RobMac Independent Financial Planning and Mortgage Management

Making the best choice for your pension

A GUIDE TO THE PROS AND CONS OF WHETHER TO TRANSFER YOUR PENSION OR NOT

introduction - the world of pensions is changing

In the past, many people who worked for private firms built up a company pension based on how long they had worked for the firm and how much they earned. The amount of pension they would get was guaranteed by the rules of the pension scheme, and so they were known as defined benefit or DB pensions. These defined benefit pensions have a number of advantages.

- Your pension lasts as long as you do, so there's no danger of you running out of money.
- There is something for a surviving spouse after you die. The details vary from scheme to scheme but survivors' pensions of half of the scheme member's pension are common.
- There is some measure of protection against inflation, which helps to maintain the spending power of your pension. Again, the exact provision varies from scheme to scheme, but there is a legal minimum which all schemes have to deliver.
- Your pension is unaffected by the ups and downs of the stock market.

Despite all of these advantages, there are some downsides to having a pension of this sort, such as a lack of choice over when and how to take your pension. So, growing numbers of people are considering whether to exchange their DB pension rights for a cash equivalent.

The purpose of this guide is to provide some basic factual information about the pros and cons of making a transfer of this sort, so that you are better informed prior to seeking impartial and expert financial advice about your individual circumstances.

However, it is important to stress that, because of the attractive features of DB pensions, the Financial Conduct Authority (FCA) tells financial advisers to start from the assumption that it is not in people's interests to exchange their DB pension rights for a cash alternative[1].

Growing numbers of people are being offered very large cash sums in exchange for giving up all of their rights in their DB pension scheme. These cash sums can be used in two main ways:

- for those who are still saving for their retirement, the cash sum can be transferred into a personal pension where it will be invested, or

[1] A good place to start is the FCA page on pension transfer https://www.fca.org.uk/consumers/pension-transfer, which says: "In most cases you are likely to be worse off if you transfer out of a defined benefit scheme, even if your employer gives you an incentive to leave. The cash value may be less than the value of the defined benefit payments to you and your eventual pension payments will depend on the performance of the new scheme, with the risk that the scheme does not deliver the returns that you expect". The FCA website does however point out that "there are risks to staying too".

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- for those who want to start living off the proceeds of their pension, it can be transferred into a drawdown account, where some of the money is invested and some is taken out either in lump sums or as a regular income.

In both cases, there is no guarantee as to the future level of income, and the only thing that is defined is the contribution going in to the scheme. For this reason, such arrangements are known as defined contribution or DC schemes.

Two particular factors have led to a growing interest in converting DB pension rights into cash lump sums which can be invested in DC pension arrangements.

First, in 2015 new pension freedoms were introduced which give you more choice over what you can do with your DC pension pots. Instead of having to buy an annuity which would provide you with an income for life, you can now choose to access your pension pot and draw an income from it when you need it. As part of these reforms, the inheritance tax treatment of money held in DC pension pots was made much more attractive.

Second, the low interest rate environment of recent years has meant that the transfer values being offered in exchange for DB pension rights have soared to record levels. This mainly reflects the fact that it is now costing DB schemes a lot more to meet the pension promises that they have made.

For all of these reasons, interest in DB to DC transfers is increasing, with advisers and schemes reporting growing numbers of scheme members asking for valuations and seeking advice.

There are a few things to be aware of at the outset.

- DB to DC transfers are irrevocable – you cannot change your mind a few months or years later even if you wish you hadn't made the transfer.
- In general, once you have started receiving benefits from your DB pension scheme you cannot then give them all up in return for cash. However, occasionally a scheme will offer you a deal where some of your pension benefit can be given up in return for a lump sum.
- There are some types of DB pension schemes where cash transfers are not possible. These are mainly public sector schemes such as those for nurses, teachers and civil servants. The reason for this is that there is no pension 'fund' – the pensions of today's retired workers are paid for out of the contributions by today's workers and their employers.

