

INCENTIVE EXERCISES FOR PENSIONS

A CODE OF GOOD PRACTICE

VERSION 2 - JANUARY 2016

www.incentiveexercises.org.uk

Disclaimer

The Code is for guidance only and does not purport to constitute legal advice. The Code is not exhaustive and nothing in the Code can be relied upon as evidence of compliance with any other legal or regulatory requirement. The Code relates to circumstances prevailing at the date of its original publication and may not have been updated to reflect subsequent developments.

Following the Code does not relieve a party of its legal or regulatory obligations and following the Code may not prevent a claim being brought against a party.

About the authors

This voluntary Code of Good Practice has been produced by the Incentive Exercises Monitoring Board, having consulted with the Incentive Exercises Industry Forum.

Incentive Exercises Monitoring Board

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|--|--|
| The Pensions Administration Association | Margaret Snowden OBE* (Chair) |
| The Association of British Insurers | Rob Yuille |
| Association of Consulting Actuaries | Andrew Vaughan (to 31.12.15) Bob Scott/David Fairs (from 1.11.16) |
| Association of Professional Financial Advisers | Chris Hannant |
| Association of Pension Lawyers | Anna Rogers* (to 31.12.15) Rosalind Connor* (from 1.1.16) |
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| The Confederation of British Industry | Dom Frost |
| Department for Work and Pensions | Gareth Thomas |
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The principles in this Code of Good Practice are supported by the following organisations:

Association of Consulting Actuaries

Association of Professional Financial Advisers

Department for Work and Pensions

Financial Reporting Council

The Institute and Faculty of Actuaries

The Association of British Insurers

The Confederation of British Industry

The Engineering Employers Federation

The Financial Conduct Authority

The Pensions and Lifetime Savings Association

The Pensions Administration Standards Association

The Pensions Advisory Service

The Pensions Regulator

The Society of Pension Professionals

A full list of supporters is shown on our website

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Forewords

The Baroness Altmann CBE

Minister of State for Pensions

The area of Incentive Exercises is an important one for pension schemes and their members. They can involve risks for all parties. For members, the risk is that they may make the wrong choices and lose valuable benefits. For consultants, employers, advisers and insurers, the risk is that some of the scheme members who accept an incentive offer may in the future feel they were misled to transfer or modify their pensions in a way that turned out to be not suited to their needs. For these reasons, it is important that all industry stakeholders understand their responsibilities and operate to the highest standard of good professional practice.

Following the publication of the Industry Code of Good Practice for Incentive Exercises in June 2012, I have been pleased to hear that the good standards set out have been embraced by so many advisers and employers alike in the period since its launch. This should lead to better outcomes for those offered incentivised transfers or modifications. It is very encouraging that the various stakeholders have recognised the benefit of good practice without the need for it to be imposed through legislation. I certainly prefer to avoid legislation and additional regulations wherever possible, but we will act if we see members' interests severely jeopardised.

The Code set challenging standards that have certainly contributed to improving Incentive Exercises, but the authors of the Code were set a further challenge to continue to monitor the Code's effectiveness and recommend to me any changes, legislative or otherwise, that they felt necessary after a period of three years. A Monitoring Board was set up to do this and to liaise with my Department throughout. Within that three-year period, there was significant change in the market with the introduction of Freedom and Choice in Pensions and the Monitoring Board considered this, and other changes, alongside their review of practice. This coupled with funding issues might increase transfer activity or benefit modification exercises, so it is increasingly vital that we ensure good practice.

It is more important than ever that members (and their partners) have independent information, guidance and advice where it is required, before giving up valuable guaranteed pension benefits without fully realising the implications.

I would like to thank the members of the Incentive Exercises Monitoring Board for their work in reviewing and updating the Code in the light of changes in regulations and market practices, and to the wider industry for their support and input to the review via the Incentive Exercises Forum.

I commend the revised Code to you and urge everyone to follow it.

Margaret Snowdon OBE, Chairman of the Incentive Exercises Monitoring Board

In June 2012, the Code of Good Practice on Incentive Exercises was launched, with the background concern that a voluntary code, written by and for the industry, may not be enough to address the impact of poor practice on member outcomes. The group that I was fortunate to chair was then tasked with monitoring the effectiveness of the Code over a three-year period and with recommending action to government, whether to continue the Code unchanged, amend it to address the evolving market or to set it aside in favour of legislation. The Incentive Exercises Monitoring Board was formed and created a Technical Group from within its members. How the industry adopted the Code would determine the future direction.

It was therefore hugely satisfying to see the Code well received by the industry. The interest shown in understanding how the Code should be applied in different circumstances through attendance at IE Forums and questions asked of members of the Board and through our website, has been encouraging. It is clear that trustees and employers want to comply with the Code, despite its voluntary nature, and we believe that the Code has resulted in better behaviours, better run exercises and less risk of members being disadvantaged.

Reviewing and monitoring the Code has not been simple. Evidence of compliance with a voluntary Code is hard to come by, but by working with the Pensions Regulator, we were able to obtain statistical information on schemes that had undertaken incentive exercises or were considering them and carry out an independent survey of a representative sample. A number of stakeholders were interviewed about their knowledge of the Code, how they had taken the Code into account and how it had influenced the exercise itself. The results supported our anecdotal evidence of compliance and also showed the importance of collaboration between advisers, employers and trustees to the conduct of an exercise.

The review process was carried out in the main by the small group of dedicated experts, the Technical Group of the IE Monitoring Board and through consultation with the IE Forum. What we realised early on was that the Principles of the Code resulted in positive behaviours and that change or withdrawal of those Principles could risk a decline in good practice. We therefore saw no need to change the Principles themselves, but to update the body of the Code to reflect the changing environment. We considered reviewing the Practitioner Notes that supported the Code, but decided against this, deciding instead to introduce Boundary Examples to help illustrate how the Code could and should be applied in practice. We hope the industry finds these examples useful. The Practitioner Notes will be archived but remain available to those who wish to refer to them.

