

## Chapter 19

# Pensions supplementary provisions

## 19.12 Non-workplace pensions: default options and cash warnings

### Definitions

19.12.1

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In ■ COBS 19.12:

- (1) 'cash warning' is the warning in ■ COBS 19.12.31R;
- (2) 'distributes' includes having an arrangement with a third party to arrange an *investment*, or to promote *platform services* that distribute *investments*;
- (3) 'filtering tool' means a tool whereby a *firm* makes the list of the *investments* it sells easier to search by allowing the *customer* to filter products based on factors presented by the *firm* and selected by the *customer*, and showing to the *customer* the *investments* that meet the factors selected by the *customer*; and
- (4) 'pre-purchase questioning tool' means a tool which involves putting a sequence of questions in order to extract information from a *person* to help them best select an *investment* that meets their needs. A decision tree is an example of a pre-purchase questioning tool. The process of going through the questions will usually narrow down the range of options that are available.

### Application of default option rules

19.12.2

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■ COBS 19.12.10R to ■ COBS 19.12.22G apply to an *operator* of a *non-workplace pension scheme* that:

- (1) offers, distributes or promotes *investments*, or promotes *platform services* that distribute *investments*, in relation to their inclusion in a *non-workplace pension* of the *operator*; or
- (2) accepts, for inclusion in a *non-workplace pension*, *investments* which are offered, distributed or promoted by another *person* where that other *person*, or another *person* connected to it, also arranges for the *retail client* to enter into the *non-workplace pension* with the *operator*.

19.12.3

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The effect of ■ COBS 19.12.2R is that ■ COBS 19.12.10R to ■ COBS 19.12.22G:

- (1) do not apply where an *operator* only *arranges* an *investment* for inclusion in, or the provision of *platform services* in respect of, a *retail client's non-workplace pension*, at the request of the *retail client*. In

		<p>these circumstances, therefore, the <i>operator</i> does not offer, distribute or promote any <i>investments</i>, nor does it promote <i>platform services</i> that distribute <i>investments</i>.</p> <p>(2) apply where an <i>operator</i> accepts, for inclusion in a <i>retail client's non-workplace pension</i>, an <i>investment</i> offered, distributed or promoted by a third party, including a <i>platform services provider</i> or an introducer, where that third party or someone connected to that third party also arranges for the <i>retail client</i> to enter into the <i>non-workplace pension</i> with the <i>operator</i> unless the <i>retail client</i> has received or will receive, either as part of transactional or ongoing advice, a <i>personal recommendation</i> in relation to the <i>investment</i> of their contributions to, or assets in, the <i>non-workplace pension</i> (see ■ COBS 19.12.5R).</p>
19.12.4	R	<p>■ COBS 19.12.10R to ■ COBS 19.12.22G do not apply where an <i>operator</i> starts treating a <i>retail client's</i> workplace pension arrangements as a <i>non-workplace pension</i> after the <i>retail client</i> has become a deferred member of the relevant <i>qualifying scheme</i>, so long as the <i>firm</i> does not offer, distribute or promote to the <i>retail client</i> any <i>investments</i> or <i>platform services</i> other than those available in connection with the former workplace pension arrangements, including the <i>default arrangement</i> and any <i>investments</i> available on a self-select basis.</p>
		<p><b>Exclusion from default option rules in relation to advised clients</b></p>
19.12.5	R	<p>■ COBS 19.12.10R to ■ COBS 19.12.22G do not apply in relation to a <i>non-workplace pension</i> where the <i>firm</i> has determined, on reasonable grounds, that the <i>retail client</i>:</p> <p>(1) has received or will receive, either as part of transactional or ongoing advice, a <i>personal recommendation</i> in relation to the investment of their contributions to, or assets in, the <i>non-workplace pension</i>; or</p> <p>(2) has appointed an <i>investment manager</i> in relation to the investment of the <i>retail client's</i> contributions to, or assets in, the <i>non-workplace pension</i>.</p>
19.12.6	G	<p>A <i>firm</i> will not have reasonable grounds to determine that a <i>retail client</i> has received, or will receive, a <i>personal recommendation</i> for the purpose of ■ COBS 19.12.5R(1) if the determination is based solely on information that:</p> <p>(1) is over 12 <i>months</i> old;</p> <p>(2) the <i>retail client</i> is in, or transferring from, an advised product; or</p> <p>(3) the <i>retail client</i> provides <i>remuneration</i> to an <i>adviser</i> in relation to other <i>investments</i>.</p>
		<p><b>Application of cash warning rules</b></p>
19.12.7	R	<p>■ COBS 19.12.23R to ■ COBS 19.12.33G apply to an <i>operator</i> of a <i>non-workplace pension scheme</i>.</p>

