

Report to the FSA from the
Consultancy Charging Working Group
March 2011

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Good Practice Guide

Introduction

In June 2006 the Financial Services Authority (FSA) launched a detailed review – the Retail Distribution Review (RDR) - of the retail investment market designed to address what was seen as insufficient consumer trust and confidence in the operation of the market.

In June 2010, the FSA announced that it intended to ban the payment of commission on new corporate pension schemes from 31 December 2012. Instead, advisers would need to be remunerated by other means, including fees and/or consultancy charges.¹ Commission arrangements for schemes in existence at this date can continue.

As part of its consultation on this issue, the FSA sought suggestions about the fairest way of allocating consultancy charges among different members of corporate pension schemes allowing for factors such as different ages, different contribution levels, etc. The responses were wide and varied, and included suggestions that a working party be established to consider the issue, with a view to issuing a form of industry guidance. The FSA recognised that the corporate pensions market was distinct from other areas covered by the RDR and that it would therefore not be appropriate for the FSA to prescribe the detail of how consultancy charging should work. Accordingly, the FSA decided to establish an industry working group to take forward discussion about the allocation of consultancy charges among members of corporate pension schemes.

At the request of the FSA the Society of Pension Consultants (SPC) agreed to facilitate the work of this group and to provide its Chairman. Terms of Reference (Annex B) were agreed between the FSA and the SPC for a “Corporate Pensions Consultancy Charging Working Group”. The SPC then sought applications to join the Working Group from its membership (which is drawn from a range of parties across the pensions industry). Applications were also invited from other firms / organisations which had expressed an interest in the issue or which were thought likely to have an interest. All who applied to join the Working Group were able to do so. Eventual membership (Annex C) comprised trade bodies, pension providers, independent financial advisers (IFAs), employee benefit consultants, third party administrators and employer bodies. (Consumer bodies were invited to attend but declined to participate.)

¹ A ‘Consultancy Charge’ is defined in the FSA’s Handbook of rules and guidance as “*any charge payable by or on behalf of an employee to a firm or other intermediary (whether or not that intermediary is an employee benefit consultant) in respect of advice given, or services provided, by the firm or intermediary to the employer or employee in connection with a group personal pension scheme or group stakeholder pension scheme, where those charges have been agreed between the firm or intermediary and the employer in accordance with the rules on consultancy charging and remuneration (COBS 6.1C)*”.

The FSA provided the Secretariat of the Working Group as well as an observer at its meetings.

The Working Group was charged to complete its work by the end of February 2011, or as soon as possible thereafter. It held its first meeting on 7 October 2010 and met a further 7 times, the final meeting being on 25th February 2011. Not all members were able to attend each meeting, and representatives of some members varied from meeting to meeting. However, minutes of meetings were circulated to all members of the Working Group.

Status

The Working group did not debate the merits or otherwise of moving to consultancy charging, as the FSA had already published its final rules. Nor did the Working Group seek to influence changes to the FSA's rules or the issuing of formal guidance by the FSA. Rather, the Working Group attempted to produce guidance on good practice (and caveats about poor practice) to which firms might look. To that end the Working Group identified Key Principles which should be adhered to in consultancy charging, together with some Factors which should be taken into account. These are set out in the following sections of this report, as are suggested main elements required in Contracts relating to adviser remuneration and consultancy charging arrangements.

The suggestions which follow are not prescriptive and are intended purely as a guide as to how consultancy charging might operate in practice. The Working Group recognised that there is no one single fairest way to allocate consultancy charges and that each scheme will have its own individual set of circumstances. However, the Working Group offers this report as guidance to firms and others about the issues which should be considered and addressed when consultancy charging is discussed with employers (and employees).

The Working Group focused its efforts mainly on contract-based pension schemes, including group personal pensions, group stakeholder pensions and group SIPPs. But the Group considers that its deliberations and conclusions around consultancy charging can have equal application to defined contribution occupational pension schemes.

