

Guidance on transfer incentives

This is a consultation document on guidance for trustees and managers of occupational pension schemes produced by The Pensions Regulator ('the regulator'), the body that regulates work-based pension arrangements.

This guidance replaces the 'Inducement offers' guidance published in January 2007.

**The Pensions
Regulator**

Contents

| | |
|---|--------|
| Introduction | page 3 |
| Background | page 3 |
| Development of guidance | page 4 |
| Format of revised guidance | page 4 |
| Consultation questions | page 5 |
| Responding to the consultation | page 6 |
| Closing date | page 6 |
| The Government code of practice on consultation | page 6 |
| Feedback on this consultation exercise | page 6 |
| Impact assessment statement | page 7 |
| Guidance on transfer incentives | page 8 |

Introduction

This is a consultation document on guidance for trustees and managers of occupational pension schemes produced by The Pensions Regulator ('the regulator'), the body that regulates work-based pension arrangements.

This guidance replaces the 'Inducement offers' guidance published in January 2007.

We have produced this guidance to clarify the role of both the employer and trustees. We want to ensure that trustees become actively involved in any transfer incentive or other benefit modification exercises that the scheme sponsor proposes to run. Trustees have an important role in ensuring that the scheme members are in the best possible position to make the right decision in relation to their pension benefits.

We expect such exercises to be conducted in an open, fair and transparent way. Members need to be provided with clear and not misleading information. They need to have access to impartial and independent advice to make decisions that are right for them. Trustee engagement is essential in ensuring that these standards are met, and the guidance underlines our expectation that trustees consider the interests of all members.

Background

We initially issued guidance in this area in January 2007, when the regulator had clear evidence that inducement exercises had the potential to be run in a way that was detrimental to the security of members' benefits.

Since then, we have been actively monitoring the development of activity and the types of practices that have been forming. We also have more evidence on the types of behaviours that are being displayed.

What we have seen and experienced has concerned us. We now believe there is a need for us to take a stronger stance in this area to protect members' benefits. This has resulted in the regulator adopting a more proactive approach towards identifying and assessing these exercises, and we are working more closely with other regulatory and enforcement bodies. The revision of our guidance supports these actions to enable clear consideration of the risks and to help form best practice.

Many industry surveys indicate that various forms of incentive exercise are increasing in popularity. The main focus has recently been on transfer incentives. But other forms of incentive exercise that can be considered benefit modifications, rather than transfers, are becoming more common. One example is 'pension increase conversions', which carry similar risks. Our revised guidance applies equally to these alternatives where members are being asked to consent to changes or reductions.

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Development of guidance

The aim of our original guidance on this issue was to establish a very high standard of practice where an employer considered that an exercise of this nature was a necessary and appropriate form of liability management for a scheme. There has been a 'box-ticking' approach that has led to exercises being run without due consideration of the needs of scheme members, and in a manner that we do not consider in keeping with the spirit of the guidance.

As a result, we have revised our guidance to a more principles-based approach. The guidance highlights key areas of consideration and clearly articulates our expectation that any exercise should be conducted with the utmost regard to members' interests. We expect market practices in this area to improve, and the success in meeting that objective will be judged by the level of member understanding, and the focus on member outcomes.

The guidance has been developed in consultation with the Financial Services Authority (FSA), and our approach is aligned with their expectations of the entities they regulate. A joint statement from both regulators will be issued to this effect.

Since the issue of our original guidance, the Government's automatic enrolment policy has been implemented into the Pensions Act 2008. Broadly, there are provisions prohibiting an employer from encouraging or coercing a worker to opt out or leave active service, and not join another qualifying scheme. This is unlawful, and has been defined as 'Inducement' in the Act.

To avoid confusion where employers offer incentives to members to transfer or modify accrued or existing benefit entitlement rights, we have named the revised guidance 'Transfer incentives', although it includes other forms of incentive exercises.

Format of revised guidance

The final guidance will be developed primarily as a web-based product.

Whilst copies of the guidance can be printed in full or in part, users will be able to access it online and navigate using a series of hyperlinks to various sections and other resources.

The guidance does not seek to duplicate material contained in other regulatory publications; however, it does include key messages, and signposts users to other resources.

Consultation questions

The regulator would like to hear from trustees and other interested stakeholders on the areas covered in the guidance. We welcome any comments on the guidance, but would particularly welcome comments on both the general and specific questions set out below.