- 19.12.8** **R** ■ COBS 19.12.23R to ■ COBS 19.12.33G do not apply in relation to a *non-workplace pension* where the *firm* has determined, on reasonable grounds, that the *retail client* has appointed an *investment manager* in relation to the investment of their contributions to, or assets in, the *non-workplace pension*.

### Purpose

- 19.12.9** **G**
- (1) The purpose of this section is to specify the circumstances where a *firm* must:
    - (a) offer a *default option* to a *non-advised client* in connection with their *non-workplace pension*; and
    - (b) provide warnings to a *retail client* who has invested, for a sustained period of time, over a certain percentage of their *non-workplace pension* in *cash-like investments*.
  - (2) The *default option* rules in ■ COBS 19.12 are designed to help *non-advised clients* who are generally unable or unwilling to engage with *investment* decisions, or find it difficult to identify appropriate *investments* for inclusion in their *non-workplace pensions*, including where questionnaires or filtering tools are used. The purpose of the rules in ■ COBS 19.12 is to help these *non-advised clients* to choose an appropriate *investment* option.

### Requirement to offer a default option

- 19.12.10** **R** A *firm* must offer its *retail clients* a *default option* for inclusion in the *non-workplace pensions* it operates for those clients.
- 19.12.11** **R** A *firm* must not:
- (1) offer more than one *default option* to each *retail client*; or
  - (2) make the decision as to which *default option* to offer to each *retail client* by depending on the *retail client's* answers to questions set out in a pre-purchase questioning tool or a filtering tool.
- 19.12.12** **G** A *firm* may, as a single *default option*, offer a series of different *target date funds* that depend on *retail clients'* target retirement dates.

### When and where to offer a default option

- 19.12.13** **R** A *firm* must offer the *default option*:
- (1) at the time the *retail client* enters into the *non-workplace pension* operated by the *firm* (regardless of whether an initial cash contribution is made at this stage); and
  - (2) again at the time the *retail client* makes their initial cash contribution (if one has not already been made on entry) into the *non-workplace pension*,
- unless the *retail client* is, at the point of entry into the *non-workplace pension* with the *firm*, only transferring in *investments* they already hold

elsewhere and will continue to use the investment strategy associated with those *investments* when making requests of the *firm*.

19.12.14 **G** Where a *retail client*:

- (1) makes their initial cash contribution at the point of entry into the *non-workplace pension* with the *firm*, the *firm* will need to bring the existence of the *default option* to the attention of the *retail client* at that stage; and
- (2) makes their initial cash contribution after the point of entry into the *non-workplace pension* with the *firm*, the *firm* will need to comply with ■ COBS 19.12.13R by offering the *default option* both at the stage at which the *client* enters the *non-workplace pension* and again at the point they make their initial cash contribution.

19.12.15 **R** Additionally, where a *firm*, or any other *person* involved in the offer, distribution or promotion of *investments* for inclusion in a *non-workplace pension* of the *firm*:

- (1) sets out, in menus or otherwise, the other *investments* available to the *retail client* for inclusion in their *non-workplace pension*, the *firm* must set out the *default option* in a location most likely to bring it to the attention of that *retail client*;
- (2) makes available pre-purchase questioning tools or filtering tools that enable a *retail client* to select *investments* for inclusion in their *non-workplace pension*, the *firm* must set out the *default option* alongside those tools.

19.12.16 **G** It is unlikely that complying with ■ COBS 19.12.15R(1) would require a *firm* to set out the *default option* in every menu, or in every level of a menu, where other *investments* are set out.

### How to present the default option

19.12.17 **R** A *firm* must present a *default option*:

- (1) when complying with ■ COBS 19.12.13R, prominently and on a standalone basis; and
- (2) when complying with ■ COBS 19.12.15R, with at least equal prominence to any other *investment*, pre-purchase questioning tool or filtering tool made available to *retail clients* alongside the *default option*.