Principles

The Working Group considered key principles, which consultancy charging should include are:

Simplicity

All parties should understand the charge and services provided should be clear, fair and not misleading

Transparency

It should be easy to see what is being paid for what service

Value

The service should provide value to the employer and member

Flexibility/Adaptability

The ability to change should be built into the scheme

Factors

The Working Group further considered that factors which advisers should consider in agreeing consultancy charges with employers included the following:

Clear, fair and reasonable charges

Charges should be clear, fair and reasonable; be commensurate with the costs and value of the advice and/or services provided; and should be unlikely to create adverse outcomes for pension scheme members.

Description of charges

Charges should, as far as possible, distinguish between:

- Initial charges
(for advice and/or services provided at scheme outset and/or date new members join)
- On-going charges
(for advice and/or services provided during the term of the scheme)
- One-off charges
(e.g. for advice and/or services provided during the term of the scheme, the costs of which have not previously been included in any initial and/or on-going charges)

Charge recovery methods

Employers should be offered a choice of charge recovery methods, which may include:

- Fees
(paid by the employer and/or recovered from employer and/or employee contributions) and/or
- Consultancy charges
(deducted from employer and/or employee contributions received by the pension scheme, and/or from funds under management)

Charge types

Employers should be offered a choice of charge types, which may include:

- Fixed or tiered monetary sum(s);
- Fixed or tiered percentage(s) of employer and/or employee contributions; and/or
- Fixed or tiered percentage(s) of funds under management

Cross-subsidies

Charge cross-subsidies should be identified and either agreed with the employer or mitigated. For example, cross subsidies may exist between:

- Employer and scheme members
(e.g. where advice and/or services to the employer are recovered in part, or in whole, from the scheme members)
- Initial scheme members and subsequent joiners
(e.g. where scheme set up costs are borne by initial joiners only)
- Existing scheme members
(e.g. where scheme members with larger funds/contributions pay more (in simple monetary terms) than those with lower funds/contributions)
- Active scheme members and deferred scheme members

Charge recovery period

Initial and/or one-off charges may be recovered:

- Immediately;
- In the shortest possible term
(e.g. if unable to recover immediately)
- Over a prescribed time period
(e.g. 12 – 60 monthly instalments)

Recovery of outstanding charges

Any liability for outstanding charges (for advice and/or services received), and the means by which they will be recovered (if at all) should be clarified and agreed. Such charges could arise, for example, in the event a scheme member leaves pensionable service² or transfers. Recovery options may include:

- One-off fee, levied against the employer
- One-off consultancy charge, recovered from the funds under management
- For deferred members, continued recovery of previously agreed consultancy charges
- Write-off of any outstanding charge(s) due

² i.e. stops accruing benefits under the employer's pension scheme as a result of leaving that employment or by requesting that pension contributions paid by them and/or on their behalf cease.

Deferred members

Any charges and the means of their recovery, for advice and/or services to, or in respect of, deferred members should be clarified and agreed. Options may include:

- Employer fees
- Consultancy charges
- Adviser charges³
(via separate, individual agreements with each deferred member)

Charge agreements

Separate agreements may exist between:

- advisers and employers
(setting out the advice and/or services to be provided, and the related charges)
- employers and providers
(setting out any consultancy charging arrangements)

The terms and conditions of the agreement(s) should be clear, consistent and unambiguous, and should define the responsibilities, duties and liabilities of the respective parties, including:

- During the term of the agreement
- In the event of a dispute or failure to comply
- On review and/or termination of the agreement

A draft contract is included in Annex A for illustrative purposes only.

Future variations and/or increments

Any charges which will be automatically levied in the event of an agreed, expected or foreseeable variation and/or increment should be clarified and agreed.