General questions

1. Do you agree that the principles-based approach adopted in this guidance is the right approach to take to protect members' benefits?
2. Do you think the guidance will fulfil the purpose of ensuring that offers are made with full appreciation of the risks being taken by all parties, and with the utmost regard for member outcomes?
3. Are there any additional messages for trustees and/or employers that you would like to see in the guidance?

Specific questions on each section

Section 1: Definition

This section is intended to outline who the guidance is for and who may be interested in the content of the guidance. It also seeks to explain the purpose of the regulator producing guidance in this area and to define the area of consideration.

4. Does this section clearly outline the area that this guidance covers, to whom it is intended to apply, and the scope of regulator's expectations with respect to those operating or involved in this area?

Section 2: Understanding the principles

This section outlines the principles which should apply to any exercise being conducted. It expands what is meant by the principles, and provides some points of consideration when considering and conducting incentive offers.

5. Do you think the principles outlined in the guidance are comprehensive, and encompass what should be considered best practice?

Section 3: Problems and concerns that can arise for members

This section is intended to encourage trustees and employer to think about the members' perspective, the nature of the decision for them and their needs in making that decision.

6. Does this section achieve its intentions?
7. Are there any points from a member's perspective that need emphasising?

Section 4: Key points of note when considering an incentive offer

This section outlines the key risks and considerations for employers and trustees when considering or becoming involved in an incentive exercise.

8. Are there any other key considerations that you feel should be included in the guidance?

Appendix

This is a list of examples of information that may be appropriate when constructing an incentive exercise. It is not meant to be exhaustive in any way, but is intended to be indicative of the type, level and complexity of information that may need to be conveyed.

Responding to the consultation

Responses may be made in either of the following ways:

- By email to:
ticonsultation@thepensionsregulator.gov.uk
(documents should preferably be in Word format)
- By post to:
Carl Davey
Regulatory Policy and Programmes
The Pensions Regulator
Napier House
Trafalgar Place
Brighton
BN1 4DW

If you would like to discuss any aspect or areas of the consultation, please call Carl Davey on 01273 648492.

We may need to share the feedback you send us within our own organisation or with other Government bodies. We may also publish this feedback as part of our response to the consultation.

If you wish your comments to remain anonymous, please state this explicitly in your response.

If you wish your response to be kept confidential, please make this known and we will take the necessary steps to meet your request. However, please be aware that, should we receive a formal request under Freedom of Information legislation, we may be required to make your response available.

When responding, please advise whether you are responding as an individual or on behalf of an organisation (and if the latter, which organisation).

Closing date

This consultation document was published on **13 July 2010**. The closing date for responses to this consultation is **5 October 2010**.

The Government code of practice on consultation

This consultation is being conducted in line with the seven criteria of the **Government code of practice on consultation**:

1. Formal consultation should take place at a stage when there is scope to influence the outcome.
2. Consultations should normally last for at least 12 weeks, with consideration given to longer timescales where feasible and sensible.

3. Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence, and the expected costs and benefits of the proposals.
4. Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is designed to reach.
5. Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
6. Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
7. Officials running consultation exercises should seek guidance in how to run an effective consultation exercise, and share what they have learned from the experience.

Feedback on this consultation exercise

We value your feedback on how well we consult. If you have any comments on the process of this consultation (as opposed to the policy issues raised) please contact our consultation co-ordinator:

- By email to:
laura.butler@thepensionsregulator.gov.uk
- By post to:
Laura Butler
The Pensions Regulator
Napier House
Trafalgar Place
Brighton
BN1 4DW

In particular, please tell us if you feel that the consultation does not satisfy the consultation criteria. If you have any requirements that we need to meet to enable you to respond, please let us know.

Impact assessment statement

The Department for Work and Pensions (DWP) is responsible for conducting impact assessments for new legislation affecting the legislative framework for pensions regulation. In some circumstances it may be appropriate for the regulator to conduct its own impact assessment, and to publish this as part of its consultation exercise, where proposals have additional costs for the regulated community above those already imposed by the legislative requirements.

In this case, undertaking incentive exercises by employers is voluntary and so no additional burden is imposed on the regulated community by amending our guidance. Where there are those that choose to undertake incentive exercises the guidance will ensure that they are conducted in the appropriate manner and with due regard for the members they are targeted at. There will be no significant cost impact on the regulated community, and so an impact assessment is unnecessary in this case.