19.12.18 **R** When complying with ■ COBS 19.12.13R and ■ COBS 19.12.15R, a *firm* must ensure that it:

- (1) labels a *default option* in a sufficiently clear way to give an indication of the nature of it and also to distinguish it from the *firm's* other offerings;

- (2) sets out, in a clear and prominent way, the aims of the *default option*, explains that the *default option* has been designed to meet the needs, objectives and characteristics of a typical *non-advised client* in the target market for the *default option*, and sets out what the *manufacturer* considers those needs, objectives and characteristics to be; and
- (3) makes it clear that the *default option* is not tailored to the specific needs, objectives or characteristics of each *retail client*, and that if the *retail client*:
  - (a) considers that their needs, objectives and characteristics may fall outside those of the typical *non-advised client* in the target market as described by the *firm*, they may wish to consider other investment options;
  - (b) wishes to ensure that the *non-workplace pension* and any *investments* included in it (including the *default option*) are suitable for them, the *retail client* should consider seeking *investment advice*.

#### Preparing to offer a default option

- 19.12.19 **R** A *firm* must be in a position to offer a *default option* in good time before it has to offer the *default option* pursuant to ■ COBS 19.12.10R, in order to allow for sufficient internal product governance.
- 19.12.20 **G** The *default option* may be *manufactured* by either the *operator* alone, by another *firm*, or by both, and *distributed* by either the *operator* alone, or by the *operator* and another *firm*.
- 19.12.21 **G** *Manufacturers* and *distributors* of *default options* must comply with the applicable product governance requirements in *PROD*. Where the manufacturing is done by another *firm* (either alone or with the *operator*), the *operator* is still responsible for the obligations under ■ COBS 19.12.10R to ■ COBS 19.12.18R.
- 19.12.22 **G**
- (1) Where *firms* decide to replace a *default option*, they may need to consider whether it would be appropriate to transfer existing clients to the new *default option*.
  - (2) This may be the case, for example, if the transfer is required to prevent consumer harm and avoid risking non-compliance with our *rules*, for example *Principle 6*. This could be the case where *firms* determine that the *default option* no longer meets the applicable product governance requirements in *PROD* and existing clients are likely to suffer harm as a result.
  - (3) If *firms* decide to transfer existing clients to a new *default option*, they will need to consider the information needs of their clients, and communicate to them appropriately and in good time, in a manner that is clear, fair and not misleading.
  - (4) *Firms* are required to have appropriate contractual arrangements in place (including contractual powers that are fair and transparent and

comply with the *CRA*) to enable them to transfer existing *clients* to a new *default option* and to comply with their obligations under the *regulatory system*.

### Cash warnings: conditions

**19.12.23 R** At least once during every 3-month period, for each of the *non-workplace pensions* that *retail clients* have entered into with the *firm*, the *firm* must assess whether the following conditions are met at the time of the assessment:

- (1) more than 25% of the *non-workplace pension* is invested in *cash-like investments*, excluding any *cash-like investments* held in connection with *lifestyling* or within a *target date fund*;
- (2) the amount of the cash holding in (1) is greater than £1,000;
- (3) the conditions in (1) and (2) were also met in all the other assessments carried out during the 6-month period preceding the day of the assessment; and
- (4) the *retail client* is more than 5 years away from:
  - (a) normal minimum pension age, as defined in primary legislation from time to time; or
  - (b) if lower, a protected pension age.

**19.12.24 R** For the purposes of ■ COBS 19.12.23R, the start of the 3-month period is

- (1) initially determined by reference to the date members enter into their *non-workplace pensions* with the *firm*; and
- (2) after the initial 3-month period, by reference to the date when, for each *retail client*, the *firm* last carried out, or should have carried out, the assessment under the *rule*.

### Cash warnings: timing

**19.12.25 R** If all the conditions in ■ COBS 19.12.23R are met, the *firm* must provide the *retail client* with a cash warning within an appropriate timeframe after the date when the assessment in that *rule* was carried out.

