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Dame Meg Hillier MP
Chair - Public Accounts Committee
House of Commons
London
SW1A 0AA

28 September 2022

Our Ref: C220725B

Dear Dame Meg Hillier

RE: Public Accounts Committee 'Investigation into the British Steel Pension Scheme'

1. Introduction

I am writing to you following the Public Accounts Committee report 'Investigation into the British Steel Pension Scheme', published on 18 July 2022 (the report), and the prior National Audit Office (NAO) report 'Investigation into the British Steel pension scheme' published on 18 March 2022 (the NAO report). We welcomed the opportunity to provide evidence to the Committee in person, and to the NAO in writing. We thank the Committee for their consideration of these matters, and for their subsequent report.

We have provided a formal response to Committee's recommendations as part of the HM Treasury minutes for September 2022. This letter is intended to accompany our formal response, providing more detailed updates in line with the Committee's recommendations and responding to some of the wider conclusions of the report.

The restructure of the British Steel Pension Scheme (BSPS) and its aftermath caused harm, affecting the lives of many thousands of British Steel pensioners. Of 122,000 BSPS members, 44,000 were eligible for a Defined Benefit (DB) transfer. Exceptional levels of unsuitable advice led to 7,700 members of the BSPS transferring out of their DB pension to a Defined Contribution (DC) pension scheme when it was not in their best interests to do so. They have suffered financial loss as a result. I acknowledge the distress this has caused these BSPS members. There are lessons to learn, both for how we operate as a regulator, and for how the wider pensions regulatory system serves to protect consumers. These are rightly made clear in the Committee's report, though this does not fully acknowledge the extent to which we have responded since 2017: acting against poorly performing firms and improving the wider defined benefit pension transfer market. For example, in the case of BSPS over £20 million of redress has been paid out by firms due to the action the FCA has taken.

We have taken significant action to encourage steelworkers to complain including using the Financial Ombudsman Service or the Financial Services Compensation Scheme if the firm in question has failed. Recognising the low levels of such complaints we are now going further and

have recently consulted on proposals for a consumer redress scheme under s.404 of Financial Services and Markets Act (FSMA). We estimate this will deliver £71.2m in total redress to 1,400 consumers. This is in addition to £55m paid out to date by FSCS for 899 customers of insolvent firms and over £20m paid out by firms due to action the FCA has taken.

2. The British Steel Pension Scheme

a. Impact of unsuitable advice

We share the concern of steelworkers, MPs and other stakeholders about the levels of unsuitable advice and recognise the harm that this has caused to steelworkers and communities.

To assess the extent of unsuitable advice, we commissioned an external statistician to establish with reasonable certainty the percentage of transactions that involved unsuitable advice to transfer from BSPS. Using data we already held from previous work, alongside additional file reviews, we carried out a review of files from firms who advised BSPS members between 1 March 2017 and 31 March 2018 to see whether this advice complied with the rules in place at the time.

In total, there were 365 files in our sample from 89 firms. Using the framework advised by our external statistician we estimate, across the market, that only 41% of recommendations were suitable, in 14% of cases the suitability of recommendations was unclear due to a material information gap, and in 46% of cases the recommendation was unsuitable.

At 46%, the proportion of advice that was unsuitable for BSPS customers is significantly higher than we have found in other contexts. Separately we reviewed higher-risk firms providing non-BSPS advice. In those cases, 17% of advice was unsuitable. There is further information about this work in our consultation paper into a redress scheme for BSPS ([CP 22/6](#))¹.

b. Update on enforcement

We have shared an update with the Committee about our enforcement work on BSPS as part of our formal response.

It is important to emphasise that we follow the statutory process in the Financial Services and Markets Act 2000 (FSMA), which sets out what we can publish, in which circumstances and the factors that we should take into account when making a decision about what and when to publish. Notices published through that process are a key way we explain our enforcement action to the public.

Cases before the Upper Tribunal and Courts are a matter of public record, and there are two enforcement matters relating to BSPS currently being litigated. We commenced High Court proceedings against Paul Steel & Jacqueline Foster of Estate Matters Financial Limited (EMF) in Feb 2021. We also published a Decision Notice in relation to Geoffrey Armin of Retirement and Pension Planning Services Limited (RPPS, in liquidation) in August 2021. Mr Armin has referred the Decision Notice to the Upper Tribunal and so our findings are provisional.

The investigations relating to BSPS represent only part of the enforcement work carried out by the FCA. In the year to March 2022, we imposed financial penalties of £313m and started prosecutions alleging insider dealing, investment fraud and breaches of money laundering regulations.