Guidance on transfer incentives

Key points

- The regulator is concerned that members of pension schemes will be disadvantaged by incentive exercises, particularly if they are not conducted in a manner that makes it most likely members will make a fully informed choice.
- Trustees should start from the presumption that such exercises and transfers are not in the members' interests, and should therefore approach any exercise cautiously and actively.
- Employers should ensure that any offers made are consistent with the principles outlined in this guidance.
- Members to whom an offer is being made should be presented with the appropriate information in a way that is clear, fair and not misleading, to enable them to make a decision that is right for them.
- Fully independent and impartial financial advice should be made accessible to all members and promoted in the strongest possible terms; in almost all circumstances, the structure of the offer should require that members take financial advice.
- Trustees should engage in the offer process and apply a high level of scrutiny to all incentive exercises to ensure members' interests are protected. Above all, trustees should ensure that they are comfortable that the selection, remuneration and broader commercial interests of advisers are aligned with members' interests.
- No pressure of any sort should be placed on members to make a decision to accept the offer.

Contents

| | |
|--|----------------|
| Section 1: Definition | page 10 |
| Who is this guidance for? | page 10 |
| Purpose of this guidance | page 10 |
| What is a transfer incentive? | page 10 |
| The regulator's expectations | page 11 |
| Section 2: Understanding the principles | page 12 |
| Principle 1: Clear, fair and not misleading | page 12 |
| Principle 2: Open and transparent | page 12 |
| Principle 3: Manage conflicts of interest | page 12 |
| Principle 4: Trustee consultation | page 13 |
| Principle 5: Independent financial advice | page 13 |
| Section 3: Problems and concerns that can arise for members | page 14 |
| Section 4: Key points of note when considering an incentive offer | page 15 |
| Employers | page 15 |
| Trustees | page 15 |
| Section 5: What to do if you have concerns | page 18 |
| Appendix: Examples of information to be included in offer | page 19 |

Section 1: Definition

Who is this guidance for?

This guidance relates to transfer incentives and other incentive exercises that are sometimes offered by employers to members of defined benefit (DB) schemes to persuade them to give up or accept a reduction in certain benefits in a DB scheme.

This guidance is primarily aimed at two distinct groups who need to understand and consider the issues involved in any incentive exercise. These groups are:

1. Sponsoring and associated employers considering offering an incentive exercise; and
2. Trustees to the pension scheme where an exercise is being considered or carried out.

In addition to these groups, this guidance may be of interest to members, benefit consultants, professional advisers, pension providers and others.

Purpose of this guidance

Consistent with the regulator's statutory objective to protect members' benefits, the purpose of this guidance is to inform those considering an incentive exercise of relevant issues from a regulatory perspective and of expected standards of conduct for all participants. It also highlights important areas of consideration for employers, trustees, advisers and members affected by an incentive exercise.

The regulator is aware that employers have sought to reduce past service liabilities or modify benefit entitlements by means of incentive exercises. There are significant difficulties in structuring these exercises to meet appropriate standards. Incentive offers can create risks for members, trustees and employers, and those risks should be evaluated before a decision is made to proceed.

What is a transfer incentive?

A transfer incentive exercise is where a sponsoring or associated employer of a DB scheme seeks to remove some or all of its liabilities by persuading members to transfer or modify benefits. This usually takes place through providing some form of financial incentive. Our previous guidance on this matter was entitled

'Inducement offers'. However, since the enactment of the Pensions Act 2008, the term 'inducement' has been given a particular meaning in the context of automatic enrolment schemes. To avoid any confusion of terms, in this guidance we have used the term 'incentive' rather than 'inducement'. This guidance, whilst specifically covering transfer incentives or Enhanced Transfer Values (ETVs) as commonly known, can equally be applied to scheme modifications or benefit forfeitures where members are being asked to make a choice; it is not intended to apply to proposals for schemes being closed to future accrual.

There are a number of ways in which an exercise can be constructed, for example, asking the member to give up non-statutory post-retirement pension increases in return for a higher flat rate pension within the scheme. The most common form is an enhancement to the calculated transfer value of the member's benefits in the scheme, or a cash payment in addition to the transfer value, on the condition that those benefits are transferred out to another form of pension provision.

The purpose of making this offer will be to reduce risk and liability upon the employer. Where the employer provides a DB pension scheme, the employer retains the risk of needing to fund an unknown pension liability. If, for example, this benefit is transferred as a cash sum, the value of the benefit is immediately crystallised. This may reduce cost and/or risk over the long term, and possibly improve the company's balance sheet in the short term.

The regulator believes that trustees should start from the presumption that such exercises are not in the members' interests. If an employer is willing to encourage the transfer, the employer's gain is likely to be the member's loss. The employer reduces or eliminates its promise to pay a defined benefit pension, but the member is unlikely to be able to purchase an equivalent promise on the open market for the transfer value offered.

