearance process if they are concerned about any transactions giving rise to unauthorised payments. Our view is this is significantly over-simplifying the reality. Our experience is that obtaining HMRC clearance is not necessarily straightforward, there is a very specific process to be followed and it can take 4 to 6 months to receive a response (which may then require further clarification). This could mean that firms would be unable to meet the proposed timetable for paying redress. What would be the consequences for firms in this scenario where the rules governing redress are in the Handbook? Would there be an exemption?

**Q52: Do you agree with the proposed wording for the warning when consumers receive redress as a cash lump sum? If not, what wording do you suggest would be more impactful for consumers?**

We note that the warning is intended to be given where the redress is paid as a cash sum and that the consumers are advised to invest it 'prudently' because otherwise they risk losing out on retirement income. 'Prudently' will mean different things to different consumers.

If consumers have the option of selecting redress as a cash lump sum (or the firm decides that it is in their interests to receive redress as a cash lump sum), it is unclear the extent to which the consumer will use that redress to provide retirement income when it is not invested in a registered pension scheme. This is another reason why augmentation would be our preferred solution.

We would query to what extent consumers should be given information about each option (redress paid to the DC scheme as an augmentation or a cash lump sum). Our view is that the consumer should be given as much information as possible about each option to all so they can make a fully informed decision. We also consider that very strong warnings about the risks associated with the payment of redress as a cash lump sum is given before the consumer can select that option, not after.

Is there a role for PensionWise/ Money helper in supporting the consumer through this process if there is a default to the DC scheme to make sure the consumer has considered the key issues? Most consumers will know if they have some form of tax protection but might not consider that an augmentation would affect it unless prompted (and would then potentially blame the receiving DC scheme if the augmentation resulted in the loss of a valuable tax protection. We think this would also relieve some of the burden from the receiving DC scheme.

We think the warning could be stronger, and perhaps provide consumers with examples of life expectancy in retirement and average income requirements.

**Q53: Do you agree that consumers should be encouraged to read their explanations carefully and that firms should be required to and set out clearly the process the consumer should follow if they have any questions, wish to challenge any of the information used in the calculation, or make a complaint?**

Yes, we agree.

**Q54: Do you agree that, subject to the differences set out in Chapter 8, the same redress calculation methodology should be used for British Steel cases as all other cases? If not, what alternative approach would you propose?**

We do not have strong views on this, but we think it would be a sensible and proportionate approach.

**Q55: Do you agree with our proposal to follow our general approach on the method of payment of redress for BSPS consumers? If not, what alternative approach would you propose?**

This would seem to be a sensible approach.

**Q56: Do you agree that where the Pension Protection Fund is used as the comparator scheme, consumers should be redressed based on the upcoming Pension Insurance Corporation benefits when available? If not, what alternative approach would you propose?**

Yes, we agree that redress should be based on the PIC benefits if the PPF is the comparator scheme for the purposes of calculating redress.

**Q57: Do you agree that where consumers made an active selection of either the new British Steel Pension Scheme (BSPS2) or the Pension Protection Fund at the time of the transfer, the redress calculation should be based on the benefits of the selected scheme? If not, what alternative approach would you propose?**

We think it would be sensible to calculate redress by references to the scheme actively selected by these consumers.

**Q64: Do you agree with our proposals for adjusting the redress payment to take account of the consumer's tax position and accumulated interest between the valuation date and payment date? If not, what alternative approach would you propose?**

Yes, we agree with the proposals.

**Q68: Do you agree that the calculator should significantly reduce or eliminate the need for actuarial input? If not, why not?**

We agree that where firms have no ready access to actuarial resource the calculator should significantly reduce or eliminate the need for actuarial input.

**Q70: Do you agree that the use of the calculator should be mandatory? If not, why not?**

We agree that using the calculator should be mandatory as we consider that it ensures consistent treatment of consumers across all of the firms required to calculate redress.

**Q71: Is your firm interested in taking part in testing the redress calculator for the proposed British Steel redress scheme?**

Not applicable to SPP.

Yours faithfully

**Sharon Piert**

Interim Chair, Financial Services Regulation Committee, SPP

**Fred Emden**

Chief Executive, SPP

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