¹ <https://www.fca.org.uk/publication/consultation/cp22-6.pdf>

c. The BPS redress scheme

Implementation of a consumer redress scheme for BPS

Under the proposed scheme, firms will be required to review the advice they gave. If the advice is identified as unsuitable and resulted in a financial loss, they would need to calculate the redress payable and provide compensation.

We are proposing detailed reporting requirements for firms and attestations from senior individuals confirming that steps have been carried out in compliance with the scheme rules. We have recently consulted on further plans that would see us receive the details of any consumers who are told by firms the advice they received was suitable. This would allow us to contact the consumer and inform them of the option of referring their complaint to the Financial Ombudsman Service (FOS) for an independent review. These safeguards will help to ensure that firms comply with the rules and that consumers can be confident in the outcomes.

Our consultation paper on the proposed BPS consumer redress scheme closed on 30 June and we are currently analysing the responses we received. We intend to publish a policy statement confirming next steps by the end of the year. If we decide to implement a scheme, we expect it will come into force in early 2023. We expect that the vast majority of consumers who are eligible would receive compensation later in 2023 or in early 2024.

If we decide to implement a scheme, we expect firms to take steps to identify and prioritise consumers that may be in vulnerable circumstances or who may need fast access to redress, for example if they are in or nearing retirement.

Redress calculation methodology

The redress calculation methodology will result in differing amounts of redress, depending on when the calculation is carried out. This is because it is designed to respond to changes in the economy by using assumptions based on financial markets' expectations of economic factors such as inflation and investment returns. This is common actuarial practice. We expect firms to update the economic assumptions used to place a value on the consumer's DB benefits, such as the pre- and post-retirement discount rates, at least every quarter. We also expect firms to issue redress offers promptly to reduce the impact of market movements in the period between calculation and settlement. To further reduce the impact of market movements on calculations, in our recently published Consultation Paper 22/15 ([CP 22/15](#))², we have proposed more frequent (i.e. monthly) assumption updates. We have also proposed that firms issue redress offers to the consumer within three months of valuing their DB benefits.

For example, redress will tend to reduce when – as is currently the case – gilt yields rise. This is because the post-retirement discount rate, which is used to price an annuity to replicate the consumer's DB benefits at an appropriate date, is based on gilt yields. Because rising gilt yields reduce the cost of an annuity, the amount of redress consumers need to make up any shortfall between the value of their DB benefits and the value of their DC pension will – other things being equal – be less.

Additionally, inflation – the likely driver of higher interest rates, which then tends to result in higher gilt yields – affects aspects of the redress calculation. This includes the level of inflationary pension increases which would have been payable in the DB scheme (which are subject to caps and floors). Future inflationary expectations are also a factor in deriving the pre-retirement discount rate. This is used to discount the estimated sum needed at retirement to today's money,

² <https://www.fca.org.uk/publication/consultation/cp22-15.pdf>

and represents the returns that may be achievable by a cautious investor over the period to their retirement.

FSCS Compensation Limits

If a redress scheme is implemented the FSCS will assess claims against any firms that go out of business that are within the scope of the scheme and calculate redress in line with the scheme rules and will pay compensation up to the limit of £85,000 per person (or £50,000 where firms failed before 1 April 2019). The FSCS compensation limits therefore apply to customers of firms that have failed before and after any consumer redress scheme is implemented._

The FSCS's operating costs and compensation payments are funded by levies on financial services firms. FSCS compensation limits were last reviewed between 2016 and 2018. In light of feedback received, we increased the limit from £50,000 to £85,000 for certain categories of claim for firms declared in default by the FSCS from April 2019 onwards. This limit was considered to represent an appropriate balance between consumer protection and the cost to industry levy payers, which is ultimately passed to consumers.

Last December, we published the [Compensation Framework Review discussion paper³](#). In this paper, we explained that we thought that current compensation limits are set at an adequate level to cover a reasonable proportion of customers' claims but that we were interested in hearing views from stakeholders on whether changes should be made. We are currently considering next steps, including whether it might be appropriate to reconsider whether the current limits continue to provide an appropriate level of consumer protection. We will publish a Feedback Statement later this year.

d. Preventing similar cases in the future

Work with partners

We accept that in the summer of 2017 there was limited information sharing between pensions regulators and this affected the focus of all organisations on the position of steelworkers who were seeking to transfer out of the DB scheme.

