PML GROUP
Pensions Management
& Financial Services

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In this issue we focus on:

- Pension Freedom and Transfer Options
- Transfer Enquiries – Act Soon

Pension Freedom was, in the Chancellor's words, "the first step in the Government's radical plan to change the tax treatment of defined contribution pension schemes, to bring them into line with the modern world" to ensure that, next year "over 400,000 hardworking people will have new choices about how to invest and spend their hard-earned retirement savings".

Pension Freedom and Transfer Options

Setting aside the political mantra within these statements, we confess that we're unashamed supporters of 'pension freedom' – and indeed of any initiative that eases the constraints that bear down on pension fund investment and pension benefit uplift. As a pension providing nation we've tumbled over the last 25 years from being the envy of Europe to 'also ran' status. With successive Governments to blame for much of this decline, we warmly welcome this change of course - and will celebrate when it finally arrives. The combination of 'Auto-Enrolment' and 'Pension Freedom' will do much to put us back on the road towards the honest accumulation of sensible retirement provision.

There's no doubt that the ability to control one's own pension fund and to boost the fund with wholly tax relieved contributions are key to the regeneration of interest in pension saving. These twin benefits are however limited to private sector 'defined contribution' arrangements. Employees in the public sector already enjoy the unique advantages that lie within their Defined Benefit (final salary) schemes. And here is where the law of unintended consequences has unexpectedly lifted its head. Growing numbers of Defined Benefit scheme members are actively investigating their Cash Equivalent Transfer Values (CETVs) in recognition that a fully exiting transfer option may shortly be denied them. Are they right to worry – and would they be right to consider a transfer?

On the worry front, there's little doubt that the Government will seek to close down the option to remove benefits by transfer, from a public service Defined Benefit Scheme. The Chancellor promised as much in his Budget announcements. But for most in public sector schemes, the combination of Treasury guarantees, inflation-proofed final benefits and rock-bottom CETVs represent a huge disincentive to any transfer action. The prospect of a permanent lock-in and the loss of the freedom to transfer-out might initially appear disadvantageous – but for most, could be best compared with the removal of the freedom to self-harm! Yes, exceptional circumstances will always arise but excluding these, the 'fix' to be enjoyed from accessing a pension fund that had hitherto remained obscure and remote, is a misguided and woeful choice, when considered against the quality of the benefits surrendered. And such a decision is too important to be influenced by a fear of 'missing out' on a transfer opportunity that will shortly be denied.

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Transfer Enquiries – Act Soon

For those with entitlements within private sector Defined Benefit Schemes, the Chancellor has been less prescriptive. At the moment, members with retained benefits in private sector schemes have the right to a Cash Equivalent Transfer Value – and have the ability to transfer the value of their benefits to any other registered scheme arrangement. For scheme members who are no longer in service but with benefits retained within a former employer's scheme, the 'stay or go' decision demands careful consideration of the mathematics employed in the CETV calculation, the composition and structure of the benefits surrendered, the funding position of the host scheme and the circumstances and aspirations of the member and his family.

Transfer action is not to be taken lightly – and must only be pursued under the advice and guidance of a qualified adviser. That said, the transfer of benefits from a private sector Defined Benefit Scheme may often be attractive to the member – and the 'pension freedoms' that are expected to be conferred by Government seem likely to accelerate interest in private sector scheme transfers.

Now although all private sector schemes are 'funded', the adequacy of that funding is dependent upon multiple economic factors and assumptions. A member's CETV is intended to reflect both the actuarial assumptions that have been made and the prevailing funding position of the scheme. The current economic climate of minimal interest rates and low gilt yields should in theory drive up transfer values – but the persistence of low yields and minimal returns has played havoc with scheme costings and undermine scheme funding levels – with a consequentially depressing effect upon quoted CETVs.

These circumstances are acknowledged by the Chancellor in his recognition of "the danger that lurks within any large-scale private sector scheme transfer action". He went on to say that "such developments would not only place many private sector schemes under pressure but could also impact upon the wider economy. The Government has therefore decided to consult on the matter and will pronounce both its findings and its intended action later in the year".

At the moment, although we're still 9 months away from Pension Freedom, we have no way of knowing the extent to which Defined Benefit Scheme members will have their transfer rights withdrawn, restricted or left unchanged. Nevertheless it looks as though those planning to exit their benefits from a Defined Benefit Scheme should start their enquiries now – and so ensure there's sufficient time to weigh up the options and make an unhurried decision.

And if that decision is to 'stay', then the member, with an eye to the future should look again at the shortcomings of their pension funding, close the gap with fresh Pension Freedom qualifying, tax relieved pension contributions – and the best of both worlds will be enjoyed!

Please contact us for more information on this important issue (0121 693 0690 or info@pmlgroup.uk.com) – we're here to help.

Geoffrey Stait
25 June 2014