The regulator recognises that in some instances accepting an incentive can be beneficial for members who consider the risks and the value offered to be in their interests. However, these cases are likely to be in a minority and very possibly a small minority.

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The regulator's expectations

The regulator is concerned that members will be disadvantaged by incentive-led transfers out of DB schemes or benefit modifications.

However, we recognise it is important that scheme members retain responsibility for their own financial decisions where those decisions impact their DB scheme benefits.

The regulator does not consider that reduced risk for one group of members is sufficient reason to allow increased risk for another group. If exercises are to proceed on an appropriate basis, trustees should ensure they consider the interests of both potential transferring members and remaining members equally, and members should be given sufficient information to be able to make an informed choice about an incentive-led activity.

If an employer considers it worthwhile to make an incentive offer, and believes it is a viable alternative to funding the scheme liabilities that represent those promised benefits, then its offer should adhere to the 5 key principles listed below (which are further expanded in section 2).

Principle 1: Clear, fair and not misleading

An offer should be made in a clear, fair and not misleading way, to enable members to understand the implications and make decisions that are right for them.

Principle 2: Open and transparent

The offer should be open and transparent so that all parties involved in the process are made aware of the reasons for the exercise and the interests of the other parties.

Principle 3: Manage conflicts of interest

Conflicts of interest should be identified and appropriately managed in a transparent manner, and where necessary removed.

Principle 4: Trustee consultation

Trustees should be consulted and engaged from the start of the process, with any concerns arising through the exercise alleviated before progressing.

Principle 5: Independent financial advice

Fully independent and impartial financial advice should be made accessible to all members and promoted in the strongest possible terms; in almost all circumstances, the structure of the offer should require that members take financial advice.

If parties adhere to these principles then the regulator expects that any member will be given all the information they need to understand the implications of accepting the offer, and will be able to make the right choices for their own specific circumstances. This will not, however, remove any legal or reputational risks to those making any offer.

The regulator takes an interest in incentives because of its statutory duty to protect the security of members' benefits. It will proactively identify and react to reports of cases where incentive offers have not observed these principles. The regulator is seeking to educate and enable best practice through this guidance, but where necessary and appropriate it will enforce the protection of members' benefits, with statutory powers, including the use of contribution notices and/or financial support directions.

The Appendix to this guidance provides some examples of the types of information that should be included in offers consistent with these principles. This list is not exhaustive and does not attempt to address all the information which would be required to comply with these principles, which will be specific to the circumstances of the offer being made. Including all the information from the Appendix in an incentive offer does not, in itself, mean that the regulator will take no action in respect of the exercise.

Section 2: Understanding the principles

Principle 1: Clear, fair and not misleading

An offer should be made in a clear, fair and not misleading way.

This principle is key to ensuring offers are communicated in an appropriate manner. It is consistent with the rules applicable to financial promotions regulated by the Financial Services Authority (FSA).

The principle supports the provision of information that is tailored and meets the needs of its audience, ensuring that it is relevant, accessible, comprehensive, and focuses on the key and important points. The offer should avoid providing excessive or confusing details, jargon, understating or overstating positions, or concealing or omitting essential pieces of information.

To align with this principle the offer should provide a clear indication of the value of benefits being given up (both in today's terms and on retirement) and the cost of purchasing equivalent benefits on the open market today (ie a deferred annuity). It should also outline fully the risks involved in accepting the incentive offer, including investment, longevity and annuity risk.

The **British Code of Advertising, Sales Promotion and Direct Marketing** provides clarification of what clear, fair and not misleading means to advertising in that context:

- **Honesty:** marketers should not exploit the credulity, lack of knowledge, or inexperience of consumers.
- **Truthfulness:** no marketing communication should mislead, or be likely to mislead, by inaccuracy, ambiguity, exaggeration, omission or otherwise. Marketing communications must not omit, hide or provide in an unclear, unintelligible, ambiguous or untimely manner any material information.
- **Fear and distress:** no marketing communication should cause fear or distress without good reason.

We believe these are good principles to apply in this context, and employers should seek to comply with these principles when communicating incentive offers to members.

Principle 2: Open and transparent

The offer should be open and transparent so that all parties involved in the process are aware of the reasons for the exercise and the interests of the other parties.