We did not always agree, given our cross section of interests from the breadth of the industry, but we were able to compromise where necessary to deliver a strong message on good practice.

One area we grappled with was the matter of Wind Up Lump Sums (WULS). We maintain the position that WULS sit outside of the Code, but can foresee the growth of WULS being used as Incentive Exercises. *We believe this is an important development and therefore state that we will consult the industry during 2016 on whether or not we should be specific about which types of WULS should fall within the Code and prepare some additional Boundary Examples to support this.*

I am grateful to the representatives of organisations from across the industry, who freely gave their time and expertise to review and produce this updated version of the Code of Good Practice and to their employers who made it possible. The members of the IE Monitoring Board (IEMB) are shown on page 2.

Introduction

Status

This Code is a voluntary Code that sets out good practice for **Incentive Exercises**.

Whilst the Code is voluntary, the Incentive Exercise Monitoring Board continues to expect that all **Incentive Exercises** will follow the spirit and principles of the Code. The Board does not expect employers, trustees or their advisers to look for creative ways to work around the Code.

Whilst the Code is not a statutory code, and so would not be considered by the courts in relation to any matters considered by the court, the Pensions Ombudsman and the Financial Ombudsman Service will have regard to the Code, where appropriate, when dealing with a complaint involving an **Incentive Exercise**.

The Code does not replace or over-ride existing requirements and guidance on **Incentive Exercises**. In particular, the Code deliberately does not address the legal and other responsibilities of the different parties, who will need to consider these in addition. The FCA's Conduct of Business Sourcebook (and other relevant rules) continues to apply to FCA regulated activity.

The Pensions Regulator supports the voluntary Code.

The party initiating the offer, typically the employer, but sometimes the trustees or another party, is responsible for following the Code and seeking to ensure that other parties follow the Code.

Commencement date for version 2 of the Code

Version 2 of the Code applies to all circumstances where an offer is made available to a member after the date of publication of the Code.

Where at the date of publication of version 2 of the Code an offer has already been made to a member in writing, the exercise is subject to version 1 of the Code (June 2012).

Scope

For the purposes of the Code, an **Incentive Exercise** is an invitation or inducement (generally referred to as an “offer” throughout this Code) provided to a member to change the form of their accrued defined benefit rights in a UK registered pension scheme, which meets both of the following tests:

- One objective of providing the invitation or inducement is to reduce risk or cost for the pension scheme or sponsor(s); and
- The invitation or inducement is not ordinarily available to members of the pension scheme.

The Code broadly covers two types of **Incentive Exercise**:

- **Transfer Exercises** involving transfers out of a defined benefit scheme. These include **Enhanced Transfer Value** exercises and **Total Pension Increase Exchange** exercises (and variants thereof); and
- **Modification Exercises** within the DB scheme. These include **Full Commutation** exercises and **Pension Increase Exchange** exercises.

These terms are referred to in the Code when differentiating between types of exercise. Examples of transactions that are out of scope are provided in the Supporting Information on page 28.

The Code does not apply to the introduction of new benefit options in pension scheme rules that will subsequently be made ordinarily available to members. For example, the Code does not apply to the introduction of a pension increase exchange offer that is subsequently made available to members as a matter of course as they approach retirement. However, the Code would apply if existing pensioners were made a similar offer. Employers, trustees and advisers are encouraged to consider the extent to which it may be appropriate and helpful to members to apply some or all of the Code both at the time of introducing the option in the rules and at each time when the option is subsequently offered to a member.

Purpose

The key objectives of the Code are to help ensure that all **Incentive Exercises** enable members to make informed decisions and better choices, whilst permitting exercises and options to be offered in a responsible manner, and that exercises are:

- carried out fairly and transparently;
- communicated in a balanced way and in terms that members can understand;
- available with appropriate financial advice (or in some limited circumstances, financial guidance) that is paid for by the party initiating the exercise (often the employer, but sometimes another party eg trustees);
- able to achieve high levels of member engagement; and
- provided with access to an independent complaints and compensation process.

Glossary

A Glossary of Definitions is included in the Supporting Information on page 23 to describe what is meant by various terms. These terms are highlighted in bold in this Code.

Boundary examples and other examples (January 2016)

The Board is publishing various examples alongside version 2 of the Code. These examples do not form part of the Code.

In any particular proposed situation, users of the Code will need to consider and reflect the full facts and circumstances of the situation when considering the application of the Code. The examples are intended to be a guide in the areas they cover, but they are not hard and fast rules. In particular, it would not be within the spirit of the Code to “cherry-pick” the facts of a situation to fit a particular example in order to conclude that an exercise is not within the scope of the Code, when other facts demonstrate otherwise.

Practitioners’ Notes (June 2012)

Practitioners’ Notes were published alongside version 1 of the Code. The Practitioners’ Notes are not part of the Code.

The Practitioners’ Notes have not been reviewed as part of the production of version 2 of the Code and are not being maintained in the future. The original Practitioners’ Notes remain available to users to the Code and might continue to be helpful in some cases.

Any questions or comments on the Code should be emailed to:

info@incentiveexercises.org.uk

The Principles for Following the Code

The Code is made up of 7 principles supplemented by information on how to apply those principles.

The Principles

To follow the Code there are 7 principles that should be followed. These are:

1. No **Cash Incentives** should be offered that are contingent on the member's decision to accept the offer.
2. For **Transfer Exercises**, **Advice** should be provided to the member. For **Modification Exercises**, either:
 - a. **Advice** should be provided to the member, or;
 - b. A **Value Requirement** should be complied with and **IE Guidance** should be provided to the member.A **Proportionality Threshold** changes this requirement for smaller pensions.
3. **Communications** with members should be fair, clear, unbiased and straightforward.
4. Records should be retained by the various parties involved in an exercise so that an audit trail is maintained that can be examined in future. When providing **Advice**, the **Member Adviser** should record and report on **Insistent Customers** to the other parties.
5. Exercises should allow sufficient time for members to make up their mind with no undue pressure applied.
6. **Incentive Exercises** should only be offered to members who are over age 80 on an "opt-in" basis. **Member Advisers** should adhere to a **Vulnerable Client** policy when providing **Advice**.
7. All parties involved in an **Incentive Exercise** should ensure that they are aware of their roles and responsibilities and act in good faith in the areas over which they have direct control.