As the Committee are aware, the Rookes review commissioned by tPR and published in January 2019 reviewed the collaboration between pensions regulators around BPS and made recommendations to improve the system. We and tPR agreed to the recommendations and published a "Joint Protocol" by way of response which sets a framework for increased communication and information sharing between FCA, tPR, the Pension Protection Fund (PPF) and the Money and Pensions Service (MaPS).

This framework now facilitates close collaboration between the organisations through regular working level meetings and a quarterly senior Steering Group. Since being established the Joint Protocol has improved intelligence sharing, facilitated joint working and early intervention in relation to the risks identified from our improved interaction. For example in 2019 we introduced the "transfer letter" for trustees and administrators to share with members considering a transfer so to provide clear information on the risks and sources of impartial advice to support the member. This is updated when required and widely used by trustees.

During the pandemic we were concerned about an increased risk of transfers that could be due to the economic impacts of the pandemic. With tPR we sent a letter to all trustees of DB schemes providing the cash equivalent transfer value (CETV) letter and encouraging those who had not

³ <https://www.fca.org.uk/publications/discussion-papers/dp21-5-compensation-framework-review>

yet used it to take it up; requesting trustees informed tPR or FCA if any spikes or unusual transfer activity was noted. In addition, we reached out to the 8 largest providers of DB transfer advice to understand the market impact. Our improved interaction and intelligence sharing between organisations has resulted in action following receipt of intelligence about potential increased transfer requests. For example:

- Rolls Royce scheme - <https://www.fca.org.uk/news/statements/fca-tpr-and-maps-joint-statement-rolls-royce-defined-benefit-pensions-scheme>
- Old BSPS scheme - <https://www.fca.org.uk/news/statements/fca-tpr-moneyhelper-joint-statement-old-british-steel-pension-scheme>
- P&O scheme - <https://www.fca.org.uk/news/statements/fca-tpr-and-maps-joint-statement-po-defined-benefit-pension-schemes>

Operational and regulatory changes

As the NAO observes, following an initial period of working with industry and pension members to try and contain the most immediate harm in 2017 and early 2018, we recognised that we needed to change our approach to regulating the pension transfer advice market, making changes to our internal processes in response to the BSPS case. These operational and regulatory changes are set out in the NAO report (paragraph 2.20). Our six-monthly data return (collected from firms) also enables us to proactively monitor trends and engage with firms which are active in the DB market.

We are continuing to build on upon our progress, which will mean we are even better equipped to anticipate harm and protect consumers. Our aim is to define and codify behaviors and events which we know are likely to end in consumer harm or markets failing to function. Doing this will allow us to intervene earlier - before consumers and markets suffer loss and harm.

e. Engagement with BSPS members

Working closely with the regulatory family, we have engaged extensively with former BSPS members. We wrote directly to BSPS members in 2018, 2019 and 2020, ran local events with BSPS members in 2017, 2019 and 2021, and communicated through trusted intermediaries (including steelworkers, MPs and unions), to raise awareness of their right to complain (or claim). We have also provided tools, such as our advice checker, to make it easier to do so. This engagement has been constructive. For example, we saw 272 former BSPS members at our face-to-face events in South Wales and Scunthorpe in late 2021. 86% of attendees surveyed said they were now clearer about their next steps and following the events we saw an uplift in FOS complaints. This summer we have discussed our redress consultation directly with 50 BSPS members and over 200 firms.

f. Further work on DB transfers

The suitability of advice in the DB pension transfer market has been a focus for the FCA from 2015, following the introduction of the Pension Freedoms. We have undertaken extensive work to address potential harm to consumers, including:

- strengthening our rules on pension transfers, including banning the practice of contingent charging (where a firm was only paid if a transfer went ahead)

- issuing a market wide data request into DB transfer advice at the end of 2018, covering advice between April 2015 and September 2018
- reviewing files from 85 firms together responsible for advice on 43% of DB transfers
- stopping firms providing further advice where we found serious concerns with their advice process, and obtaining redress for consumers through past business reviews where appropriate, with over £27mn having been paid to 166 consumers in redress to date
- writing to 1,649 firms in Autumn 2019 providing individualised feedback on their data submissions, following which 402 firms chose to vary their permissions, meaning they will not advise on DB transfers in future.

We consider the factors leading to the high level of harm associated with the BSPS case do not apply to other schemes. The restructuring of the BSPS scheme led to all members having to make a decision about their pension, there was significant media coverage of the scheme's financial difficulties, and uncertainty regarding whether BSPS2 would proceed. Members may have felt distrustful of the scheme and its future, which may have influenced their own views on the merits of transferring out. Since 2015 we have not seen any other scheme where these circumstances applied, and we have not found any other scheme where the level of unsuitable advice was as high as that for BSPS. As I said in my response to recommendation 1, when we have assessed advice on non-BSPS transfers from pensions schemes provided by high-risk firms we found a much lower unsuitability rate of 17% compared with 46% for BSPS.