³ An 'Adviser Charge' is defined in the FSA's Handbook of rules and guidance as "*any form of charge payable by or on behalf of a retail client to a firm in relation to the provision of a personal recommendation by the firm in respect of a retail investment product (or any related service provided by the firm) which is agreed between that firm and the retail client in accordance with the rules on adviser charging and remuneration (COBS 6.1A).*"

Good and Poor Practice

The Working Group noted that there is no one size fits all approach to consultancy charging and that what is practical for one scheme may not be practicable for another scheme. As a guide, however, they concluded that the following were examples of good and poor practice which should be kept in mind when implementing a consultancy charging arrangement:

Good Practice

- The consultancy charging arrangement should take account of the needs of the employer
- It should also take account of the needs, demographics and characteristics of the employer's workforce so that it's fair, as far as possible, to all members
- The arrangement should detail clearly the services being provided, to whom, the cost of these services, who is paying for them and how they are being paid for
- There should be a clear distinction between services provided under the consultancy charging arrangement from those provided under any adviser charging arrangement
- Where the consultancy charge includes a prearranged individual advice service, the cost of the service should be clearly shown. The member should be told where they can opt out of an individual advice service
- Cross-subsidy between members may be appropriate. For example, a consultancy charge proportionate to contributions or member funds may be preferable to a flat charge which penalises lower earners. This should, however, be weighed against the need for simplicity and consistency of approach across the membership as a whole
- If consultancy or adviser charges will have a significant adverse impact on members' funds, consideration should be given to whether member advice may be delivered more cost effectively. For example, by providing guidance via employee seminars
- The charge structure should be simple and transparent so that employers and members understand how much the advice and services cost, and the benefits they receive from it
- The charge structure should be stable, as far as possible, so that it does not have to be changed often. Costs incurred by the scheme as a result of legislative changes may be an example where an increase in charges cannot be avoided

- The charge structure should be adaptable to a member's changing needs. For example, on a member leaving the employer's service
- Clear communications and disclosure of the charges to members
- An education program explaining to employees the benefits of the scheme and saving for retirement
- For a member leaving the employer's service, any consultancy charges in respect of ongoing (as opposed to initial set up) services should be replaced if necessary by an adviser charging arrangement where individuals wish to continue to receive ongoing services

Poor Practice

- Charging an employer or member for a service not provided. For example, if a member opts out of an individual advice service or leaves employment
- Overcharging an employer or member for an agreed service
- Services and costs not clearly defined under the consultancy charging agreement
- Complex charging structures that employers and members don't understand
- Charges which disproportionately impact on different categories of members. For example, high initial charges may disproportionately impact on members paying low contributions
- Applying unexpected additional charges (which could reasonably have been anticipated in advance) to an existing member. For example, the costs and timings of periodic reviews should be able to be anticipated whereas costs arising from future legislative changes will be unknown
- Continuing to apply the same level of ongoing consultancy charging to deferred members (unless the same level of services is maintained)
- Failure to review an agreement in light of changes in circumstances.

Disclosure to Employers and Employees

The Working Group thought that when offering guidance with respect to good practice in consultancy charging it would also be helpful to remind firms about the FSA's rules in respect of disclosure of consultancy charges to employers and employees:

Employers

The rules on disclosure of consultancy charges by advisers to their employer clients are set out in the FSA's Handbook at COBS 6.1C.18 R with some extra guidance at COBS 6.1C.19 G.

For full details, please refer to the FSA's rules. In brief, an adviser should discuss and agree any consultancy charges with the employer before the employer settles on a particular course of action regarding its pension arrangements. As part of that discussion, the information given to the employer should include a document disclosing the consultancy charges that their various employees will bear, including the amounts and timespans and the effects on members' funds should they leave the employer or the scheme is cancelled before all charges are paid.

The format of the disclosure document is not prescribed, but disclosure of consultancy charges should be in cash terms and should illustrate how the charges may change over time.

Employees

The rules on disclosure of consultancy charges to employees are set out in COBS 6.1D.11 R with extra guidance at COBS 6.1D.12 G and 6.1D.13 G.

Comprehensive and clear disclosure of the consultancy charges an employee will bear should be made to the employee in good time so that he or she can make an informed decision before being committed to joining the scheme. The issue of the Key Features Document (required elsewhere in the FSA's rules) presents a suitable opportunity to deliver the consultancy charges information to new joiners at an appropriate time.