Steps that should be taken in order to apply the principles are set out below.

How to apply the Principles

PRINCIPLE 1: No Cash Incentives.

Cash Incentives include anything which has a value to the member that is not a pension benefit arising from a UK registered pension scheme. This includes payments in cash, goods and services.

How to apply this principle

- To follow the Code, there are no circumstances in which a **Cash Incentive** can be offered to a member where the incentive is only available if the member accepts the **Incentive Exercise** offer.
- Cash payments designed to encourage members to engage with the process and that are not on the condition that the offer is accepted (for example incentives to encourage members to engage with **Member Advisers** before making a decision on whether or not to accept an offer) are permissible. The expectation is that these incentives would usually be of relatively small material value (for example £100 retail vouchers offered and paid to members who actively participate in the advisory process, regardless of their decision on the offer). It must be made clear to members that accepting any incentive to engage with **Member Advisers** does not put them under any pressure to accept the offer.
- Members over age 55 (or in certain circumstances age 50) may be entitled to cash from their pension scheme. For the avoidance of doubt, this principle of the Code does not restrict exercises that provide opportunities for members to access pension cash at retirement in the normal way.
- For **Modification Exercises**, the offer must not include a significant immediate lump sum. For example, backdating a **Pension Increase Exchange** for a short period for the specific objective of administrative simplicity (usually no more than a few months) is acceptable but back-dating with the objective of creating an additional **Cash Incentive** to accept the offer would not be following the Code.

PRINCIPLE 2: For **Transfer Exercises, Advice** is provided. For **Modification Exercises, either Advice is provided or a Value Requirement** is complied with and **IE Guidance** provided. This principle is amended where the **Proportionality Threshold** applies.

How to apply this principle

Section A below is on how to meet the **Value Requirement**. Section B is on how to provide **Advice** or **IE Guidance**. Section C is on the application of the **Proportionality Threshold**.

A. Meeting the Value Requirement

For a **Modification Exercise** to meet the **Value Requirement**:

- a **Balanced Deal Calculation** must be undertaken and
- the **Balanced Deal Percentage** must be 100% or more.

The **Balanced Deal Calculation** is a calculation of the expected present value of members' additional benefits to be awarded following the **Modification Exercise** (assuming 100% take-up) as a percentage of the expected present value of the benefits being given up, to arrive at the **Balanced Deal Percentage**. It is an aggregate calculation for all members who are informed that the **Modification Exercise** offer is open to them (including any members who are informed of the exercise on an "opt-in" only basis). The **Balanced Deal Calculation** will result in a single **Balanced Deal Percentage** figure for all members.

For example, with a **Pension Increase Exchange** exercise the **Balanced Deal Percentage** is:

Present value of the additional pension following the **Pension Increase Exchange**

Divided by

Present value of the pension increases given up as part of the **Pension Increase Exchange**

This calculation must be undertaken using the framework for actuarial equivalence tests under section 67 of the Pensions Act 1995 (the subsisting rights provisions). This requires a comparison of the actuarial value of members' accrued rights on an actuarial basis consistent with that used to calculate cash equivalent transfer values (CETVs) from the pension scheme. The **Balanced Deal Calculation** must ignore any reduction in CETVs arising from underfunding.

Whilst the Code does not require each member's individual balanced deal calculation to exceed 100% in order for the **Balanced Deal Percentage** to be in excess of 100%, approaches to designing **Modification Exercises** that leave some members materially below 100% of the Balanced Deal and others materially above should be avoided.

It is recognised that CETV bases change following changes in market conditions, typically monthly or quarterly. A pragmatic approach to addressing these timing issues when assessing the **Balanced Deal Percentage** is acceptable, in particular:

- Calculations of the **Balanced Deal Percentage** may be completed based on market conditions (and a CETV basis) as at a date within 3 months prior to the date the offer is issued to members.
- Once the offer has been issued to members, and the **Balanced Deal Percentage** has been communicated to members, the **Balanced Deal Percentage** and the communications do not need to be revisited for the period of an offer (up to 6 months).

The **Balanced Deal Percentage** must be communicated prominently to members (see how to apply principle 3).

B. Providing Advice and IE Guidance

Where **Advice** is provided, key points on how this should be carried out are described below. The table further below shows which points apply where **IE Guidance** is provided, and how this differs from the DC Guidance Guarantee offered by Pension Wise.

