



Institute
and Faculty
of Actuaries

Flexibility at Retirement

Alice Evans, Towers Watson



04 February 2014

Overview

- An additional option given to members of DB pension schemes to transfer their benefits out of their scheme when they reach retirement
- Scheme members are provided with support from an IFA and annuity broker to consider the benefits they could obtain outside the DB scheme, using the open market in a similar way to DC members
- Various names to describe these exercises e.g. Retirement Transfer Options, Reflex, FRO, FaR and, more historically, TPIE



Institute
and Faculty
of Actuaries

04 February 2014

2

Illustration

1. Scheme pension <ul style="list-style-type: none"> £10,000 pa LPI increases 	2. Scheme cash and residual pension <ul style="list-style-type: none"> £7,000 pa LPI increases £45,000 tax-free cash 	3. RTO illustration <ul style="list-style-type: none"> £9,000 pa No increases £62,500 tax-free cash
Existing scheme options		New RTO option

Why introduce RTO?

Member perspective
<ul style="list-style-type: none"> The standard DB scheme pension may not be the best fit for a member's needs. For example: <ul style="list-style-type: none"> Would a flat pension in retirement be a better "shape", giving a greater income in earlier years and a lower income later? Does the member's spouse need the full scheme reversionary pension of 50%-80% of the member's pension? Or do they have their own source of retirement income? A member may want to maximise their tax-free cash lump sum If a member has other pensions and meets the Minimum Income Requirement, they may prefer to move their scheme pension into a DC arrangement to make use of drawdown flexibilities

Why introduce RTO?

Trustee perspective

- A responsibility to make members aware of other options besides the DB pension particularly as options outside of the DB scheme may be in the best interests of some members
- RTO brings with it the added benefit of a robust advice framework at retirement to ensure members make informed choices, whether this involves staying within the DB scheme or reshaping benefits outside the scheme
- Levels the playing field for schemes with both DB and DC sections

Why introduce RTO?

Company perspective

- Reduces the size of the DB scheme as liabilities will be removed over time
- Removes DB risks such as investment, longevity and inflation
- Reduces volatility as the scheme is smaller
- Liabilities can be removed at significantly lower cost than buy-in/buy-out – once members are pensioners it is much more difficult to do this
- Lower headcount means lower PPF levies and administration charges

The Code of Practice on Incentive Exercises

Ongoing RTO

The Code does not apply to the introduction of benefit options that are “made ordinarily to members” (e.g. commutation and PIE option at retirement)

- Could justify a conclusion that ongoing RTO is not in the scope of the Code
- However, engaging more with members with the aim of increasing transfers, particularly with IFA advice, could be considered an Incentive Exercise under the Code

Bulk RTO

Bulk RTO exercises are considered Incentive Exercises under the Code – in fact TPIE exercises (“and variants thereof”) are specifically referenced as a form of Transfer Exercise in the Code

Conclusion

Following the principles of the Code such as providing clear member communications and IFA support would be expected to result in **more members engaging** with the retirement process and potentially taking up an option to transfer their benefits, having made an **informed decision** based on a **robust advice framework**.

We therefore recommend the Code’s key principles are followed when implementing RTOs



04 February 2014

7

What’s involved?

Key stages

Stage one	Feasibility
Stage two	Design
Stage three	Legal & practical considerations
Stage four	IFA selection and communications



04 February 2014

8

Stage One: Feasibility

Key considerations	
Attractiveness to members	What does CETV buy on the open market vs. scheme pension?
Scheme specifics	e.g. AVCs/DC benefits, reduced CETVs, early retirement terms
Funding/solvency impact	Trustee concerns vs. Company objectives
Accounting impact	Settlement accounting required?
Advice costs	Options for meeting these
Member profile	How will impact come through over time?



04 February 2014

9

Stage Two: Design

Key considerations	
Transfer terms	Amend CETV basis if required
Selection risk	Only a concern if take-up is low
Ongoing or bulk?	Offer to all those retiring imminently, or on an ongoing basis
Combine with other exercises?	e.g. could boost impact of an early retirement exercise