The law requires that if you wish to transfer a DB pension pot valued at £30,000 or more you must seek financial advice before doing so[2], and rightly so. These are valuable pension rights and they should not be given up lightly. Any decision about what to do with them should be made on an informed basis and few individual savers would have the necessary expertise to make that judgment. So we strongly support the requirement to take advice before giving up significant DB pension rights. This advice can also look at the whole of an individual's pension rights which may lie in

[2] The rules on which transfers must be made with advice are slightly more complex than this but a scheme would be expected to tell a member if advice is required before the transfer of their particular rights can take place. The current FCA rules are set out in Policy Statement PS15/12: https://www.fca.org.uk/publication/policy/ps15-12.pdf

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several schemes and be a mixture of DB and DC rights. This guide is not designed as a substitute for impartial, tailored financial advice.

What this guide does seek to do however is simply to help you in the early stages of considering a DB to DC transfer by familiarising you with some of the key issues that you will need to take into consideration. This will hopefully lead to a more informed conversation with your adviser if you decide to proceed to the next stage. The guide seeks neither to encourage nor to discourage such transfers, but rather to set out in a balanced way the pros and cons of retaining your DB pension rights as compared with taking a transfer.

Our second purpose is to offer some thoughts on how the process could work better for the general public and for those who advise them. We explain the current regulatory regime around advice on transfers and argue that it needs to be updated in light of the new pension freedoms. We also argue that the current choice between transferring all of your pension rights and none of them is too black and white. We make the case for giving people the option of a partial transfer, leaving some of their rights within their DB scheme and transferring the remainder as a cash sum. We believe that this could produce better outcomes for some consumers than the current, rather polarised, options open to them at present.

the current system

At present, if you are a member of a DB pension scheme you have the right to ask the scheme to offer you a cash lump sum in exchange for your entire DB rights[3]. This lump sum is known as a cash equivalent transfer value (CETV).

If the transfer value is more than £30,000 you are required to seek independent financial advice before deciding whether or not to proceed with the transfer. This advice must be provided by, or at least checked by, a specially-qualified pensions transfer specialist.

In order to provide advice on the suitability or otherwise of the transfer, the adviser must undertake a "Transfer Value Analysis"[4]. The central idea here is that the adviser will look at the cash sum which is being transferred, assess how much that sum might grow to by scheme pension age and calculate the income for life that could be bought with that pension pot. This can then be compared with the pension that would have been paid had the scheme member remained in the DB pension scheme.

Advisers will often talk about assessing a potential transfer with reference to a critical yield. The critical yield is the investment return that would be needed on the transferred sum to build up a large enough pot at retirement to buy retirement benefits at least as good as the DB pension given up.

In many cases, to achieve a pension pot large enough to buy an income for life of equal value to the DB pension foregone will require a relatively high rate of return which in turn would imply taking a high degree of investment risk. Whilst this is not an absolute bar to an adviser recommending a transfer, many advisers would be nervous about recommending a transfer in such a situation. However, as we discuss later in this guide, this is not the only consideration – or even necessarily the most appropriate one – when deciding whether or not a transfer would be in your interests.

If an adviser concludes that a transfer is not in your interests, this is not necessarily a barrier to the transfer taking place. If you are insistent that you wish the transfer to go ahead, some advisers will implement the transfer in any case, stressing that this is not in line with their advice and that you need to accept responsibility for this decision. Others will simply decline to facilitate the transfer and you will need to go elsewhere. This is something worth exploring with your adviser before starting the process.

[3]This right does not apply to members of 'unfunded' schemes such as those in the public sector for teachers, nurses, civil servants and others, as there is no 'fund' to transfer.

[4]The automated system which uses the FCA's standard assumptions to evaluate transfer values is known as 'TVAS' or the Transfer Value Analysis System.