1. Impartial financial **Advice** by a **Member Adviser** that can show independence from the party making the offer should be made readily accessible to all members who are part of the offer, and promoted clearly. Where existing employer or trustee advisers play a role in **Advice** to members, they will need to ensure that an appropriate conflict of interest policy is established and relevant disclosures are made to all parties.
2. The **Member Adviser** should be suitably qualified and experienced. For advice that is regulated by the Financial Conduct Authority (FCA), the **Member Adviser** will need to comply with the FCA's requirements. For other **Advice**, the **Member Adviser** will need to demonstrate suitable qualifications and experience, which should be disclosed to the member.
3. The contract between the **Member Adviser** and the member should make clear that the member has legal recourse to the **Member Adviser** if necessary in the future; should clearly state the complaints process; should clearly state any limitations in liability (which should be reasonable) and should refer to any relevant Professional Indemnity (PI) insurance (where permitted by the PI insurer).
4. The party initiating the offer (typically the employer, but sometimes the trustees) should pay for the **Advice** and associated services, for example helplines and the Transfer Value Analysis report production. Remuneration for **Advice** must not be related to take up rates or involve commission. These points should be communicated to the member.
5. The **Advice** should be tailored to the individual and their circumstances as a whole including consideration of all materially relevant factors known after reasonable enquiries. This applies whether or not the **Advice** is a regulated FCA activity. To do this, the **Member Adviser** will need to collect personal information from the member using a fact find or similar process. The **Member Adviser** should:
 - Follow **Know Your Client** principles and should have, and should follow, a written **Vulnerable Client** policy.
 - Assess **Suitability**, including an assessment of the member's capacity for loss, their attitude to risk and their ability to manage risk.
 - Assess the relative value and risk of the member's current benefits (including discretionary benefits and benefit options) and the alternative benefits they are being offered (this may involve presenting benefit projections and/or values to members). This assessment should be made bearing in mind the potential implications for the member in the short, medium and long term, and considering various outcomes based on different events (for example early retirement, ill health, death).
 - Consider the implications of the offer on other parties, for example the spouse and other beneficiaries of the member, and advise the member (and as appropriate the other parties) on those implications.
 - Consider the extent to which the employer's financial strength and its covenant to the pension scheme, and the protection offered by the Pension Protection Fund and FSCS might be relevant factors to the **Advice**.
6. **Advice** should include at least one face-to-face or telephone meeting with the member. Face-to-face meetings should be available to all members who are classified as **Vulnerable Clients**.

7. The **Advice** should result in a written, tailored **Recommendation** to each member that is in each member's best interests and should explain the reasons for the **Recommendation**.
8. For **Transfer Exercises**, the **Advisory Process** should be structured so that a member is required to take **Advice** before the offer can be accepted. This should be clearly communicated in early member communications. In the majority of cases the **Advice** will be regulated by the FCA. Where this is not the case the **Member Adviser** should apply the same processes and principles as would apply to FCA regulated advice (for example, on a transfer to a DC occupational scheme, the **Member Adviser** should follow the same process as if it was a regulated transfer to a personal pension).

For **Modification Exercises** that do not meet the **Value Requirement**, the **Communications and Advisory Process** should be structured so that **Advice** is strongly recommended. However, if a member does not wish to engage with **Advice**, the **Member Adviser** may, as an alternative, provide **IE Guidance** and the member may be permitted to accept the offer if the member signs a suitably worded statement that confirms that they were offered **Advice** but did not accept it and they accept the consequences of this.

For **Modification Exercises** that meet the **Value Requirement**, the **Communications** and guidance process should be structured so that it is a requirement to take **IE Guidance** before the offer can be accepted.

Nothing in this Code should be taken to mean that the member may not, as an alternative, or in addition, seek **Advice** or guidance from their own financial adviser. Where a member seeks **Advice** from their own financial adviser for a **Transfer Exercise**, there should be clarity between all parties as to which adviser is taking responsibility for the **Advice**. Where a member seeks **Advice** or guidance from their own financial adviser for a **Modification Exercise**, the member will need to at least engage with **IE Guidance** and (if appropriate) sign a statement saying they do not want **Advice** from the **Member Adviser** being used for the exercise.

9. Employer advisers, trustee advisers and **Member Advisers** should not promote themselves by reference to the features of their own **Advisory Process** that are designed to result in higher take-up rates (for a given level of engagement with **Advice**). For the avoidance of doubt, it is acceptable for advisers to promote themselves by reference to innovative ideas to encourage engagement with **Advice**.

The following table shows which of the above points apply when providing **IE Guidance** (these differences are also listed at the end of the Glossary of Definitions), and also shows a comparison with the DC Guidance Guarantee by way of reference and to avoid confusion:

| Key points to provide Advice | Does this also apply to IE Guidance? (Yes/No/Partial) | Comments | DC Guidance Guarantee comparison, as provided by Pension Wise |
|--|---|---|---|
| 1. Impartial financial Advice by Member Adviser independent from employer | Y | | Yes – to be provided by Pension Wise (only available to over 50s) |
| 2. Member Adviser suitably qualified and experienced | Y | | Pension Wise requirements are set out in regulations |
| 3. Contract between member and Member Adviser specifying legal recourse for member | N | No need for a written contract under IE Guidance | No |
| 4. Advice paid for by party initiating offer | Y | | Free to member |
| 5. Advice tailored to individual and their circumstances as a whole | Partial | IE Guidance should be as complete and relevant as possible but not a written fact-find; IE Guidance does not require following Know Your Client, Vulnerable Client and Suitability procedures | Pension Wise's, operating scope is specific, primarily focusing on DC |
| 6. Advice includes at least one face to face or telephone meeting | Partial | No need for face to face meeting to be offered to Vulnerable Clients under IE Guidance but at least one telephone meeting in all cases | Face to face or telephone meeting, or internet self-service |
| 7. Advice results in tailored Recommendation to each member | Partial | Recommendation not required under IE Guidance but record of conversation required to be provided to the member | Record of conversation to be provided to the member |
| 8. Advice or IE Guidance is required | Y | As indicated in the Code text | No – Voluntary |
| 9. Employer advisers and Member Advisers should not promote themselves by take-up rates | Y | | Not applicable |

C. Application of the Proportionality Threshold

Where the **Proportionality Threshold** applies to an offer that is made to a member, the **Advice** and **IE Guidance** requirements under Principle 2 are amended for that member as follows:

- There is no requirement to provide **Advice**, regardless of the **Balanced Deal Percentage**;
- There is no requirement to structure the guidance process so that it is a *requirement* for the member to take **IE Guidance** before the offer can be accepted;
- However **IE Guidance** should be made available and readily accessible to members who wish to have it.

Whilst the Code's **Advice** and **IE Guidance** requirements are amended in these circumstances, users of the Code may wish to consider whether it would be good practice to provide or require further **Advice** or guidance, based on their knowledge and experience of the membership.

PRINCIPLE 3: **Communications** should be fair, clear, unbiased and straightforward.

This section assumes that the employer is the party making the offer and has been written primarily with the employer's communications to members in mind. Where another party is making the offer (eg trustees) the wording should be interpreted accordingly.