A number of people will be involved in the creation and structuring of an incentive offer, each with specific roles and responsibilities in designing and undertaking the exercise. The relationship of the parties involved should be accurately and openly communicated to all, including the nature and arrangements of that relationship. Reference to the regulator's guidance, the reason why the exercise is being undertaken, and the employers' long-term funding objectives for the scheme (eg to buy out the benefits over time) are all examples of transparency consistent with this guidance.

No undue pressure should be placed on individuals to accept an offer, and members should be provided with a reasonable amount of time to make an informed decision. In particular, the basis for remuneration of advisers should be clearly articulated, as well as the process used for selection of any adviser where services are offered.

Principle 3: Manage conflicts of interest

Conflicts of interest should be identified and appropriately managed in a transparent manner, and where necessary removed.

Conflicts can arise when parties involved in the exercise have multiple interests, either by being both a trustee and a director or employee of the employer or, for instance, where financial advisers are remunerated on the level of take-up of the offer.

Such a conflict can inhibit open discussions or result in decisions, actions or inactions that are not in the best interests of scheme members. This may lead to parties acting improperly, or a perception that the parties have acted improperly, resulting in invalid decisions or actions.

Step should be taken to manage any conflicts of interests effectively, and in every case they should be proactively identified, disclosed to relevant parties, and appropriately managed. This includes any partnerships, exclusivity deals, and adviser or broker incentives. For this purpose, please see the regulator's guidance on conflicts of interest available on our website.

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Principle 4: Trustee consultation

Trustees should be consulted and engaged from the start of the offer process, with any concerns addressed before progressing further with the offer process.

Trustees have an important role to play in ensuring that the interests of the scheme and its membership are properly addressed at all times. Consistent with their fiduciary duties and statutory obligations, trustees should question and challenge the appropriateness of an incentive offer and ensure it is in keeping with the principles of this guidance.

Owing to the need for meeting liquidity requirements of the potential take-up of any exercise, the trustees will also need to manage the scheme's investment, funding and cash flow through any cycle of membership or benefit change.

Principle 5: Independent financial advice

Fully independent and impartial financial advice should be made accessible to all members and promoted in the strongest possible terms; in almost all circumstances, the structure of the offer should require that members take financial advice.

Members of most pension schemes will not have, and should not be expected to have, sufficient knowledge to make an informed decision on their own, and steps should be taken to ensure they fully appreciate the risks involved.

Employers should ensure that fully independent and impartial advice is accessible to members, and the impartiality of that advice should not be compromised, so that members can make informed decisions as to what is in their interest, with clarity and understanding on what is an important and complex matter.

If the employer has any concerns about the scheme members' ability to understand the structure and implications of the offer, then it should pay for independent financial advice and require that members take advantage of this advice before making a decision. Each member should be able to choose whether he or she takes advice from any appointed adviser, or takes advice from one of his or her own choosing.

This advice will need to be tailored to the individual and their circumstances, and cannot be generalised for the membership as a whole or even groups of members.

The basis on which advice is remunerated, and who is paying for that advice, should be made clear to the member before it is provided.

It is in everyone's interest that members make the right choices, and that the decision-making process should not be adversely affected by conflicts arising, such as commission-based remuneration, or payment based on the level of take-up or the amount of reduction in scheme liabilities.

Trustees should, above all, ensure that they are comfortable that the selection, remuneration and broader commercial interests of the adviser are aligned with members' interests.

Financial advice should only be provided by those authorised to give advice on pensions by the FSA – see the regulator's **relations with advisers guidance**, available on our website. (Contact details for organisations who may be of assistance to employers, trustees and members are given in section 5.) Members need to understand the specific implications for their pension benefits in accepting the offer, and the complexity involved in understanding and advising in this area means that advice must only be provided by those deemed capable to do so.

FSA authorised advisers have a broad range of skills and expertise. Employers and trustees must ensure that the adviser selected for the task has appropriate qualifications and demonstrable expertise in advising members on the specific area of pensions.

Employers who wish to appoint advisers should consider a due diligence process for appointment to ensure that the adviser has the capacity and competence to advise members.

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Section 3: Problems and concerns that can arise for members

A member who is offered an incentive to transfer out of a scheme, or to agree to a rule change leading to a reduction in benefits, can be faced with a complicated financial decision.

In many instances it will not be within a member's retirement interests to accept enhanced transfer offers, but only the member can truly determine whether it is the right option for them.

For example, in the case of an incentive offer to transfer, the member will probably need to consider:

- whether the transfer value that he or she is offered represents good value for his or her DB scheme benefits;
- the type and likely amount of benefits the transfer value will secure under the scheme to which it is paid, and the likelihood of those benefits being provided; and
- the security of his or her benefits in the employer's scheme and the role of the Pension Protection Fund ('PPF').