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Of course, there is still likely to be a cost for the work that has been done even if the recommendation is not to transfer. In this case, if the consumer proceeds on an 'insistent' basis, the adviser fee can be deducted from the value of the transfer or the consumer can pay a fee directly to the adviser. If the consumer accepts the recommendation they will have to meet the cost of the advice from their own resources. The prospect of paying from one's own pocket may act as a further incentive towards going ahead with the transfer.

In the next two sections we consider some of the reasons why turning DB pension rights into cash might be a good idea for some, and then some of the reasons why others might be better advised to keep their pension rights where they are.

five good reasons to transfer

1. Flexibility

Whilst DB pension rights can be very valuable and attractive, they can also be rather rigid and inflexible. For example, a scheme may have a set pension age and although taking an early pension may be possible, it may not be on favourable terms. In this case, taking your pension earlier may mean it is much lower than if you had waited until you reached pension age. Similarly, a scheme may have generous arrangements for married members who leave behind a widow or widower but these may be of no value to unmarried members of the scheme.

If you convert your DB pension rights into cash and put the money into a DC pension instead, then you benefit from the new pension freedoms which allow you much more choice about how you use your money. In addition, the cash amount that you are offered will generally reflect the average cost to the scheme of providing benefits to widows and widowers, so if you are a single person you will get some of the value of that provision which you would not have done if you had stayed in the scheme[5].

In terms of flexibility, those aged 55 and over can now generally access their DC pension pot as they wish. So if you wanted to retire at 60 and live off your savings you could do this with a DC pension whereas you might have had to wait until you were 65 if you had stayed in the DB scheme. Of course, transferring the money does not mean it will last any longer (and indeed if the valuation of the rights is done on a cautious basis you may be losing some value when you transfer). So although you can take your pension earlier under a DC arrangement, you will be spreading the value of your pot over more years than if you had waited until the scheme pension age under the DB arrangement.

Another important aspect of the increased flexibility following a transfer is that you can decide how you want to spread your income and spending through your retirement rather than having a rigid amount throughout. For example, you may take the view that you want to spend more in earlier retirement while you are more mobile and able to travel, and spend less later in retirement, and having a DC pot to draw on enables you to make choices of that sort.

2. Potential for access to more tax-free cash

Whilst income from a private pension is subject to income tax, most pensions allow you to take one quarter in the form of tax-free cash. In a DB pension this usually means you get a cash lump sum at retirement plus a lower regular pension than if you had not taken the cash[6]. In a DC pension you can generally take one quarter of your pension pot as a tax-free cash lump sum provided you are aged 55 or over.

One reason why a transfer to a DC arrangement may be attractive is the potential to draw a larger tax-free cash lump sum than if you remained in the DB scheme.

If you stay in a DB arrangement you can generally give up a quarter of your pension rights in exchange for a tax-free lump sum. However, the value you get is generally less than a quarter of the value of your pension. This can be for a number of reasons. These include the fact that:

- schemes have varying rules for how the pension you have given up is converted into an equivalent lump sum and in some cases these can be very ungenerous,

[5]Of course, if you are married, the opposite argument would apply.

[6]Some DB schemes are designed by default to give you a lump sum plus a regular pension and may not have the option to take the benefits exclusively as a (larger) regular pension with no lump sum.

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especially in today's low interest rate environment.

- the process of converting from a regular pension to a lump sum is based on the scheme member's pension only but the rights given up include a potential pension for a widow or widower.

- complex tax rules can mean that the size of the lump sum is reduced relative to the amount of pension given up.

One way of thinking about these rates for converting pension foregone into a lump sum is to think about how long you are likely to live[7]. Suppose you expect to live for 20 years and are giving up a pension of £250 a month or £3,000 a year. Over the next 20 years you would receive £3,000 times 20 or £60,000 in pension (excluding the effects of inflation). So if the DB scheme offers you a tax-free lump sum of less than £60,000 you might feel that you are not getting a good deal.