The **Member Adviser** should also apply these points in their member communications (unless the point is irrelevant). The trustees and any other party (for example **Insurers**, employer advisers) who communicate with members should also apply these points when communicating to members about the offer unless irrelevant or inappropriate in the context.

How to apply this principle

1. **Communications** should be fair, clear, not misleading and, wherever possible, use plain English. This includes ensuring the following principles (drawn from The British Code of Advertising, Sales Promotion and Direct Marketing) are met:
 - **Honesty**: no party should exploit the credulity, lack of knowledge, or inexperience of members.
 - **Truthfulness**: no **Communication** should mislead, or be likely to mislead, by inaccuracy, ambiguity, exaggeration, omission or otherwise. **Communications** must not omit, hide or provide in an unclear, unintelligible, ambiguous or untimely manner any material information.

- Fear and distress: no **Communication** should cause fear or distress without good reason.
2. **Communications** should be unbiased and straightforward. Employer **Communications** should be factual and should simply inform the member of the offer and the process. Employer **Communications** should not attempt to influence the member one way or another. However, the member may be encouraged to engage with the **Advisory Process**.
 3. In preparing **Communications**, employers and other parties should consider: the member's perspective; the nature of the decision for them and their needs in making that decision.
 4. There should be an initial written communication from the employer that includes at least the following information (it will invariably be appropriate to include further information to follow the Code and ensure that the offer is understood by members):
 - A clear statement that the member does not need to accept the offer and the default position if the member takes no action.
 - A description of the offer – what is being given up, and what is being offered, including the benefits and risks of both alternatives.
 - The employer's reason for making the offer.
 - Warnings about the potential downside risks of accepting the offer.
 - Easy to find contact details to be used if the member wishes to take the next step (usually this will be a telephone number for the **Member Adviser**).
 - Contact details for the Pensions Advisory Service and their availability at any time to assist members in connection with any pensions query they may have.
 - Contact details for the Pensions Ombudsman and an explanation of their role in case of the potential need for redress.

- An explanation of the role of the Pension Protection Fund (and FSCS where applicable) and how this is relevant to the exercise.
 - An explanation of the roles of FCA and the Pensions Regulator as appropriate to the exercise.
 - A prominent statement that this Code has been followed.
 - Prominent statements of compliance with any other relevant requirements or guidance.
 - For **Modification Exercises**, the **Balanced Deal Percentage** and an explanation of what this means.
 - If the **Balanced Deal Percentage** is less than 100%, a clear and open explanation of the expected gain to the employer and expected loss to members if the offer is accepted, making it clear that the security of the scheme is the employer's responsibility.
5. Charts, tables of figures and descriptions should illustrate the risks and benefits of an offer in a fair and balanced way. For example:
- For **Pension Increase Exchange** exercises, projections of future pensions should continue to at least the average expected lifetime of a member based on the same age and sex, and should be based on a suitably wide range of future inflation assumptions; charts should be to scale and appropriate to the member to ensure the correct impression is given. Consideration should also be given as to how to fairly communicate any impact on dependants' pensions.
 - For **Enhanced Transfer Value** exercises, illustrations of risk (if included) should include a suitably wide range of possible future inflation, investment return and annuity price outcomes.
6. **Communications** should be tailored and meet the needs of the intended audience, ensuring that they are relevant, accessible, comprehensive and focussed on the key and important points.
7. Where presentations are held the employer should ensure that those who are unable to attend can access the information at the same time as attendees or shortly afterwards.

8. The employer may remind the members of the deadline by which decisions need to be made. A reminder should be brief and should make it clear that the member does not have to take up the offer but, if they do want to accept, they need to respond by the deadline date. A reminder letter may restate the offer to the member. A reminder letter should not seek to influence members, for example by informing them of take-up rates to-date.
9. All parties to an offer should promptly circulate all template **Communications** to the other parties associated with an offer that have an interest in those **Communications** and provide adequate opportunity for consultation and comment before issue.

PRINCIPLE 4: Records should be retained and **Insistent Customers should be reported.**

Record retention provides protection for all parties by providing the evidence of what was intended and what actually transpired. It provides an objective source of evidence to confirm that an **Incentive Exercise** has sought to follow the Code and assists in the resolution of complaints and disputes.

How to apply this principle

All parties should be mindful of their duty to retain appropriate records to meet statutory and regulatory obligations. They should also consider how they would make available records of their decisions and the information used in their consideration. It is likely that such records will need to be retained indefinitely to satisfy this principle.

Where providing **Advice** rather than **IE Guidance**, the **Member Adviser** should record and report on **Insistent Customers** to the other parties (the employer, the trustees, the where applicable the **Insurer**). In order to follow this requirement without breaching member confidentiality, it may be necessary to seek the member's permission (perhaps as part of the member offer acceptance form) for evidence of their acceptance of the offer to be passed to the **Member Adviser**. The **Member Adviser** can then collate a report for the other parties on the outcome of the **Advisory Process**, and which members have followed the **Recommendation**. The report can be on a summary aggregate basis.

PRINCIPLE 5: Exercises should allow sufficient time.

Incentive Exercises should not be rushed. Members should have sufficient time to consider offers and to contact the **Member Adviser** to raise questions, and reflect on the issues, before proceeding. Members should not feel under undue pressure when considering an offer.

