

Potential change to Retail Price Inflation (RPI) will impact member options now



What you **need to know**

- A Government consultation will be launched with the Budget on 11 March on aligning RPI inflation with CPIH inflation between 2025 and 2030.
- If aligned, this will directly impact on any member benefits that increase in line with RPI. This will not immediately flow through to benefit increases now. The earliest that increases can be impacted is 2025.
- Members are however realising the value of their future increases when they take options from schemes today such as cash, transfers or pension increase exchanges.
- Assumptions being made for future inflation expectations are more likely to be different to future experience depending on if, when and how a change to RPI is made.
- Members taking options now may therefore end up being a winner or a loser.



Actions you can take

- **Assess** member benefits in the scheme and identify those linked to CPI and RPI inflation.
- **Review** member options available in the scheme and which terms will be materially impacted.
- **Decide** for each option whether to maintain terms, review terms or withdraw the option temporarily.
- **Reconsider** the feasibility of any bulk member option projects.

Possible impact on member options

Option	Degree of risk	What do we expect for most schemes?
Transfers		Likely review of terms
Tax free cash		No review of terms
Trivial commutation		Possible review of terms
Pension increase exchange		Possible review of terms or suspend option temporarily
Early or late retirement		No review of terms

 High risk  Medium risk  Low risk



The finer detail: Member options

Brief on the member option impact of the possible alignment of RPI with CPIH.

Recent views on RPI	The UK Statistics Authority believes RPI is a flawed measure and should be aligned with CPIH, or better still, removed altogether. A report on 17 January 2019 from the House of Lords supported this view.
Recent developments	The UK Statistics Authority needs the approval of the Chancellor to change RPI before 2030. On 13 January 2020, the Chancellor confirmed that the Government consultation on aligning RPI inflation with CPIH inflation between 2025 and 2030 will be launched with the Budget on 11 March.
Impact on CPI	The change does not affect CPI but may affect CPI assumptions used in calculating member options because these are typically set as a fixed deduction to RPI.
Transfer values	Members have a statutory right to transfer so it is hard for trustees to suspend or delay transfers to await more clarity. Transfer values must be a best estimate of the cost of providing benefits. Uncertainty on RPI creates a challenge in setting transfer value assumptions for both RPI and CPI increases.
Tax free cash	Most schemes fix tax free cash terms for a number of years. As such, the impact of possible inflation changes may be outweighed by changes to gilt yields and life expectancy. There is also no explicit requirement for tax free cash to be best estimate. Schemes with CPI pension increases should check assumptions provide fair value.
Trivial commutation	Terms can be either market related, like transfer values, or fixed terms, like cash commutation, so the considerations are similar. Given the benefits are by nature small, trustees may not feel the need to prioritise updating these terms.
Pension increase exchange	Many schemes allow members to exchange future pension increases for a higher fixed pension. This can involve exchanging future inflation increases. It is possible that terms will no longer represent fair value unless they are updated. If the terms are not updated, communications to members may be misleading in the way they describe the value that has been provided for future increases. Trustees who offer this should review whether to put this choice on hold, update the terms or amend communications.
Early or late retirement	Terms for these options are often not sensitive to price inflation. We do not anticipate trustees reviewing these terms solely due to possible RPI changes.
Bulk exercises	Trustees and sponsors should pause to reflect if they are about to engage members in a project to promote options such as a transfer or retirement exercise. If terms are not considered carefully, the consequences of paying higher or lower values to members may be significant given possible large take up. In some cases, it may be preferable to postpone an exercise until there is more certainty on RPI inflation.

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