In the case of an offer to accept a reduction in benefits, the member will need to consider how the incentive offer compares to the benefits being given up.

Members need to fully understand the implications of a decision to accept an incentive offer and in most cases impartial, independent and properly qualified financial advice will be crucial in making the right decision on that offer.

Some of the terminology used in pension literature can be very confusing for members. For instance, the words 'incentive' and 'enhancement' can suggest the member is getting good value for the level of benefit being forgone. This cannot be determined without further consideration.

There are many factors beyond the rate of investment return (critical yield) that the member will need to weigh up. These include assumption of longevity and annuity risk, the significance of the member's DB scheme benefit in overall retirement plans, and how they value their benefits and protections awarded under the DB scheme. Members will need adequate time and advice to consider these factors.

When accepting advice, members will be influenced by the employer's future intentions towards the scheme or, for instance, the basis of remuneration of advisers. Without clear and concise information, members may later feel unjustly treated, or that they have made the wrong decision by not knowing or understanding all the relevant facts.

Section 4: Key points of note when considering an incentive offer

Employers

Employers should be aware that:

- Incentive exercises are fraught with legal and reputational risks. Without the utmost regard and diligence to members' needs in this very complex financial decision, members' claims on the employer could be made many years after the exercise has taken place.
- Employers should consider how incentives to transfer or modify benefits present risks that may arise in their own specific circumstances. For example, selective offers to certain scheme members can carry a greater risk of one section of membership being advantaged over another. Any attempt to exploit the protection of the PPF is likely to attract sanction from the regulator.
- Cash incentives distort the members' decision making process in respect of their retirement provisions. The regulator finds it difficult to see how an offer involving cash incentives would lead to sound decisions being made.
- The Pensions Ombudsman can investigate complaints made by members about employers. When reviewing a complaint the Pensions Ombudsman will take this guidance, as well as other factors, into account in determining whether the employer is at fault. If the complaint is upheld, the Pensions Ombudsman can direct the employer to compensate the member accordingly. The Pensions Ombudsman's directions are enforceable in the same way as court judgements.
- When providing advice on incentive offers to members, employers should be aware that they have a duty of care and should ensure that advice is fair, accurate and not misleading.
- Incentive exercises can be very costly in nature, from taking the appropriate legal, financial, and actuarial advice to providing enhancements or incentives in order to offer fair value to the member in exchange for the benefits being given up. The costs may outweigh the perceived benefit of any such exercise.

- The regulator expects that an employer will not conduct an incentive exercise if it could have an adverse effect on the employer's ability to fund the scheme's deficit in accordance with the scheme's existing recovery plans.
- There are strict laws and provisions governing the modification and forfeiture of benefits under a scheme. This includes the scheme's governing documentation which sometimes contains relevant restrictions.
- Coercing or placing undue pressure on members to transfer or give up benefits held within their pension scheme is a serious risk to members' benefits and will result in action by the regulator.
- The regulator expects employers to make independent and fully impartial financial advice available to members, tailored to the members' individual needs.

Trustees

Key considerations for trustees:

- Trustees should start from the presumption that such exercises and transfers are not in the members' interests, and should therefore approach any exercise cautiously and actively.
- Fundamental to the trustees' role in administering a pension scheme are their duties of care and skill, and in particular their duty to act in the best interests of beneficiaries. The trustees should be mindful of this obligation throughout an enhanced transfer exercise because they must ensure members' interests are properly protected at all stages, and they may need to take active steps in order to meet their legal obligations.
- The trustees should engage with the employer from an early stage during a proposed incentive exercise. This will assist in satisfying the trustees (and keeping them satisfied throughout the process) that any offer made is in keeping with the principles of this guidance.

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Trustees continued...