3. Transformation

a. Data strategy

Last year I said that I wanted to see the FCA transform as a regulator, to be more innovative, assertive and adaptive. As our transformation programme continues, a key area of investment is in our capabilities to become a data-led regulator. In our formal response to the Committee, we refer to our commitment of £120 million over three years to deliver our Data Strategy. This aims to make us more effective by harnessing data, converting it into actionable intelligence, and improving our real time understanding of what is currently happening and, crucially, of emerging risks.

b. Processes

I welcome the report's conclusion that we acted fairly and swiftly to deal with the impact of COVID-19 on consumers of financial services.

Alongside making improvements to our technology and how we use data, our Transformation Programme also involves reforming our decision-making and governance so we can respond more quickly to prevent or address consumer harm.

As part of this work, we have reviewed how our Regulatory Decisions Committee (RDC) functions. The RDC is a final decision maker on contested enforcement, supervisory and authorisation interventions. Following this review, we are moving some decision making from RDC to the FCA's senior managers.⁴ We have also recently made changes to our rules to streamline decision making processes for the regulation of claims management companies,

⁴ <https://www.fca.org.uk/publication/policy/ps21-16.pdf>

enabling us to be more assertive and act more quickly where firms and individuals do not meet the required standards.

c. Consumer investment strategy and PII work

We recognise the challenge from the Committee on professional indemnity insurance (PII), particularly in relation to the availability and pricing of cover, and we continue to actively review how our policy and industry communications may affect this. Recently we have gathered information from insurers to assess the extent of premium increases in PII over recent years, the use of exclusions and excesses by providers and the impact on the cover available. This evidence will inform our supervision of the PII market going forward. We will be in the position to share our conclusions and next steps on this front in October 2022. Additionally, we are currently undertaking qualitative analysis on the potential impact of our proposals for BSPS redress specifically on the PII market. Our objective is to ensure that the PII market is working well, while recognising that the level of cover offered is a commercial decision for insurance providers.

The vision set out in our [consumer investments strategy](https://www.fca.org.uk/publications/corporate-documents/consumer-investments-strategy)⁵ (published in September 2021) is for consumers to be able to invest with confidence, understanding the risks they are taking, and the regulatory protections provided. We have set ourselves four ambitious outcomes: to reduce the number of consumers who could benefit from investing in the mainstream market but who are missing out; to reduce the number of consumers investing in high-risk products when this does not suit their circumstances; to reduce the amount of money consumers lose to investment scams; and to stabilise and over time reduce FSCS compensation paid out for the Life Distribution and Investment Intermediation and the Investment Provision funding classes. This strategy allows us to work across teams and departments to drive better consumer outcomes. We also consider emerging risks, such as how the cost-of living crisis might impact consumers in this market. The consumer investments strategy is a three-year strategy and we use data to track progress towards our goals (the same approach used in our organisational strategy published earlier this year)

Since publishing the Consumer Investments Strategy, we have been delivering changes which will make a difference for consumers in this market. For example, we recently published our Policy Statement on strengthening our financial promotion rules for high-risk investments and firms approving financial promotions. We also launched our InvestSmart consumer education campaign (with a budget of £11.5 million over five years), to help a new audience of investors make better-informed investment decisions and understand the risks they are taking. Our proposed consumer redress scheme for British Steel Pension Scheme members is also a significant part of this Strategy.

Our organisational strategy sets out our expectations for financial services over the next three years and how we will measure our performance to improve, adapt and deliver in the interests of consumers, markets, and the economy. Setting higher standards and putting consumers' needs first is central to our strategy. In July we published our final rules and guidance for a new Consumer Duty, which will set higher and clearer standards of consumer protection across financial services and require firms to put their customers' needs first. We want to see a higher level of consumer protection in retail financial markets, where firms compete vigorously in consumers' interests. This is particularly important as consumers face increasing pressures, including those relating to the cost of living.