How to apply this principle

1. The **Communication** and **Advice** timetable, and any reminder letters, should not put undue pressure on members to make quick decisions.
2. From the date of receiving the final information and communications on the offer, members should be provided with at least three months to make a decision.
3. From the date the final piece of **Advice** or **IE Guidance** has been provided, members should be given at least two weeks to make a decision before the final deadline.
4. It is recognised that some employers may wish to set a fixed cash budget to spend on an **Incentive Exercise** (for example the employer may have a fixed cash budget to spend on topping up transfer values). In such cases, particular care should be taken with **Communications** so that they are not perceived as putting undue pressure on members – for example, the communication of “first come first served” should be avoided. Employers should not set cash budgets with an objective of encouraging take up of an offer.
5. A two week cooling off period should be provided to members; from the point at which each member returns his/her option forms. For **Modification Exercises**, this means designing option forms such that they allow members to change their decisions within two weeks. For **Transfer Exercises**, this means retaining the transfer value within the scheme for two weeks, before transferring it to the **Insurer**. (The parties will need to liaise closely with the **Insurer** so that members are not confused by any subsequent FCA required cooling off notice.) As this introduces additional out-of-market risk for members, it would be appropriate to bring this to the attention of members early on in the communication process so that members are fully aware of this additional delay and the reasons for it.
6. It is recognised that some decisions are necessarily time critical (for example, the acceptance of an annuity quotation) and where this is the case, there will be less time available. To meet this principle, information and advice should be provided to members in a timely way within these constraints so as to avoid undue pressure.

PRINCIPLE 6: Treatment of **Vulnerable Clients**.

How to apply this principle

1. For exercises where pensioner members are included:
 - Pensioners under age 80 may receive an offer pack.
 - Pensioners aged 80 and over should only receive a short letter to notify them that the exercise is taking place and that they will not be contacted again unless they get in touch to ask for an offer pack. This letter should be unbiased, factual and not seek to influence the member one way or the other.
2. For all members, regardless of age, the **Member Adviser** should have a **Vulnerable Client** procedure (for example covering those over a certain age or with reduced mental capacity) and should follow it when providing **Advice**. It is acceptable for a different procedure to apply when providing **IE Guidance**.
3. More generally, those initiating the exercise may choose to target only specific groups of members who may be more likely to benefit from an **Incentive Exercise** and this is acceptable under the Code. If they do so, care must be taken to comply with all relevant legislation (for example, age discrimination legislation).

Principle 7: Aware of roles and responsibilities and acting in good faith

The following points describe key roles and responsibilities in **Incentive Exercises** and how parties should follow the Code in their areas of control. This has been written on the assumption that an employer associated with a pension scheme is the party making the offer. If another party is making the offer these points should be interpreted accordingly.

How to apply this principle

1. It is the responsibility of advisers (for example actuarial and legal advisers of employers and trustees) to ensure that their clients are aware of the Code if they are asked to advise on an **Incentive Exercise** and pro-actively bring to their attention any areas that they become aware of that are not being followed.
2. If an employer is considering an **Incentive Exercise**, they should engage with the trustees of the pension scheme at an early opportunity and confirm to the trustees whether or not it is their intention to follow the Code.
3. The employer, with the help of their advisers, is ultimately responsible for ensuring the Code is followed and reporting on this to the other parties involved in the exercise.

4. The Code envisages that trustees, providers and **Member Advisers** may choose not to participate in an exercise that does not follow the Code, other than where there are clear reasons to depart from the Code and those departures do not adversely affect the protection of members and other stakeholders, although this should not be taken to over-ride other legal obligations of the various parties.
5. The primary duty of trustees is to comply with trust law, which includes for example seeking to protect the security of existing accrued benefits. Following the Code is not a legal duty for trustees. Trustees should seek advice on their responsibilities in relation to a particular **Incentive Exercise** at an early opportunity. The Code deliberately does not address trustee responsibilities as they may vary in different cases depending on the facts. This is likely to at least include trustees seeking advice on the following: data protection matters, conflicts of interest, their own Trust Deed and Rules, and the extent to which they should satisfy themselves that the design of the offer, the **Communications** and the **Advisory Process** are appropriate for members.
6. Employers and trustees will need to consider their responsibilities in relation to the **Balanced Deal Calculation**. Trustees may wish to validate an employer's calculation of a **Balanced Deal Percentage**. Trustees and employers should allow the other party adequate time to consider and respond to any proposals in a timely manner.
7. The trustees should play a role in ensuring that the **Communications** principle (principle 3) is met. The employer and other parties (as appropriate) should confirm to the trustees that this principle has been followed. In this connection the trustees may also choose to review, and ask their advisers to review, written material, **Member Adviser** scripts for member **Advice** and/or **IE Guidance**.
8. The **Insurer** has a duty of care to its policyholders. Therefore the **Insurer** should seek sufficient information to be assured that any transactions received and that are covered in the scope of the Code have followed the Code. Where the **Insurer** is not assured, the necessary governance procedures should be in place to make and record a formal decision whether to accept the transactions.
9. Adoption of the Code will be monitored. Employers, trustees and advisers should therefore assume that they will be asked to provide information about an exercise, and may also be asked to take part in research.
10. TPR will continue to monitor incentive exercises through the scheme return. Any concerns about the running of an **Incentive Exercise**, for example reports of coercive, pressuring, or misleading behaviour, or any concerns about the structure or conduct of parties involved in an exercise, should be reported to the Pensions Regulator.

The Pensions Regulator

Tel.: 0345 600 0707

Email: customersupport@tpr.gov.uk

Address: Napier House, Trafalgar Place, Brighton BN1 4DW

Supporting Information

Glossary of Definitions

Advice* – Every aspect of the advice given to members that leads to a written **Recommendation**, including: the **Advisory Process**, the pre-advice information provided to the member, the collection of information from members using fact-finds, the verbal advice given to the member, the actual recommendation, and all advice supporting documentation. The **Recommendation** to members should be clear and unambiguous.

Advisory Process – The process of taking general information, and specific information from the member, and leading towards a **Recommendation**.

Balanced Deal Calculation – a calculation completed for a **Modification Exercise**, typically a **Pension Increase Exchange** exercise, to value members' benefits before and after the **Modification Exercise** using the framework of Section 67 of the Pensions Act 1995, and to compare the two, so as to assess the **Balanced Deal Percentage**.

Balanced Deal Percentage – the result of a **Balanced Deal Calculation**; a single result will apply to all members for a particular exercise.

