Incentive Exercises

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Agenda

A. Incentive Exercises – overview
B. The Code of Practice
C. What is happening today?
D. Trivial commutation
E. Will the Code need to change?
F. Questions

Incentive Exercises - Overview

- What?
  - Individuals encouraged to give up/vary/transfer etc. their pension rights (ETVs, PIEs, etc.).
- Why?
  - Part of the wider risk-management landscape.
- Member protection
  - Imbalance between employer/trustees and member.
  - Code of Practice.

Incentive Exercises – The Code of Practice

- Code of Practice introduced in June 2012.
- Intention of the Code to balance the use of incentive exercises as a legitimate tool to help employers manage risk against the need to provide members with an appropriate level of protection.
- Code is voluntary
  - Pensions Ombudsman/Financial Ombudsman Service to have regard to the Code.
  - Behavioural change

Incentive exercises – The Code of Practice

- An invitation or inducement (offer) to a member to change their existing defined benefits in a UK registered pension scheme, which meets both of the following tests:
  - The offer is intended to reduce risk or cost for the pension scheme or sponsor(s); <u>and</u>
  - The offer is not ordinarily available to members of the pension scheme.
- Either
  - **Transfer Exercises** involving transfers out of a defined benefit scheme. These include Enhanced Transfer Value (ETV) exercises and Total Pension Increase Exchange (TPIE) exercises (and variants); or
  - **Modification Exercises** within the DB scheme. These include Pension Increase Exchange (PIE) exercises.
- A legitimate tool for managing DB liabilities

The seven principles

1. No cash incentives contingent on accepting the offer
2. Transfers = Advice to be provided: Modification Exercises = either Advice <u>or</u> Guidance if a Value Requirement met
3. Communications with members should be fair, clear, unbiased and straightforward.
4. Records should be retained by the various parties involved. Insistent Customers should be reported to the other parties.
5. Exercises should allow sufficient time for members to make up their mind with no undue pressure applied.
6. Exclude over age 80 on an “opt-in” basis – subject to adviser Vulnerable Client policy.
7. All to be aware of their roles and responsibilities and act in good faith.

What does the Code cover?

In scope

- Enhanced Transfer Values
- Pension Increase Exchange
- Other bulk transfer or modification offers
- Variations on these, e.g.
  - ETV to occupational scheme
  - Standard CETVs but with similar comms / advice
  - Transfer to immediately vesting policy
  - TPIE (FRO, FaR etc)
  - Enhanced ER

Out of scope

- DC benefits
- Unregistered schemes
- Benefit changes for future service
- Commutation at retirement
- Member initiated "normal" transfers
- **BAU options**, e.g. PIE at retirement
- Benefit changes impacting past service (i.e. salary capping)

What’s happening today?

- Few ETV exercises
- Mainly BAU PIE and TPIE (FaR, FRO)
  - Advice is the norm
- Trivial Commutation
- Better member engagement
- Better member communications
- Real focus on compliance
  - Lots of questions of interpretation
- Freedom and choice – are incentive exercises dead?

Trivial Commutation – well you did ask….

- Budget changes to trivial commutation increased the impact of TC
- Created questions, we had to answer
- Trivial commutation can be an incentive exercise
- <u>Not a change to the Code</u>
- Trivial commutation is a modification, so Guidance applies
- Information on available option is not an incentive exercise
- Typical exercises will be BAU, therefore not caught by Code
  - » but principles should apply
  - » Consider vulnerable members

Will the Code need to change?

- Almost certainly
- Review of the Code begins 5th May
- Consult with Industry Forum in summer 2015
  - » Effectiveness of the Code?
  - » DB to DC transfers?
  - » Definitions?
  - » Code becomes statutory?
  - » Code becomes focused on modifications?
    - BAU PIE, BAU trivial commutation
  - » Code falls away?

QUESTIONS?

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