**19.12.26 G** For the purposes of ■ COBS 19.12.25R, an 'appropriate timeframe' is likely to be within 3 months of carrying out the assessment in ■ COBS 19.12.23R, unless the current market conditions would make it inappropriate to warn the *retail client* about their cash holdings within that timeframe, although providing the cash warning later than 6 months after the date of the assessment is unlikely to be appropriate.

**19.12.27 R** If a *firm* has provided a cash warning pursuant to ■ COBS 19.12.25R, the requirement in ■ COBS 19.12.25R does not apply again until after 1 year of the *firm* providing the previous cash warning.

**19.12.28** **G** Notwithstanding **■ COBS 19.12.27R**, a *firm* can choose to provide a new cash warning during the year following the previous cash warning, in which case **■ COBS 19.12.27R** would apply from the date when the new cash warning is provided.

**19.12.29** **G** Where the condition in **■ COBS 19.12.23R(4)** is no longer met, a *firm* should consider whether it would be appropriate to keep providing the cash warning up until the time a *retail client* accesses their pension.

**19.12.30** **G** A *firm* may send the cash warning with other client communications, provided that the cash warning is included in a document separate to those other client communications.

### Cash warning: form and content

**19.12.31** **R** The cash warning at **■ COBS 19.12.25R** must:

- (1) be provided in a *durable medium*;
- (2) using plain language, warn the *retail client* that:
  - more than 25% of their *non-workplace pension* is invested in *cash-like investments*; and
  - the value of their *non-workplace pension* is at risk of being eroded by inflation;
- (3) include a generic example (provided as an explanation, an illustration or both) of how inflation erosion would affect a £10,000 cash pot over 10 years, assuming 0% interest and using a measure of inflation generally accepted in the *United Kingdom*; and
- (4) inform the *retail client* that they should consider whether their current investments are likely to grow sufficiently to meet their objectives.

**19.12.32** **G** The *firm* should also:

- (1) inform the *retail client* that:
  - (a) the cash warning is not advice or a substitute for it; and
  - (b) the value of any *investment* can fall as well as rise;
- (2) explain to and/or illustrate for the *retail client* that different types of *investment* have a different balance of risk to potential gain; and
- (3) include in the cash warning a statement to the effect that, where applicable, the *firm* makes available *investments* for inclusion in *non-workplace pensions*, including the *default option*.

**19.12.33** **G** In the *FCA's* view, the Consumer Prices Index is a national index of retail prices and so may be used as a measure of the current inflation rate for the purposes of **■ COBS 19.12.31R(3)**.



**Record keeping**

- 19.12.34** **G** A firm to which the record-keeping rules in ■ SYSC 3 (Systems and controls) or ■ SYSC 9 (Record-keeping) apply will need to maintain a record of its compliance with the requirements in this ■ COBS 19.12 section including, where relevant, how it has determined on reasonable grounds (including records of the evidence it has relied upon) that, in accordance with ■ COBS 19.12.5R, a *retail client* is not a *non-advised client*.
- 19.12.35** **R** A firm must also maintain a record of:
- (1) the number of *non-advised clients* entering into a *non-workplace pension* with the *firm* each year;
  - (2) the number of those *retail clients* in (1) who chose the *default option*;
  - (3) the number of *retail clients* not included in (1) that choose the *default option* each year, distinguishing between *retail clients* who were *clients* of the *firm* before ■ COBS 19.12.10R to ■ COBS 19.12.22G came into force and those who became *clients* later;
  - (4) the volume of contributions made by *retail clients* to the *default option* each year;
  - (5) the volume of assets under management attributable to the *default option*;
  - (6) a description of the product approval process for the *default option* and of any reviews undertaken in compliance with ■ PROD 6;
  - (7) in relation to cash warnings, differentiating between advised clients and *non-advised clients*, as well as between those *retail clients* who were *clients* of the *firm* before ■ COBS 19.12.23R to ■ COBS 19.12.33G came into force and those who became *clients* later:
    - (a) the dates when assessments were carried out, alongside the number of *retail clients* assessed on those dates;
    - (b) of the *retail clients* in 7(a), the number who met the conditions at ■ COBS 19.12.23R; and
    - (c) of the *retail clients* in 7(b), the number who continue to meet the conditions at ■ COBS 19.12.23R in subsequent assessments.