Cash Incentives – Any part of the **Incentive Exercise** offer which has a value to the member that is not a pension benefit arising from a UK registered pension scheme and which is contingent on the acceptance of the offer. This includes payments in cash, goods and services of value which are immediately available to the member on completion of the exercise. It also includes cash, goods and services of value – including additional salary increases – which are available in instalments or deferred until a later date. For the avoidance of doubt, this refers to additional amounts beyond (or earlier than) what an individual could otherwise receive from a UK registered pension scheme.

Communications – communications to members in relation to an offer. This includes all written and verbal communications from all parties, depending on the context.

Enhanced Transfer Value – an offer made as part of an exercise where a member or members of a UK registered defined benefit pension scheme are offered an enhancement to the transfer value(s) that would otherwise have been available to them (or another inducement to transfer).

Full Commutation – an offer made as part of an exercise where a member or members of a UK registered defined benefit pension scheme are offered a cash lump sum in full replacement for a pension that would otherwise have

been available to them. For clarity, any offer of cash that first involves conversion to DC benefits should be treated as a Transfer Exercise.

IE Guidance* - Every aspect of a member guidance process by which a member is assisted by a **Member Adviser** in making a decision, by the **Member Adviser** being available to answer questions, provide information, educate and explain relevant issues to the member. There is no formal written contract with the individual, and no **Recommendation** is made to the individual. For the purposes of the Code the provision of **IE Guidance** must be backed up with a written record of the **IE Guidance** that is issued to the member.

Incentive Exercises – an invitation or inducement (generally referred to as an “offer” throughout this Code) provided to a member to change the form of their accrued defined benefit rights in a UK registered pension scheme, which meets both of the following tests:

- One objective of providing the invitation or inducement is to reduce risk or cost for the pension scheme or sponsor(s); and
- The invitation or inducement is not ordinarily available to members of the pension scheme.

The Code broadly covers two types of **Incentive Exercise**: **Transfer Exercises** and **Modification Exercises**.

Insistent Customer – a member who has received **Advice** and chooses to act contrary to the **Recommendation** in relation to acceptance of the offer. A member who acts contrary to another part of the **Recommendation** is not an **Insistent Customer** for the purposes of this Code.

Insurer or Pension Provider – the insurance company that is offering the investment product that receives a transfer from a UK registered defined benefit pension scheme. Example products include a personal pension, stakeholder pension, annuity or income drawdown product.

Know Your Client – used in the same way as for FCA requirements, referring to the process by which a **Member Adviser** ascertains relevant information about their client, including whether they are a **Vulnerable Client**, before being able to assess **Suitability**.

Member Adviser – The party providing **Advice** or **IE Guidance** to the member. This term may be used to refer to the individual adviser or his/her firm depending on the context.

Modification Exercise – an **Incentive Exercise** that involves an offer to members to change the terms of their accrued defined benefit rights usually within the same trust or by offering a cash alternative; typically a **Pension Increase Exchange** exercise or a **Full Commutation** exercise.

Monitoring Board - the Incentive Exercises Monitoring Board established to monitor the effectiveness of the Code.

Pension Increase Exchange – an offer made as part of an exercise where a member or members of a UK registered defined benefit pension scheme are offered an enhancement to their pension income (or another inducement) in return for surrendering all or part of their future pension increases.

Proportionality Threshold – for **Transfer Exercises** and similar, this threshold applies where a member is being offered a transfer value of £10,000 or less; for **Full Commutation** exercises and similar, this threshold applies where a member is being offered a cash commutation payment of £10,000 or less; for **Pension Increase Exchange** exercises and similar, this threshold applies where the pension that can be modified under the offer for a particular member is a pension of £500 per annum or less; for other exercises, a broadly equivalent value / pension may be set by users of the Code. The **Proportionality Threshold** should be applied cumulatively (for example, the **Proportionality Threshold** would apply to an initial offer of a **Pension Increase Exchange** modification of a pension amount of £400 per annum, but would not apply to a subsequent offer to the same member for a further modification of a pension amount of £100 per annum or more)

Recommendation – A final written recommendation provided to members. This includes a clear statement on whether or not the **Member Adviser** recommends the offer is accepted and if there are options on implementation, which options should be selected.

Suitability – used in the same way as for FCA requirements, referring to the assessment of whether a financial choice and/or financial product is suitable for a client.

Total Pension Increase Exchange – an offer made as part of an exercise where a member or members of a UK registered defined benefit pension scheme (typically over age 55) are offered a transfer value to an immediately vesting annuity, income drawdown arrangement or other similar product. Such exercises can also be called flexible retirement offers (or FROs).

Transfer Exercises – an **Incentive Exercise** that involves an offer to members to transfer defined benefit rights out of their pension scheme; typically an **Enhanced Transfer Value** exercise or a **Total Pension Increase Exchange** exercise. **Transfer exercises** include exercises which offer the conversion of safeguarded DB rights into flexible DC benefits.

Value Requirement – a **Modification Exercise** meets the **Value Requirement** test if the assessed **Balanced Deal Percentage** is at least 100%.

Vulnerable Clients – used in the same way as for FCA requirements, referring to clients who may be particularly vulnerable by virtue of age, health, understanding etc, and who may therefore require special treatment.

* Differences between **Advice** and **IE Guidance** include the following:

- **IE Guidance** does not require a written contract between the member and the **Member Adviser** (the **Member Adviser** firm may wish to consider whether any **Communications** imply there is a verbal contract).
- When providing **IE Guidance**, the **Member Adviser** may require the member to confirm by signature that a **Recommendation** has not been provided and **Advice** has not been given.
- **IE Guidance** does not require the collection of, and retention of, personal information about the member and their attitude to risk etc (for example using fact finds).
- **IE Guidance** does not require a written **Recommendation** to be made to the member but does require a written record of the **IE Guidance** to be issued to the member.
- Whilst **Member Advisers** should make reasonable efforts to ensure that **IE Guidance** covers all the relevant issues, **IE Guidance** need not be complete if the member has little interest in discussing particular issues.
- When providing **IE Guidance**, there is no need to follow **Vulnerable Clients** and **Know Your Client** procedures, although the **Member Adviser** should bear in mind these principles when giving **IE Guidance** (**IE Guidance** does not require a face to face meeting to be available to **Vulnerable Clients**).
- When providing **IE Guidance**, there is no need to record and report **Insistent Customers**.