An alternative would be to withdraw your entire DB pension rights and transfer them into a DC arrangement. Once the money is in a DC arrangement (and assuming you are aged 55 or over) you can then take one quarter of the whole pot as a tax-free lump sum and this is likely to be a larger figure than under the DB arrangement. If tax-free cash is particularly important to you, there may be some advantages to transferring out, especially if your scheme is one which offers relatively ungenerous tax-free lump sums within the scheme[8].

3. Inheritance

Whether or not it makes sense to stay in your DB scheme may depend in part on who will be left behind after your death and to what extent you want to support them financially. Recent changes in the tax rules on inheritance of certain sorts of pensions have made it more attractive to consider having your pension rights outside the existing DB scheme.

If you remain a member of your current pension scheme then when you die there may be a pension for your surviving widow or widower. If you die very early (perhaps a few years into receiving your pension) your widow or widower may benefit from a guarantee period where the full pension has to be paid for a minimum of (say) five years.

If you are part of a couple but not married, those rights may be more limited but this will vary from scheme to scheme and may be at the discretion of the scheme trustees. And there may also be some pension entitlement to any surviving dependants such as children of school age.

Whilst such provision is welcome and valuable, it does mean that in many cases when you (and perhaps your widow/widower) die, your pension dies with you. In particular there is nothing left to pass on to your heirs and successors.

An alternative is to convert your DB pension rights into cash and then transfer the money into a pension (if you are still saving) or a drawdown arrangement. In this case, if you were to die, the value of the assets in the pension or investment could pass on to your heirs. One particularly important consideration is the tax treatment of such money. Under recent changes, if

[7] A good place to check is the Office for National Statistics website entitled 'How long will my pension need to last' — http://visual.ons.gov.uk/how-long-will-my-pension-need-to-last/

[8] Note that the amount of tax-free cash is potentially larger if you immediately take 25% following the transfer. If you simply put your transfer value into a DC pension some years before retirement then whether or not you get a larger tax-free lump sum depends on the investment performance of the funds between the transfer and when you take the lump sum.

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you die before the age of 75, then the cash balance left behind can be received by your successors completely tax free. Even if you die over the age of 75 then whoever inherits your pot only has to pay income tax in the usual way when they make withdrawals. Furthermore, if your successors do not draw on this inheritance (perhaps because they already have sufficient income) then it can be passed on to subsequent generations[9].

4. Health

One of the advantages of a DB pension is that it lasts as long as you do.

But what about people who think – or know – that their life expectancy is likely to be on the short side? For example, if you draw a pension at 65 and die at 71 then you will not have got much out of the pension scheme compared with someone who lives well into their nineties. DB pension schemes work by pooling risk, and in effect those who live for the longest time are subsidised by those who live for the shortest time.

If you think you might be one of those whose life expectancy is below average then you might consider taking a transfer out. The value you are offered should (broadly) reflect average life expectancy and this may be a bigger amount of money than the amount it would have cost the scheme to pay your pension if you had stayed in but died relatively young.

If you take your money out in this situation you could simply invest it with a view to your heirs receiving the cash when you die. Alternatively, if you are not concerned about leaving anything behind after you are gone you could buy something called an enhanced annuity. This is basically an income for life, but one which takes some account of your likelihood of dying prematurely. So, for example, someone who has been a chain smoker all their life or who has a serious medical condition might be able to get a relatively generous annuity rate because the annuity provider does not expect to be paying the annuity for very long. One option would be to obtain a transfer value quotation from your current scheme and then find out what annuity you might be able to buy before actually making the transfer. You could then form a view as to which option would give you the better value.

5. Concerns about the solvency of the sponsoring employer

If the employer who sponsors your final salary pension scheme is at risk of becoming insolvent, then there is a chance that you might not get all of the pension you were expecting. But if you transfer out of the scheme then your investment fund will be unaffected by what subsequently happens to your ex-employer's business.

The way the system works is that if the firm that stands behind a DB pension scheme becomes insolvent, and if the pension scheme is well short of the money it needs to pay all of its future pension promises, then the scheme will be transferred into an insurance-type lifeboat arrangement called the Pension Protection Fund (PPF).