⁵ <https://www.fca.org.uk/publications/corporate-documents/consumer-investments-strategy>

d. Consumer engagement, engagement with consumer groups and identification of risk

In section 2 of this letter, I spoke about our engagement with BSPS members. More widely, we use a range of methods to engage with consumers and understand their experience of financial services, their needs and the potential for harm within the wider economic context:

- The FCA consumer partnerships network provides insight to inform our policy development and build relationships and understanding with consumer groups. Members include MoneySavingExpert and Citizens Advice on the national side, as well as more issue focused organisations such as MacMillan Cancer research and Scope and debt charities such as Stepchange and Money Advice Trust.
- FCA's Executive committee carries out a regular programme of visits to towns and cities across the UK to engage directly with consumer and community groups and their clients, firms, institutions such as universities and schools and local authorities, to understand the experience of financial services on the ground and ensure we keep in touch with the diverse experience of financial services and local economies for whom we regulate.
- Our devolved nations team works with consumer and community organisations in the devolved nations and with parliamentarians and national institutions such as Consumer Scotland to understand the experience and perspective of consumers across the UK.
- We refer to our Financial Lives Survey in our formal response. Financial Lives provides data on the characteristics of vulnerability including poor health, a life events, low resilience or low capability. It allows us to find correlation with income levels, social deprivation scores, and personal characteristics like gender or ethnicity as well as product holdings and covers both qualitative and quantitative responses. We also carry out bespoke market research on the consumer experience of specific products and markets.
- Each year we survey a sample of our stakeholders to understand how they perceive our activity and to assess the effectiveness of our engagement strategies. This helps us to identify any issues and take action accordingly.
- Our Supervision hub also provides a channel for consumers to come to us direct to check who is authorised, how to avoid scams, how to complain about a firm and how to report an issue.
- As the Committee is aware, the Financial Services Consumer Panel provides an independent forum for challenge and discussion of FCA developing policy by formally appointed consumer representative experts to ensure the consumer perspective is considered.

4. The FCA position on DB transfers

The Committee's report concludes that in response to the 2015 Pension Schemes Act, 'the FCA provided guidance that advisers should assume that, in most cases, a transfer will be unsuitable, creating confusion among advice firms'. This is expanded upon in the section of the report entitled 'Confused regulatory expectations'. Whilst we recognise some of the points made in this section, we do not agree that there was any lack of clarity on our expectations of those providing advice on potential DB transfers.

The report observes that: 'In direct response to the 2015 Act, the FCA announced a new starting position for advisers who should assume that in most cases a transfer will be unsuitable.' However, our starting assumption - that when an adviser is assessing the suitability of a pension transfer it will not be suitable, unless it can be shown to be in the client's best interests - has been in our rules since 2007. Advisers should have been fully aware of this starting assumption. We also had pre-existing rules and guidance on advice and specific qualification requirements for those involved in giving DB transfer advice, prior to the pension freedoms.

The papers that we published following the announcement of the pension freedoms in 2014 set out our expectations regarding how our existing rules and guidance operated in the new environment. This provided additional clarification on what we expected from provider and advice firms when dealing with consumers who may be affected by the reforms. We made clear that: 'Assessing the suitability of this type of transfer is not a trivial exercise. It will require a comparison between the DB guarantees and benefits the client would be giving up, relative to the resultant DC benefits, taking into account the transfer value offered by the trustees of the DB scheme and in the context of the client's overall financial situation and future needs.' We also observed that consumers were likely to be heavily reliant on advice due to their own lack of knowledge, including their potential inability to understand the implications of losing the underlying guarantees provided by a DB scheme.

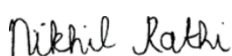
Using evidence gathered by our substantial programme of ongoing supervision, we undertook targeted policy work to raise standards in key areas. This included several consultations setting out the process we expect firms to follow when giving pension transfer advice, as well as reviews of relevant qualification and exam standards. These consultations from 2017-2019 preceded a comprehensive guidance publication in March 2021 which industry considered was a useful tool in raising standards, based on our subsequent research.

For example, we made rules on how firms should assess consumers' preferences for different types of pension benefits and how to compare the benefits and options in a DB scheme with those in a DC scheme. In June 2017, we consulted on amending the 'starting assumption' to one which expected firms to have regard to the likelihood that it will be in the best interests of the majority of consumers to retain their DB benefits. This consultation was clear that this was not a softening of our position: for the majority of people a transfer will be unsuitable.

We did not proceed with that change because of the growing volume of evidence about the proportion of unsuitable advice and because we wanted our position to continue to be expressed for each individual case considered by firms, rather than across all cases. We also published comprehensive guidance in 2021 on how to give suitable transfer advice which, like our other policy work, was informed by the advice we had seen.

I hope that this is helpful.

Yours sincerely,



Nikhil Rathi
Chief Executive