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# REVIEW

## Hello Pension, Goodbye Tension?

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# Hello Pension, Goodbye Tension?

*We currently live in a world of uncertainty and so for many, the financial certainty of a Defined Benefits Pension is the holy grail of retirement. Many people with that kind of pension entitlement may not be aware of that; or of the high risks there are in transferring a Defined Benefits Pension. In this article Advocate Damian Molyneux of M&P Legal outlines some potential risks faced when transferring from a Defined Benefits Scheme.*

A Defined Benefit Pension Scheme is one which pays a pension on retirement, usually based upon the salary you earned with the employer who provides the pension. It is sometimes called a final salary scheme. They can be costly for employers hence today, new schemes are hen's teeth. And for many years such final salary schemes have been shut down in favour of the Money Purchase Schemes. The John Lewis Partnership has, for instance, just closed its generous final salary scheme in favour of a contribution scheme, reportedly saving £80 million by doing so.

Money Purchase Pension Schemes (sometimes referred to as Defined Contribution Schemes) require single or regular premiums to be paid which are used to purchase investment funds. Those funds are subject to fluctuations as with any other investment (i.e. they can go down or up) depending upon how global markets perform. The value of what the investment is worth (or at least a large proportion of it) at retirement age is then usually used to purchase an annuity, which is a financial instrument used to convert a lump sum into regular annual or monthly payments.

On the one hand therefore, with a Defined Benefit Scheme the income received on retirement is all but set in stone. It is not dependent upon investment return and so should be relatively protected from fluctuations in global markets. With a Money Purchase Scheme however, the income is dependent, first of all upon the performance of the investments throughout the lifetime of the pension policy, and then on retirement, the value of the annuity which can be purchased with the lump sum that has been invested.

The risks are fairly obvious. A Defined Benefits Scheme should provide a pensioner with a predetermined income on retirement. The income from a Money Purchase Scheme is however first of all dependent upon how investments perform before retirement, and then, post retirement, what the fund built up can purchase by way of annuity. Neither of these factors is known until retirement age. The income generated by annuities

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has trended downward over the years. For example, according to sharingpensions.co.uk in May 2008 £100,000 would purchase an annuity worth approximately £7,900. That figure had dropped to approximately £5,400 in May 2019, a fall of over 30% in just over 10 years (figures correct as at 10 May 2019).

It seems obvious therefore that the general rule of thumb is that there is a greater advantage for an employee to having a Defined Benefit Scheme than there is to a Money Purchase/ Defined Contribution Scheme and so transfer of a Defined Benefit Scheme to a Money Purchase Scheme must be given a great deal of consideration and will only be appropriate in a fairly limited set of circumstances. There are exceptions to every rule however and anyone with a pension scheme, of whatever type, should take appropriate advice before considering their options, either on transfer, or at retirement.

Earlier this year, the Financial Times reported that since pension reforms were introduced in 2015 the Defined Benefit transfer market has "boomed" (see report of Josephine Cumbo dated 4 January 2019). The article reported that the English regulator has revealed that less than half of the transfer recommendations it reviewed which were made by financial advisers were suitable, meaning that most should not have gone ahead. The Financial Conduct Authority (the regulator in England) believes that it is not in most people's interests to give up Defined Benefit arrangements (i.e. to transfer out of such a scheme).

This is not a problem unique to the United Kingdom and advisers within the Isle of Man report a substantial increase in defined benefit transfers over the course of the last few years. Whilst there is no publically published guidance in respect of Defined Benefit transfers, generally speaking regulated Manx Advisors should follow the standards of practice and advice recommended by the English Financial Conduct Authority.

It is telling that the Financial Times reported that the Financial Conduct Authority found less than 50% of the defined benefit transfer advice that it reviewed was suitable. There is undoubtedly a possibility that similar levels of unsuitable advice may be prevalent within this jurisdiction. Any individual who has received advice to transfer a Defined Benefit Scheme should have that advice reviewed by a professional if they are unsure about the appropriateness of it. If the advice to transfer was not appropriate at the time given and/ or was not advice which a reasonable and competent adviser would normally give, then it may be possible for the individual to seek redress.

*Damian Molyneux is a director of M&P Legal, and a former financial adviser, and regularly deals with financial mismanagement claims. This article does not give legal advice, specific advice should be sought in all cases.*

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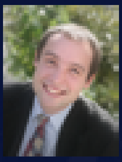

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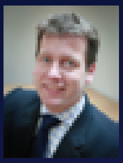

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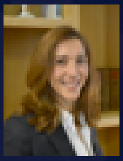

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