Under the rules of the PPF, those who have already reached the normal age for drawing a pension by the time of the insolvency will get 100% of their pension paid by the PPF, whilst those who are under the scheme's pension age will get 90%. Note that what matters is your age relative to the scheme's pension age and not whether or not you have retired.

[9]It is worth noting that if you die within two years of a transfer, your adviser or representatives may be expected to prove that they did not know your death was imminent. If they cannot do so, the favourable inheritance tax treatment of the remaining pension pot may be called into question.

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In addition to the reduction for those under scheme pension age, there are several other reasons why the pension you get from the PPF may be lower than the pension you would have got had the employer remained in business.

- The PPF only provides annual inflation protection in respect of years of service since 1997. This is because this is the minimum required by law but if your scheme had more generous rules (for example, giving you inflation protection for all your service) then you may get a series of smaller annual increases through your retirement.
- The PPF uses the Consumer Prices Index (CPI) as its measure of inflation when setting pension increases. Some schemes use the generally higher Retail Prices Index (RPI). Over time this could make a significant difference to how much pension you get.
- For those with the highest pension entitlements, the PPF applies a cap if you enter the PPF below scheme pension age. The cap in 2016/17 is £37,420.42 which equates to £33,678.38 when the 90% level is applied. The cap is reduced further if you started to draw your scheme pension early (ie before normal scheme pension age)[10].

For all of these reasons, if you think that your employer might not still be in business in a few years' time and might leave the pension fund with a significant shortfall, it might be advantageous to consider moving the cash equivalent value of your current pension rights into a pension fund of your own.

[10]There are plans to increase the cap on a sliding scale for those who have more than 20 years' service in the scheme in question.

five good reasons not to transfer

1. Certainty

One great advantage of having a DB pension is that it lasts as long as you do. If you happen to live longer than average then it is the scheme that has to find the money for this.

By contrast, if you transfer your DB pension rights into cash and manage it yourself, you are taking on the uncertainty about how long you are going to live. There is clear evidence that people tend to under-estimate how long they will live, so there is a risk that you will run out of money prematurely. On the other hand, you may be so worried about running out of money that you draw down the money too slowly and do not enjoy the full benefit of your retirement savings.

You could overcome this uncertainty by buying an income for life (an annuity) but for various reasons this is very unlikely to be as good as the pension you have just given up in your DB pension scheme. Indeed, if all you want is a guaranteed income for life then it is hard to see why you would have left your DB scheme in the first place.

It is more likely that you will go on investing your money and drawing an income from your fund, and the big unknown is how quickly it is safe to withdraw money.

There are, of course, things that you can do to manage this risk. For example, if you use the services of a financial adviser, they can help you to review your investments and your withdrawal rate and make adjustments if you are running down your pot too quickly[11].

Whether you are concerned about running out of money too quickly, or about having to be overly cautious about the rate of withdrawal, it is important to understand that these are not problems you would have if you left your money in your DB scheme.

2. Inflation

In these days of inflation close to zero, it is easy to forget that over a retirement which could last 20 or 30 years, the value of having an income which has some protection against rising prices could be considerable.

Within your DB scheme the extent of protection against inflation which you enjoy will depend on the rules of the scheme and on when you were a member of the scheme.

To give an example of the importance of inflation protection, let us assume that inflation runs at 2% a year, that your entire DB pension rights are guaranteed to rise by this much, and that you have a 20 year retirement. If your starting pension at retirement was £100 a week, it would be £148.59 by the end of your retirement. Without inflation protection you would still be getting £100 a week – a final pension nearly one third lower.

Clearly the cash transfer value that you are offered will reflect the value of the inflation protection built in to your pension scheme. But once you have taken the cash, all of the inflation risk falls to you. If, for example, inflation were to reach 4% then in the DB scheme your pension would rise by at least 2.5%, and possibly more. So the real year-on-year fall in the value of your pension would only be around 1.5%. But with a DC pension pot a 4% rise in the price of goods represents a 4% fall in your standard of living.