Ownership, Maintenance and Monitoring of the Code

The Incentive Exercises Monitoring Board is responsible for ownership, maintenance and monitoring of the Code. It is a volunteer board representing key industry interests.

The **Monitoring Board** “owns” the Code and makes it available to the industry, promoting it as necessary.

Maintenance includes liaising with stakeholders to ensure the Code remains fit for purpose as well as making and communicating version changes. The **Monitoring Board** seeks to achieve this through encouraging practitioners to share experiences of exercises, in a non-attributable way. It does not seek to interfere with exercises and does not publish information on exercises that would identify any scheme or stakeholder, but it uses statistics collected on exercises and the extent to which they follow the Code, as provided by the industry and where relevant via information collected by the Pensions Regulator. The **Monitoring Board** will ensure full compliance with Data Protection Act principles in the sharing and use of such information.

Modifications to the Code may be considered where these are in line with the objectives of the Code.

The **Monitoring Board** does not have an advisory role. For example, it will not clarify what is meant by the Code or confirm whether specific actions are in line with the Code.

If there is evidence of significant departures from following the Code, the **Monitoring Board** might recommend Government to introduce legislation.

One area that the **Monitoring Board** will be monitoring over time will be the extent to which employers introduce offers outside of the scope of the Code (for example, **Pension Increase Exchange** options offered ordinarily at the point of retirement) and do not appropriately apply relevant principles of the Code. The **Monitoring Board** may review, remove or add to the Boundary Examples published on its website from time to time.

Comments on the Code and monitoring may be directed to:

info@incentiveexercises.org.uk

or via the website www.incentiveexercises.org.uk

Examples of transactions that are out of Scope

For the avoidance of doubt, the following transactions are outside the scope of the Code:

- An individual member transfer request which is in line with normal ongoing terms for the scheme – both in financial terms and associated communication / any financial advice.
- Transfers or modifications made without member consent accompanied by the required certificate from the scheme actuary.
- Transfers with member consent from one defined benefit scheme to another defined benefit scheme where identical benefits are being provided.
- Changes to defined benefit schemes solely relating to future accrual for active members (i.e. not affecting accrued rights and entitlements).
- Member options ordinarily available on certain events, such as retirement or leaver processes, including early retirement and options to commute pension for a tax-free lump sum.
- Securing benefits with an insurance company or any transfer value offered after a wind up has been triggered which is an equivalent value alternative to a buy out.
- Any situation involving only defined contribution pension rights.

The Boundary (and other) examples published alongside version 2 of the Code provide further examples of cases that are in / out of scope.

The Code is not intended to apply generally in relation to exercises associated with winding-up, on the basis that trustees can be expected to set terms for all options appropriately in the context of the wind-up. Therefore, in many cases, wind-up lump sums can be expected to fall outside of the scope of the Code. However, all parties should be mindful of the principles of the Code in such circumstances to ensure that members' interests are appropriately protected.

Where users of the Code decide that a transaction or offer is not in scope of the Code, employers, trustees and advisers should be mindful of the principles of the Code and seek to ensure that changes to benefit options offered by the scheme will maintain suitable protection of members' interests. In some cases it may be appropriate to apply some aspects of the Code to exercises that fall outside the scope of the Code. For example changes to defined benefits for current employees such as introducing restrictions on pensionable pay may impact accrued rights over time. Employers, trustees and advisers are encouraged to consider the extent to which it would be appropriate and helpful to members to apply some or all of the Code in such situations.

Complaints and Redress

Evidential value of the Code

The Pensions Ombudsman and the Financial Ombudsman Service often consider industry and Government codes of practice when deciding cases. And although each case will be decided on its own merits, where employers and advisers are unable to demonstrate they have followed the Code in good faith then the ombudsman may take this into consideration when deciding the case.

Making a complaint

Should a member have cause to complain about an **Incentive Exercise**, this should in the first instance be raised with the employer, trustee, administrator of the pension scheme or **Member Adviser** as appropriate. If the complaint is against the trustees, the member will need to go through the scheme's formal Internal Dispute Resolution Procedure (IDRP). The member should be aware that there are time limits within which the complaints procedure should be instigated.

The Pensions Advisory Service (TPAS)

TPAS is an independent, non-profit organisation, providing free and impartial information to members. The Pensions Ombudsman expects complainants to have consulted TPAS before coming to him.

The Pensions Advisory Service

11 Belgrave Road

London

SW1V 1RB

020 7630 2250

The Pensions Ombudsman

The Pensions Ombudsman may consider a complaint about the management or administration of a pension scheme including in relation to **Incentive Exercises**. Current, former or potential members of an occupational or personal pension scheme may make a complaint. This may be against the trustees, manager, or administrator of a pension scheme or the employer. Trustees or managers of an occupational pension scheme may bring a complaint against the scheme's participating employer (or a trustee or manager of a different scheme). Employers may bring a complaint against the trustees or manager of the same occupational pension scheme.

The Office of the Pensions Ombudsman

11 Belgrave Road

London

SW1V 1RB

020 7630 2200

Financial Ombudsman Service (FOS)

FOS may be able to help with complaints about sales or advice given by FCA regulated financial firms.

The Financial Ombudsman Service

South Quay Plaza

183 Marsh Wall

London

E14 9SR

0800 023 4567

The Pensions Ombudsman and FOS have an agreement in place known as a Memorandum of Understanding by which they ensure that complaints are directed to the correct office and that complaints that may straddle the two jurisdictions are dealt with appropriately.