- Trustees should already be alert to conflicts of interest or close personal relationships between employers and advisers, or trustees and advisers. Conflicts are a particular risk during enhanced transfer exercises, so trustees should identify and manage appropriately any conflicts of interests or potential conflicts of interest from an early stage.
- The trustees will need to ensure they understand the structure and process of the proposed enhanced transfer. This will enable them to recommend safeguards to ensure the members' interests are sufficiently protected and that the members properly understand the decision they are being asked to make. To alleviate any concerns about the scheme members' ability to understand the structure and implications of the offer, trustees should request that the employer pays for independent and impartial financial advice.
- A key role for trustees is to reassure themselves that the broader commercial interest, remuneration basis and process for selection of advisers does not militate against the likelihood of members seeking or receiving impartial advice.
- The trustees should have a clear understanding of their duties and legal obligations throughout the enhanced transfer exercise. The trustees are subject to requirements under legislation when calculating and providing transfers, as well as considerations under the scheme rules. Specifically, where an offer is made to a member who is being asked to give up an entitlement to certain accrued benefits through a modification of scheme rules, the trustees must ensure compliance with the provisions of Section 67 of the Pensions Act 1995 (in particular Section 67E – the trustee approval requirement, and the informed consent requirements). Trustees should therefore consider their legal position in any decisions they will be required to make, as well as their fiduciary duties more generally and whether or not this will require them to take action. If necessary, they should seek their own legal advice.
- The trustees have an ongoing legal obligation to establish and operate adequate internal controls. Therefore, to the extent that the employer fails to engage with the trustees, the trustees' ongoing maintenance of effective internal controls should ensure that the trustees are alert and able to identify potential enhancement offers by the employer at an early stage. For example, increased requests for personal data by third party advisers should alert trustees to a potential exercise.
- At the preliminary stages of structuring an enhanced transfer, the trustees may be asked to provide scheme data to employers or other advisers. The trustees should be mindful of their data protection obligations and be satisfied that they would not be breaching the relevant legislation if they were to release any personal information about members to employers, financial advisers, or any other third parties. If the trustees are uncertain as to their legal obligations, they should take their own legal advice in this regard before releasing the data.
- Trustees should consider the source of the employer's capital used to fund the incentive exercise and its effect on the employer's covenant including, for example, whether additional security has been given over the employer's assets in exchange for the financing.
- Trustees should also consider the implications of the employer's capital being used to fund any incentive exercise on the company's ability to directly repair any deficit in the scheme, and if necessary bring forward a formal scheme valuation.
- Trustees should ensure that the funding position of the scheme does not deteriorate as a result of any exercise.

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- Although the employer will communicate and/or manage communications to employees, in order to fulfil their duty to protect members' interests, the trustees should ensure that the communications to members are accurate and complete. This will include ensuring that:
 - members are presented with an offer they can properly evaluate;
 - employer's communications contain the key messages described in this guidance; and
 - based on the trustees' knowledge, the information to members is not misleading. For example, comments relating to the ongoing financial health of the employer should be reconciled with the trustees' own knowledge and information.
- The trustees should raise any concerns formally with the sponsoring employer and work with the employer to ensure those concerns are alleviated. This includes reviewing and commenting on the employer's communications to members.
- The trustees should at all times be mindful of their fiduciary duty to act in the members' best interests. Trustees are not expected to make members' decisions for them, but should ensure members are properly protected in making a decision on an incentive offer. Therefore, if the trustees consider that the information and or communications to members are insufficient to enable the members to make an informed decision, the trustees will need to consider what action to take to address this issue; they may wish to issue their own communication to ensure key messages reach members. In engaging with members, however, the trustees need to take care that they do not find themselves giving financial advice if they are not authorised to do so.
- If the trustees are unable to resolve concerns with the incentive exercise, they should seek their own legal advice and should consider raising any unreconciled concerns with the regulator in a timely manner.
- The Pensions Ombudsman can investigate complaints made by members about trustees. When reviewing a complaint the Pensions Ombudsman will take this guidance, as well as other factors, into account in determining whether the trustee is at fault. If the complaint is upheld, the Pensions Ombudsman can direct the trustee to compensate the member accordingly including personal redress on individual trustees. The Pensions Ombudsman's directions are enforceable in the same way as court judgments.
- Alternatively, a member may bring a claim against a trustee for losses arising as a result of a breach of duty by the trustee.
- Where an incentive exercise warrants review by the regulator, this review will take into consideration the trustees' involvement in the exercise. Where the regulator has concerns as to the ability of the trustees to act in accordance with their trustee duties and to demonstrate sufficient knowledge and understanding, this may result in a much wider review of the general administration and governance of the scheme. Where significant concerns exist in this area, the regulator has powers to impose sanctions on the trustees (such as the removal of trustees or the appointment of an independent trustee).

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Section 5: What to do if you have concerns

The organisations listed below may be of assistance to employers or trustees, and can be recommended to members with any information needs or concerns.