It's essential that employees are made fully aware on joining if there is the potential for consultancy charges to increase or change at some later stage, for example should additional charges arise when fresh services are provided to the employer. Full details will need to be disclosed to each employee of any fresh charges in good time before any increase takes effect, along with the actions the employee can take.

As with employers, the information given to an employee should disclose the consultancy charges, including the amounts and timespans and the effects on the employee's funds should he or she leave the employer or the scheme is cancelled before all charges are paid.

Disclosure of consultancy charges should be in cash terms and should illustrate how the charges may change over time.

Acknowledgments

As the original FSA consultation showed, the issues involved in consultancy charging are complex, and discussion within the Working Group was lively. I am grateful, however, for the positive and constructive spirit in which all members participated in the Working Group. They did so as individual industry practitioners, rather than as representatives of their firms and organisations, who have not necessarily endorsed the report. I am also grateful for Faiza Ahmad's (FSA) patient work as Secretary.

Sir James Hodge

Chairman

Consultancy Charging Working Group

25 February 2011

Annex A: Contracts

THIS AGREEMENT is made on [date]

BETWEEN

- (1) XYZ Limited, a company registered in England with registered number [RN] and having its registered office at [address] ("the Employer"); and
- (2) Adviser Limited ("the Adviser")

WHEREAS

- (A) The Adviser is to provide services to the Employer;
- (B) The services to be provided may include arranging personal pension contracts with an approved provider of such policies ("Approved Provider");
- (C) The Adviser may be remunerated for providing the services, in whole or in part, by payments made by the Approved Provider on behalf of the Employer.

IT IS AGREED THAT

THE SERVICES

- 1 The Adviser will provide the services detailed in Schedule 1 to this Agreement ("the Services") to the Employer.
- 2 The Employer undertakes to provide the Adviser with such information as it requires to facilitate the provision of the Services.
- 3 The Adviser undertakes to provide the Services within such timescale as may be agreed between the Employer and the Adviser from time to time.
[Consider including a performance standard. Since the provider will not be a party to the agreement, performance standard may need to be subject to provider performance]
- 4 In providing the Services the Adviser may arrange personal pension policies ("the Policies") with an Approved Provider.

REMUNERATION OF ADVISER

- 5 The Adviser will be remunerated for the provision of the Services on the basis set out in Schedule 2 to this Agreement ("the Agreed Fees"). [Fees can be specific amounts, and/or specified percentages of contributions/fund value. They can include amounts paid directly by the Employer to the Adviser]
- 6 All or part of the Adviser's remuneration may be secured by the payment by the Approved Provider to the Adviser of consultancy charges, as defined in the Financial Services Authority's Handbook ("Consultancy Charges").
- 7 The basis for payment of Consultancy Charges will be set out in the Approved Provider's Declaration ("the Declaration") to be appended to this Agreement.
- 8 The Employer confirms that it agrees to the payments specified in The Declaration being paid to the Adviser by the Approved Provider, and undertakes to provide confirmation of its agreement to such payments as may be required by the Approved Provider not later than [one month] after such confirmation being requested.

TERMINATION OF AGREEMENT

- 9 This Agreement will remain in force for a minimum period of [two years], unless the parties agree otherwise.
- 10 This Agreement may be terminated by either party giving [three] months' notice in writing (or such shorter period as may be agreed in writing between the parties) to the other party, such notice to expire not earlier than the end of the minimum period specified in Clause 9.
- 11 [Clauses that survive termination – e.g. right to be paid, dispute procedure..]

DISPUTES

- 12 In the event of any dispute arising between the Employer and the Adviser..[specify dispute procedure, if arbitration who appoints, cost sharing etc]

RIGHTS OF THIRD PARTIES

- 13 It is declared by the parties to this Agreement that none of the terms of the Agreement are to be enforceable by virtue of section 1 of the Contracts (Rights of Third Parties) Act 1999 by any other person. [Note that where the Services specify services to be provided to employees, the Employer will be responsible for ensuring they are provided. Any dispute raised by an employee about payment of a Consultancy Charge for services not provided to the employee will be between employee and employer.]