[11] For Royal London customers a Drawdown Governance Service is available to advisers which models a range of scenarios about how your investments might do and provides an early warning system for advisers if your strategy needs to be reviewed.

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Whilst it is possible to insure against rising prices by, for example, turning your pension pot into an inflation-linked annuity, this is likely to be very poor value compared with the pension that you have given up. Essentially, a DB pension scheme is able to make much more cost-effective provision against the risks of inflation than an individual can do by buying an index-linked annuity from an insurance company. Of course, if you invest your DC pension successfully you may be able to achieve an above-inflation rate of return but the protection against inflation is not guaranteed in the way that it is in a DB scheme.

In short, if you are concerned about the potential impact of rising prices over the course of a long retirement, and/or about the uncertainty of whether future inflation will be high or low, then staying in a DB scheme will give you both better inflation protection and greater certainty.

3. Investment risk

When you are a member of a DB pension scheme your money is generally invested in a range of assets. This could include shares, bonds, property, infrastructure

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assets, commodities and so forth. The value of these different assets can, of course, go up or down. But when you are in a DB pension scheme, the ups and downs of these investments make no difference to the amount of pension you receive – the scheme still has to pay your pension and the employer has to bear the investment risk. You are, in effect, insulated against the ups and downs of investment.

By contrast, if you take a cash transfer and invest the money yourself, the value of your fund can – and will – go up and down. This could have a considerable upside – your assets might appreciate considerably. But there is also a considerable downside risk – that your assets will perform badly and you will have to live on a much reduced income.

A key consideration therefore is your attitude to risk. If pretty much all of your non-state pension rights are in your DB scheme and you convert all of them to a cash lump sum to be invested, then you are taking a big risk. You need to consider how you would feel and how you would cope if your investments did badly.

Obviously there are ways in which you can reduce the risk associated with investing in a DC pension or in a drawdown product. For example, you could invest in lower-risk investments but the potential returns may be smaller as a result[12].

The key point here is that when you transfer out of a DB pension scheme you are transferring investment risk from your old employer's shoulders onto your own shoulders.

It is also worth bearing in mind the additional costs which you would face if you manage your own DC pot rather than leaving your rights in a DB scheme. These would include the costs of initial and ongoing advice as well as product fees and charges. These costs would not arise if you left your funds in a DB scheme.

4. Provision for survivors

Since 1997, DB pension schemes have had a legal duty to provide a pension for a surviving widow or widower if a scheme member dies after reaching scheme pension age[13] and many schemes will offer benefits for widows, dependent children etc beyond the legal minimum.

This is a valuable benefit and should not be disregarded lightly. There will also be some rights for widows (from 1978) and widowers (from 1988) under the rules around Guaranteed Minimum Pensions (GMPs) which many schemes had to provide.

Of course, any cash offer which is made to a scheme member will to some extent reflect the fact that the scheme offers benefits to survivors. But because not all scheme members will be married or have dependants, the cash value on offer will tend to reflect the average value of such benefits across all scheme members, including those who will get no survivor benefits. In simple terms therefore, the amount of money you might get to reflect the fact that the DB scheme offered survivor benefits would probably be well short of what you would need to buy equivalent benefits if you were to try to do so as an individual.

It is, of course, possible to turn your pot of money into an income for life with an income for your surviving partner if you were to die. But DB pension schemes are generally able to offer benefits of this sort in a more

[12] There is a different sort of risk associated with having your money in a DC arrangement, namely that the provider may go bust. In this case there is a Financial Services Compensation Scheme which can provide assistance up to a cap. More details can be found at: www.fscs.org.uk.

[13] There are complex rules about survivor benefits for same-sex married couples, cohabiting partners etc and some schemes will do more than the statutory minimum in such cases.