Contact **The Pensions Advisory Service** with any questions or concerns about an offer at:

The Pensions Advisory Service

11 Belgrave Road
London
SW1V 1RB

T 0845 601 2923

E enquiries@pensionsadvisoryservice.org.uk

W www.pensionsadvisoryservice.org.uk

Contact the **Pensions Ombudsman** if you feel you are or have been unjustly treated (their booklet headed 'What to do before you come to us', available on their website, should be consulted before making an official complaint):

The Office of the Pensions Ombudsman

11 Belgrave Road
London
SW1V 1RB

T 020 7630 2200

F 020 7821 0065

E enquiries@pensions-ombudsman.org.uk

W www.pensions-ombudsman.org.uk

Contact the **Financial Services Authority** with any concerns on regulated advice provided, or for more information on pensions and pension transfers generally:

Financial Services Authority

25 The North Colonnade
Canary Wharf
London
E14 5HS

T 0300 500 5000

W www.moneydeclar.fsa.gov.uk

Contact **The Pensions Regulator** with any reports of coercive, pressurising, or misleading behaviour or with any concerns regarding the structure or the conduct of parties involved in the exercise at:

The Pensions Regulator

Napier House
Trafalgar Place
Brighton
BN1 4DW

T 0870 6063636

F 0870 2411144

E customersupport@thepensionsregulator.gov.uk

W www.thepensionsregulator.gov.uk

As employers or trustees receiving professional advice: if you have concerns on the advice you are being provided, contact the adviser's regulating professional body, or in the case of financial advice contact the FSA.

Appendix: Examples of information to be included in offer

We have produced a list illustrating some of the information that it may be necessary to include in an offer that is consistent with our guidance principles. This list is for illustrative purposes only, and information provided in any exercise should balance the need to be open and transparent, whilst being clear, fair and not misleading.

This is not an exhaustive list and should not be used as a checklist to guarantee the offer complies with the principles of this guidance. It is likely that different and additional information will be required in the individual circumstances of your particular scheme, membership, and incentive offer.

Offers may include information to:

- explain the nature of the benefits being given up in exchange for the offer. In particular, where reductions in pension increases are involved, it should explain the potential loss in inflation protection;
- explain, where a transfer out of a DB scheme is involved, that the scheme which accepts the transfer value may not provide the same level of benefits;
- explain the protections offered where a transfer out of a DB scheme is involved. This should cover the protection afforded by scheme wind-up legislation, and that of the PPF in employer insolvency;
- explain, where a rule change leading to a reduction of benefits is involved, the likely cost of making good any forgone benefit;
- explain that there may also be tax implications for the member if he or she accepts a cash incentive payment;
- explain why the member should take independent financial advice before making any decision about the possible transfer-out of his or her benefits from the DB scheme or accepting a reduction of benefits, and provide a link to the website www.unbiased.co.uk to facilitate any wish for finding an adviser of their own choosing;
- explain, where a transfer out of a DB scheme is involved, that there are various risks that the member will be taking on, including investment risk, longevity risk and annuity risk, and that the member should ensure his or her independent financial adviser ('IFA') explains these risks to them;
- explain any limitations of the financial advice being made available to members, the basis for remunerating any financial adviser retained, and who is paying for that advice;
- where a transfer is being offered and the scheme is in deficit, state the amount of the reduction applied to the member's transfer value and when the trustees expect the scheme to be in a position to offer full and unreduced cash equivalent transfer values;
- specify the amount being offered to the particular member concerned;
- say whether the incentive is a cash payment (and if so how and when it will be paid), an increase to the transfer value that would otherwise be paid by the scheme, or a combination of these, and whether the member is able to pick and choose from these options;
- say if the amount offered is affected by any member choice (for example, if the member chooses to accept a cash incentive instead of an enhancement to the transfer value);
- say how long the offer will be open;
- say why the employer is making the offer, and disclose any longer term plans for the scheme. It would be helpful if the impact that acceptance would have on the employer's accounts could be quantified in relation to the particular member concerned;
- make clear that the member does not have to accept the offer and that the member can retain his or her benefit entitlement under the scheme. The communication to the member might also usefully outline the consumer protection available to the member under the law with this type of financial transaction; and
- recommend and direct members to the relevant pages of The Pensions Advisory Service website www.pensionsadvisoryservice.org.uk, and recommend that members use this free and impartial service to address any questions or concerns they may have.

How to contact us

Napier House
Trafalgar Place
Brighton
BN1 4DW

T 0870 606 3636

F 0870 241 1144

E customersupport@thepensionsregulator.gov.uk

www.thepensionsregulator.gov.uk

www.trusteetoolkit.com

Consultation document

Guidance on transfer incentives

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