04 February 2014

10

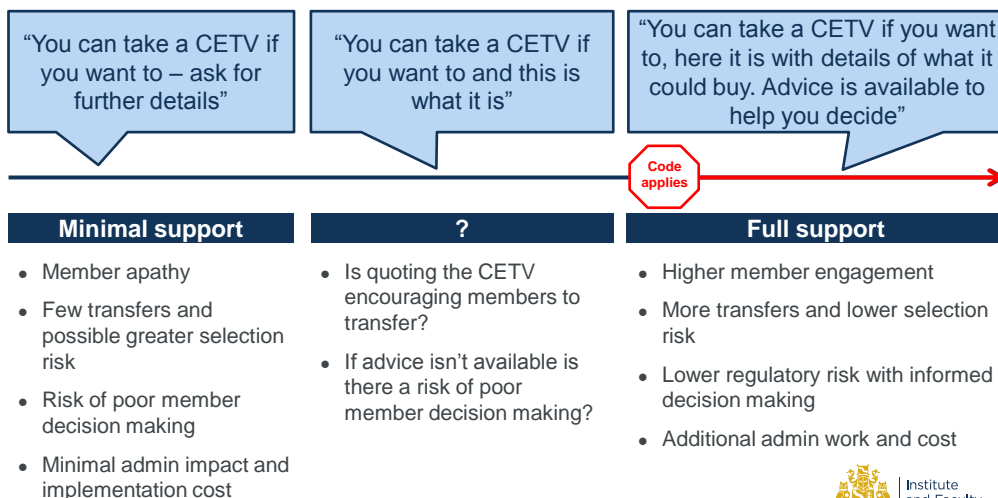
Stage Three: Legal & practical considerations

Key considerations	
Rule amendments	Allow transfers in the year up to retirement
Investments	May need to rebalance and/or increase liquidity
Administration and processes	Additional work required, some time-sensitive
Data cleansing	May be needed beforehand

Stage Four: IFA selection and communications

Key considerations	
Member engagement	How to educate and communicate effectively with members in the run-up to retirement – balancing costs against engagement levels
Code of Good Practice	Ensure advice process and communications comply with the Code and legal sign-off is obtained
IFA selection	Agree selection criteria and process, structure of IFA fees and who will meet these

Levels of member support at retirement



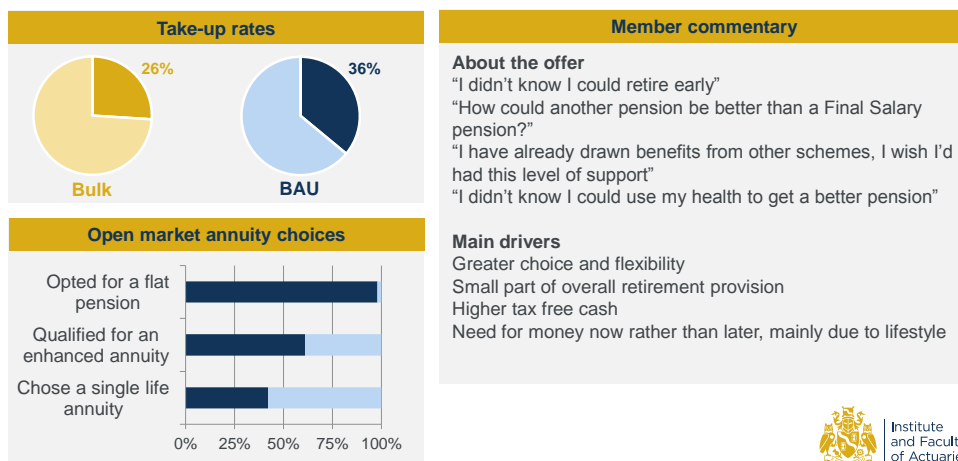
Institute
and Faculty
of Actuaries

04 February 2014

13

Case study

Bulk RTO for 55-65 year olds followed by "business as usual" implementation



Institute
and Faculty
of Actuaries

04 February 2014

14

Audience survey highlights from the Incentive Exercise Forum

Decision timeframes		Market experience	
Question	Response	Question	Response
Q1: Are the timescales for member option decisions stated in the Code appropriate?		Q3: Which exercises are currently most appealing to companies?	
a) Yes – the timescales are appropriate	95%	a) ETV	5%
b) No – the timescales are too long	0%	b) PIE	15%
c) No – the timescales do not allow enough time	5%	c) RTO	80%
		d) None – not interested in member option exercises	0%
Q2: Has the Code facilitated appropriate engagement of Trustees?		Q4: Which exercises are currently most acceptable to Trustees?	
a) Yes	95%	a) ETV	5%
b) No	5%	b) PIE	10%
		c) RTO	80%
		d) None – not interested in member option exercises	0%



Institute
and Faculty
of Actuaries

04 February 2014

15

Questions

Comments

The views expressed in this presentation are those of the presenter.



Institute
and Faculty
of Actuaries

04 February 2014

16