PAYMENT

- 14 [Primary responsibility for payment of Agreed Fees resting with Employer. In the event of a dispute about payment the normal procedures for enforcing a contract would apply.]

DISCLOSURE

- 15 [Restrictions on disclosure (if any) and confidentiality].

CHANGE OF CONTROL

- 16 [How fees to be paid if change of control of Employer / Approved Provider / Adviser? Linked to this, normally include provision making it clear that the agreement is personal to the parties and is not capable of assignment without having obtained the prior agreement in writing of all parties]

[DUTIES OWED?]

- 17 [Worth being explicit about the nature of duties owed by the Adviser to the Employer / scheme members? – esp. fiduciary if any?]

AMENDMENT

- 18 [Who can amend and in what circumstances].

GOVERNING LAW

This Agreement is to be interpreted according to, and be governed by, the laws of England and will be subject to the exclusive jurisdiction of the English courts.

Schedule 1

The Services

1 Fact finding

Discussions with regard to objectives
Establish budget available
Establish level of benefits wish to provide
Advice regarding typical benefit structures
Advice regarding the setting of contribution levels
Advice regarding enrolment procedures
Discussions regarding impact of auto-enrolment obligations and qualifying scheme requirements
Consideration of all potential benefits and possibility of flexible benefits
Obtain data on the membership to be covered so that full quotations can be prepared.

2 Provider Selection

Consideration of full market to determine appropriate providers for pension and other benefits and preparation of report outlining recommendations
Report to provide reasons for selection of provider(s), payment methods, charges and detail of investment funds available.
Report to also outline default funds to be offered and reasons for their selection including lifestyle options and target date fund options
If desired arrange beauty parade of shortlisted providers and discuss outcome to agree final choice.
Options with regard to advice proposition
Remuneration options and impact on terms

3 Employer Meeting

Meeting to discuss report and recommendations and agree way forward
Agree the details of the scheme design including contribution rates for employees and employer, and eligibility terms.
Discuss the impact of auto-enrolment
Agree the extent to which the employer wishes members to receive individual advice and how the cost of this is to be covered.
Review draft communications and agree time to issue
Agree start date of scheme
Agree establishment of Governance Committee and its terms of reference

Agree timetable for review meetings to cover initial establishment and then future operation.

Agree remuneration and method of payment

4 Member Communications

Prepare announcement to all potential scheme members explaining scheme in simple terms and benefits of joining

Prepare notes on scheme fund choices available and their risk profiles

Issue risk questionnaire to assist members determine their attitude to risk

Provide details of default fund or funds and attributes of these funds and how they have been selected

Prepare “Scheme Booklet”, providing more details of scheme, and choices available and generic illustrations of potential benefits

Establish a member helpline

Arrange seminar presentations to introduce the pension scheme and any other benefits and give opportunity for questions

Provide details of online support and how to access this

Confirm what can and can not be done online.

5 Establishment

Arrange meeting between provider and employer to ensure all administration procedures clear and understood

Arrange preparation and issue of all individual member quotations

Issue application forms for members to complete and return allowing collection of member contributions and confirming investment choice

Collate and schedule information from member application forms to pass to employer and provider

Ensure initial premium collection works smoothly and procedure in place for efficient processing of all subsequent premium collections.

Agree procedures for subsequent entrants – provision of list of potential new members each month so that they can be sent an introductory pack with details of arrangements and application form to be completed

6 Salary Sacrifice

Discuss this option with employer outlining advantages and disadvantages. If to offer agree how any NI saving is to be treated.

If employer wishes to offer then prepare announcement to potential members explaining this option

Prepare exchange of letters template.

7 Individual Advice

If part of main service arrange meeting days to schedule individual appointments and discuss options and particularly investment choices with each member

If not part of main service , prepare and issue announcement explaining benefit of individual advice and details of how it will be paid for with offer of meetings for those who so wish to use the service.

8 Review Meeting

Agree timetable for regular review meeting every 6 months/year to check that all aspects of arrangements performing as they should and review any issues.