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economical way than an individual annuity purchaser is able to. In addition, depending on your surviving spouse's circumstances, s/he may prefer the certainty of a pension from a DB scheme rather than having the responsibility of managing an inherited DC pension pot.

5. Taxation

For those with larger pension entitlements, the relatively generous tax treatment of DB pension schemes compared with DC schemes is another reason to think carefully before transferring out of a DB scheme.

Under current tax rules, you can build up pension rights worth £1 million over your lifetime. If you go beyond this you can face tax penalties.

For DC schemes, it is largely a matter of comparing the total amount of money in the pot against the £1 million lifetime limit. For DB schemes, a different (and more generous) process applies. The amount of pension to be paid is multiplied by 20 and any tax-free lump sum is added in. The result is then tested against the £1 million threshold. An example will show that as a result there are situations in which a pension left in a DB scheme could be under the tax limit but the DC equivalent could be over the limit.

Consider, for example, someone with a DB pension at 65 worth £40,000 a year and assume they do not take a tax-free lump sum. Multiplying this by 20 gives a figure of £800,000 which is comfortably within HMRC's £1 million limit. Now suppose the member asks for a cash equivalent transfer value. The low level of interest rates and the terms of the pension might result in a multiplier of 30 being applied and a CETV of £1.2 million being offered. If the transfer goes ahead, the member is now potentially at risk of a tax charge on the £200,000 in excess of the £1 million limit.

Clearly in this case the individual has been offered a very large cash sum and the fact that the transfer would result in a tax charge is not of itself a reason not to go ahead. But it does mean that if you have a larger value pension pot you need to be aware that there could be tax consequences of making the switch which need to be taken into account.

to transfer or not to transfer?

To reiterate the point that we made in the introduction to this guide, we are neither promoting DB to DC transfers nor seeking to discourage them. The FCA is clear that a sensible starting point is the assumption you are likely to be worse off if you transfer out of a defined benefit scheme. This presumption should help to ensure that you appreciate the value of what you already have by way of guaranteed pension rights in a DB arrangement.

In saying that, we hope that what this guide has done is make you aware of some of the many factors which have to be considered by each individual when deciding whether or not to trade in DB pension rights for a cash sum.

For some people, the arguments in favour of transferring may be particularly compelling. Those who want to maximise their tax-free cash, do not expect to live long in retirement, are thinking about how best to pass on unspent pension to their heirs, are willing and able to take on the investment risk associated with their pension and/or are worried that the ex-employer standing behind their pension might not be there in years to come, could all find the current terms on offer to be attractive.

On the other hand, those who value the certainty which a DB pension provides may well wish to stay put. If they do so, they will know that their pension will last as long as they do, that they have a measure of insulation against inflation, that they are less likely to breach tax relief limits, that they do not need to worry about the ups and downs of the financial markets and that there will be a pension there for a widow or widower when they are gone.

Ultimately, the decision about whether to transfer should be made after a conversation with a regulated adviser who is either a qualified pension transfer specialist or has their work checked by one. The adviser can take account of your personal circumstances and preferences. Whilst such advice is not binding on the individual, we hope that this guide has shown that the complexity of the choice involved means that such advice should be taken very seriously.

We also believe that ongoing advice through retirement is of value, particularly if a transfer is made. With the large sums that are now being offered to many people to transfer out of DB pension rights, skilled management of the resultant investment pot is of the utmost importance. This will help to mitigate against some of the risks identified in this guide.

appendix – for regulators and policy makers – is the policy framework right?

In preparing this guide we have become increasingly concerned that there are some key aspects of the current regulatory regime which do not seem to be fit for purpose. We mention these here for the consideration of those who regulate such transfers and those who make public policy in this area.

a) Partial Transfers

As things stand, individual DB scheme members have the right to ask for a CETV in respect of the whole of their rights under a scheme. But they have no right to insist on the option of cashing out part of their pension rights. This seems to us to be a problem because a partial transfer might well be the optimal solution for some people.

