Since we issued our last Member Options Survey in November 2012, there has been significant activity and the outlook is that this is set to continue. The Industry Code of Practice (“Code”) was issued in June 2012 (and endorsed by DWP and the Pensions Regulator) and has provided a clear framework for the implementation of these exercises. This note is not a full market review but provides an update on developments in the market since our Survey and considers exercises since the Code, most of which were executed throughout 2013. The options provided to different groups of members will largely depend on their age (see Figure 1).

**Figure 1:** Options relevant to different groups of members

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Enhanced Transfer Values</th>
<th>Flexible Retirement Option</th>
<th>Pension Increase Exchange</th>
</tr>
</thead>
<tbody>
<tr>
<td>25-29</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>30-34</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>35-39</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>40-44</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>45-49</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>50-54</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>55-59</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>60-64</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>65-69</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>70-74</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>75-79</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>80-84</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>85-89</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>90-94</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
<tr>
<td>95-100</td>
<td>Non-pensioner</td>
<td>Pensioner</td>
<td></td>
</tr>
</tbody>
</table>

**SUMMARY**

**Pension Increase Exchange**

Pension Increase Exchange (“PIE”) exercises are continuing to be popular, with post Code take up rates averaging at 30%. The majority of these exercises have been run below “Balanced Deal” and there is an increasing trend for the option to be embedded at retirement.

**Flexible Retirement Option**

Also known as TPIE (Total Pension Increase Exchange), these exercises are growing in popularity with trustees and sponsors alike. Post Code take up rates are averaging at 25% and, again, there is an increasing trend for the option to be embedded at retirement.

**Enhanced Transfer Values**

We are seeing fewer Enhanced Transfer Value (“ETV”) exercises but for those that have been run, this has been driven by specific scheme/sponsor considerations. Typically the exercises are being designed on a more targeted basis (i.e. targeting specific groups, such as those with the highest liabilities).

**Market outlook**

Both we and a number of Independent Financial Advisors (“IFAs”) are anticipating that the increase in the number of exercises may lead to capacity constraints during 2014. Early engagement with IFAs and robust project management will, therefore, be critical to the successful completion of exercises.
**Pension Increase Exchange ("PIE")**

Offered to members who are currently receiving their pension (including spouses of deceased members), PIE allows members to exchange future non-statutory increases in return for an additional non-increasing pension (see Figure 2). This provides additional benefit flexibility that may better meet their lifestyle needs (e.g. providing a greater income when they are younger and have more financial commitments).

Whether guidance or full financial advice needs to be provided to a member considering a PIE offer depends on what proportion of the value of pension increases is passed onto the member in the form of additional pension (the “Balanced Deal Percentage”). If the Balanced Deal Percentage is under 100% (i.e. less than full value is passed to the member), then full advice must be made available to the member, with a recommendation on whether or not to accept the offer.

Since the Code was introduced, we are aware that some exercises have had a Balanced Deal Percentage of 100%, although our experience is that non-Balanced Deals remain the norm. Take up rates do not appear to be significantly impacted by the offer being a Balanced or non-Balanced Deal. Figure 3 shows the IFA engagement rates (i.e. the proportion of members contacting the IFA on receipt of the offer) and member take up rates (i.e. the proportion of members accepting the offer). The exercises included in this update cover more than 100,000 members and all were carried out post Code.

**Potential Benefits of PIE:**
- Additional benefit flexibility for members
- Reduced pensions risk by removing inflation link on exchanged pensions
- Reduced funding and accounting deficits
- Reduced pension costs in the accounts (P&L credit)
- Reduced buy-out costs

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**Figure 2: PIE example**

Source: KPMG analysis
Note: Assumes a starting pension of £10,000, of which £5,000 is available for pension increase exchange

**Figure 3: Engagement and take up rates for PIE exercises post Code**

Source: KPMG analysis
Flexible Retirement Option (“FRO”)

Offered to members who are eligible to retire early (typically those over age 55), FRO allows members to select a more flexible range of benefits tailored to personal circumstances (e.g. higher tax free cash, pensions with or without increases and with or without contingent spouse’s benefits) by purchasing an annuity with an insurance company (see Figure 4).

FRO exercises are proving popular with both trustees and sponsor alike; trustees see the benefits of an improved retirement process for their members whilst providing greater benefit flexibility and reducing the overall size and risk of the scheme. Importantly, this exercise does not require members to take any investment decisions and does not typically require any top ups (as is often the case for a conventional Enhanced Transfer Value exercise).

Potential Benefits of FRO:
- Additional benefit flexibility for members, including higher tax free cash
- Cost effective discharge of pension liabilities and risk (interest, inflation and longevity)
- Typically reduces funding deficits
- Final opportunity to discharge liabilities below buy-out

Figure 5 shows engagement and take up rates for FRO exercises post Code. The exercises included within this update cover more than 2,000 members.

Figure 4: FRO example

From the scheme

<table>
<thead>
<tr>
<th>LUMP SUM ON RETIREMENT</th>
<th>ANNUAL PENSION FOR LIFE</th>
</tr>
</thead>
<tbody>
<tr>
<td>£9,400</td>
<td>£15,000</td>
</tr>
</tbody>
</table>

Flexible Retirement Options

<table>
<thead>
<tr>
<th>LUMP SUM ON RETIREMENT</th>
<th>ANNUAL PENSION FOR LIFE</th>
</tr>
</thead>
<tbody>
<tr>
<td>£15,000</td>
<td>£2,100 (Per annum) No increases</td>
</tr>
<tr>
<td>OR</td>
<td>£2,250 (Per annum) No dependant provision &amp; no increases</td>
</tr>
<tr>
<td>OR</td>
<td>£2,700 (Per annum) Impaired life, no dependant provision &amp; no increases</td>
</tr>
</tbody>
</table>

Source: KPMG analysis

Figure 5: Engagement and take up rates for FRO exercises post Code

%age

<table>
<thead>
<tr>
<th>Exercise 1</th>
<th>Exercise 2</th>
<th>Exercise 3</th>
<th>Exercise 4</th>
<th>Exercise 5</th>
<th>Exercise 6</th>
<th>Exercise 7</th>
<th>Exercise 8</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>20</td>
<td>30</td>
<td>40</td>
<td>50</td>
<td>60</td>
<td>70</td>
<td>80</td>
</tr>
</tbody>
</table>

Source: KPMG analysis

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Enhanced Transfer Values ("ETV")

Pension legislation gives deferred members the option to transfer their benefits out of a scheme into an alternative pension arrangement.

ETVs are typically offered to deferred members who are under age 55. The sponsor offers to increase the standard transfer value available to members (for a limited period of time), to encourage members to transfer their benefits to a defined contribution scheme and reduce pension scheme risk (see Figure 6). The logic is that improved transfer terms will be attractive for some scheme members.

One of the key changes introduced by the Code for ETVs is that enhancements should be included as part of the transfer amount, rather than as an optional cash lump sum payable directly to the individual.

**Figure 6: ETV example**

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**Potential Benefits of ETV:**
- Additional flexibility for members
- Discharge of pension liabilities and risk (interest, inflation and longevity)
- Reduces buy-out and possibly funding deficits

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