Ensure that all parties are happy with efficiency of administration and consider any potential improvements.

Attend and minute Governance Committee meetings

Provide regular management information

9 Presentations

Arrange annual generic presentations to update employees on pension benefits generally, outline how the scheme has performed, any amendments proposed and to encourage those who have not joined to reconsider their position. Opportunity for all members to ask questions.

10 Helpline

Maintain helpline so that members can raise any queries that they may have and these can be resolved efficiently.

Schedule 2

The Agreed Fees

Example

- | | | |
|---|-----------------------|---|
| 1 | Fact finding | £ABCD fee |
| 2 | Provider Selection | £ABCD @ £ABCD per month consultancy charge for six months |
| 3 | Employer Meeting | £ABCD fee |
| 4 | Member Communications | £ABCD per member per month consultancy charge |

etc.

(If performance standards are specified in Schedule 1 include reference to any penalty provision for failing to meet standards, although note that penalties cannot be dealt with by way of Consultancy Charges)

Annex B: ToR

Corporate Pensions Consultancy Charging Working Group: Terms of Reference (TOR)

The Financial Services Authority (FSA), having determined that consulting charges should be introduced for Group Personal Pension schemes (GPPs) by the end of 2012, has undertaken to convene an industry working group, to be styled the Consultancy Charging Working Group (the WG) to:

- discuss the allocation of “consultancy charges” among members of GPPs, with a view to
- arriving at a clear and comprehensive statement of the factors which should be taken into account when considering any GPP scheme, while
- recognising at the same time that there will be no single solution as to what makes for the most equitable allocation of consulting charges.

The Society of Pension Consultants (SPC) has agreed to facilitate the work of the WG, which will be Chaired by the SPC Chairman, Sir James Hodge. The FSA will provide the Secretariat of the WG and will observe, but not participate in, the deliberations of the WG.

Membership of the WG will include representatives drawn from, among others

- Trade Bodies
- Leading GPP Providers
- Firms of Independent Financial Advisers (IFAs)
- Employee Benefits Consultants
- Third-party Administrators
- Consumer Bodies

The WG will begin its deliberations in October 2010 and meet regularly thereafter at intervals and with a frequency to be determined by the Chairman, with the aim of producing by 28 February 2011, or as soon as possible thereafter, proposals and suggestions intended to be of assistance to corporate advisers in discussions with employer clients about consultancy charging.

How the WG’s conclusions should or might be disseminated to interested parties is yet to be determined: proposals in respect of that should also form part of the WG’s conclusions.

Agreed between the FSA and the SPC

London

3 September 2010

Annex C: Eventual Membership

Member	Representing:
Sir James Hodge (Chair)	The Society of Pension Consultants
John Quinlivan	AEGON
Adam Potter	
Steven Cameron	
Douglas Herdman	
Peter Williams	
Jacqueline Thornton	AIFA
Andrew Strange	
Peter Jolly	Association of British Insurers
Alexander Smith	
Alexandra Hughes	Aviva
Steve Jackson	
Teresa Wagstaff	
Alex McGill	Blake Laphorn
Mario Lopez-Areu	CBI
Doug Johnstone	Creative Benefit Solutions
Sally Webber	
Andrew McCarthy	
Rob Pearce	HSBC
Jason Owen	
Joanne Weightman	
Carolyn Jones	FIL Pensions Management
Alistair Wadsworth	Jardine Lloyd Thompson Benefit Solutions
Paul Armitage	
Paul McBride	Legal & General
Roger Breeden	Mercer
Duncan Revolta	One Pension Consultancy LLP
Sarah Munro	
Russell Warwick	Prudential
Ian Ormrod	
Alan Gaukroger	Punter Southall D C Consulting
Robert Young	Regents Pensions Ltd
Robin Nimmo	Scottish Life
Robert Kerr	Scottish Widows
Allan Richardson	
Michael Craig	Standard Life Assurance
Chris Goodeve-Ballard	The Society of Pension Consultants
Ken Anderson	Xafinity Consulting
Joanne Hull	
Ian Johns	