Consider, for example, the case of someone who has a full state pension and whose non-state pension rights are wholly or mainly in a single DB pension scheme. As things stand, that individual can receive either wholly guaranteed income (state pension plus DB pension) or just a guaranteed state pension and a very large cash sum to invest. They may prefer an intermediate solution where they have a higher level of guaranteed income (e.g. state pension plus half the DB pension) and an intermediate cash lump sum which they can invest more adventurously because they have secured their minimum income[14].

Now it could be argued that the individual who transfers out can secure a guaranteed income at the necessary level by using part of their DC pot to buy an annuity. But, as we have noted throughout, this is likely to be a much less cost-effective way for an individual to secure a guaranteed income than doing it through a large-scale pooled vehicle such as a DB pension scheme.

Apart from the potential administrative cost to schemes (which could be recompensed for this work perhaps by deduction from the transfer value) it is hard to see why you should not have the right to ask for a partial transfer. This might be in the interests of schemes (which could see a higher volume of transfers by those willing to undertake a partial transfer but not a full transfer), in the interests of savers (who can choose their preferred mix of guaranteed and variable income) and even in the interests of HM Treasury which might see some additional upfront tax revenue rather in the way that the DC pension freedoms generated additional tax revenue in 2015/16.

We therefore recommend that the Government should consider as a matter of urgency giving scheme

[14]It would be necessary to consider how new rules around partial transfers would interact with the duties on some schemes to provide 'guaranteed minimum pensions' or GMPS.

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members the right to a partial transfer of their DB rights.

In addition, there would be much to be said for a requirement on schemes to provide members with regularly updated information on the transfer value of their DB pension rights and also for individuals to have the right to transfer right up to retirement age.

b) Transfer Value Analysis

At present, advisers are expected to look at the CETV on offer, assess how much it is likely to grow between the point of transfer and scheme pension age and then calculate how much pension could be bought with that pot in the form of an annuity. If the annuity is much less than the DB pension which the individual would have received, it can be difficult for advisers to recommend a transfer even if they believe that it is in the member's interests taking into account the individual's circumstances.

Based on the reducing volumes of annuity sales, it is reasonable to assume that relatively few people who take a large CETV will use all of it to buy an annuity. This therefore seems like a questionable benchmark. One of the reasons for taking a CETV might be to enable some of the pot to remain invested for longer and to potentially generate a larger total return. There needs to be a way for advisers to be able to take account of this fact. Indeed, for a client who has already indicated that they wish to move their funds into a 'deferred drawdown' arrangement, rather than buy an annuity, it seems particularly inappropriate to use an annuity-based benchmark in assessing whether a transfer should take place.

More generally, advisers should find it easier to form a balanced judgment on the pros and cons of a transfer in each individual case. Many advisers have been reluctant to provide advice in this area at all for fear of subsequent challenge from customers whose transfers take place and do not turn out as they wish, and for fear of having to refuse insistent clients who demand to be allowed to transfer against the recommendation of their adviser.

Given that DB to DC transfers will be in the interests of some individuals, it is essential that there is a strong supply of willing impartial advisers who are suitably qualified to undertake this work and can do so in good faith without fear of undermining their personal indemnity insurance.

We therefore recommend that the FCA reviews as a matter of urgency the advisory framework around DB to DC transfers to ensure that it enables advisers to offer the balanced and impartial advice which is so important to those considering going down this route.

c) Regulatory Certainty

One issue raised by advisers as a barrier to providing advice on DB to DC transfers is a perceived inconsistency between the rules as set out by the FCA and the way in which complaints are handled by the Financial Ombudsman Service (FOS). In some cases advisers report that they followed the rules laid down by the FCA, were the subject of a complaint to the FOS and had that complaint against them upheld because the FOS was applying slightly different criteria. Anything which can be done to ensure consistency between

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regulators and Ombudsmen would provide greater certainty for both advisers and consumers, and should help to increase the supply of advisers willing to provide advice in this area. The recommendations of the recent 'Financial Advice Market Review' may help in this regard.

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