Everything You Need To Know About Pension Transfers

JESSICA COOK
In Partnership with AES Wealth

Contents

What is a pension transfer?

Pension arrangements generally allow you to transfer your pension benefits from one arrangement to another. The transfer rules depend on the arrangement you are transferring from and the arrangement you are transferring to.

A pension transfer is a process of transferring – ie switching or changing the contributions made from one pension scheme to another. Or by exchanging your future annual pension from a final salary scheme for a cash equivalent transfer value (CETV) into a scheme that can be flexibly accessed. Doing this ends your membership in the original pension scheme. Most schemes will allow you to transfer your pension pot to another pension scheme. This can either be an employer's workplace pension scheme, a personal pension scheme, such as a Self-Invested Personal Pension (SIPP) or a Qualifying Recognised Pension Scheme (QROPS). Although there are specific rules in place for final salary pension transfers and limitations on some receiving schemes based on residency.

In March 2015, the Government introduced 'Pension Freedoms', allowing much more flexibility in the way people can take pension income from Money Purchase schemes, such as Personal Pensions and Stakeholder pensions. Money Purchase scheme members can now take uncapped withdrawals from age 55, via a mechanism known as Flexi Access Drawdown (FAD).

These new freedoms have prompted many members of Final Salary Schemes to look at transferring their benefits to a Money Purchase arrangement, and therefore access the income flexibility. Transferring out can create greater financial flexibility, which could be a key benefit when it comes to lifestyle planning in retirement. It can also create flexibility in tax planning. And provide superior death benefits assisting in robust legacy planning.

Understanding whether you will benefit from a pension transfer can be complicated and you should take appropriate advice.

When would a pension transfer be a good option to consider?

Here are just a few examples;

- Your final salary scheme may be in deficit and you are concerned it may not be able to meet its obligations.
- Your pension scheme is being closed or it is underfunded
- You reside overseas and wish to move your pension outside of the UK.
- Potential tax advantages and the use of Double Taxation Treaties (DTA's) if overseas.
- You are due a large pension from your final salary scheme and the benefits payable by the PPF (in the event it enters the PPF) would be less.
- The options in relation to succession planning may be greater following a pension transfer.
- It may be advisable to transfer if you are going to be affected by the lifetime allowance. See Lifetime Allowance section for further details.
- Your existing company scheme is being wound up.
- You have been offered an enhanced transfer value from your final salary scheme.

- You have funding needs that cannot be met by your final salary scheme. Such as the need to pay off your mortgage.
- The parameters of your defined benefit scheme have worsened. Such as an increase in the retirement date, lower accrual rates, reduction in spouses benefits
- You may wish to access your pension benefits earlier than the schemes' normal retirement date (without penalty)
- Your current provider doesn't offer the type of pension you want. For example, flexibility may be more important to you than a guaranteed income from a final salary scheme.

Are there any circumstances under which I may not transfer my pension?

It is no longer possible to transfer benefits from unfunded public sector final salary schemes, such as the Fire Service or an NHS pension. You will also not be able to transfer away from a final salary scheme if you are already in receipt of your pension. And may not be able to transfer if you have reached the scheme's normal retirement date.

You cannot transfer an annuity to a QROPS or SIPP or other flexible product. If you are already in receipt of a final salary/DB scheme you can no longer transfer these

benefits. You can generally transfer at any time up to a year before the date that you are expected to start retirement. The scheme's normal retirement age (NRD)

Do I need to take financial advice if I want to transfer my pension?

That very much depends on the pension you are considering transferring and the scheme you are transferring to. For any defined benefit pension worth more than £30,000 or a scheme with a guarantee attached to it, such as a guaranteed annuity rate (GAR) you will need to need to take advice. If you are considering transferring a defined benefit/final salary scheme that is valued at over 30,000 pounds, you will need to take regulated advice from a Pension Transfer Specialist with the appropriate permissions. Even though it may not necessarily be a requirement, it is advisable to seek professional advice when transferring from a defined contribution scheme.

Final Salary Pension Transfers

A defined benefit pension is a special type of workplace pension. Instead of building up a pension pot over time by way of contributions, it provides you with a guaranteed annual income for life, based on your final or average salary (hence the name). Over the last couple of decades, final salary schemes have become increasingly scarce and today very few employers provide them – especially in the private sector. This is largely because of the expense of offering such pensions and, in particular, the fact that the future costs associated with these schemes can be very unpredictable.

Transferring out of a final salary scheme

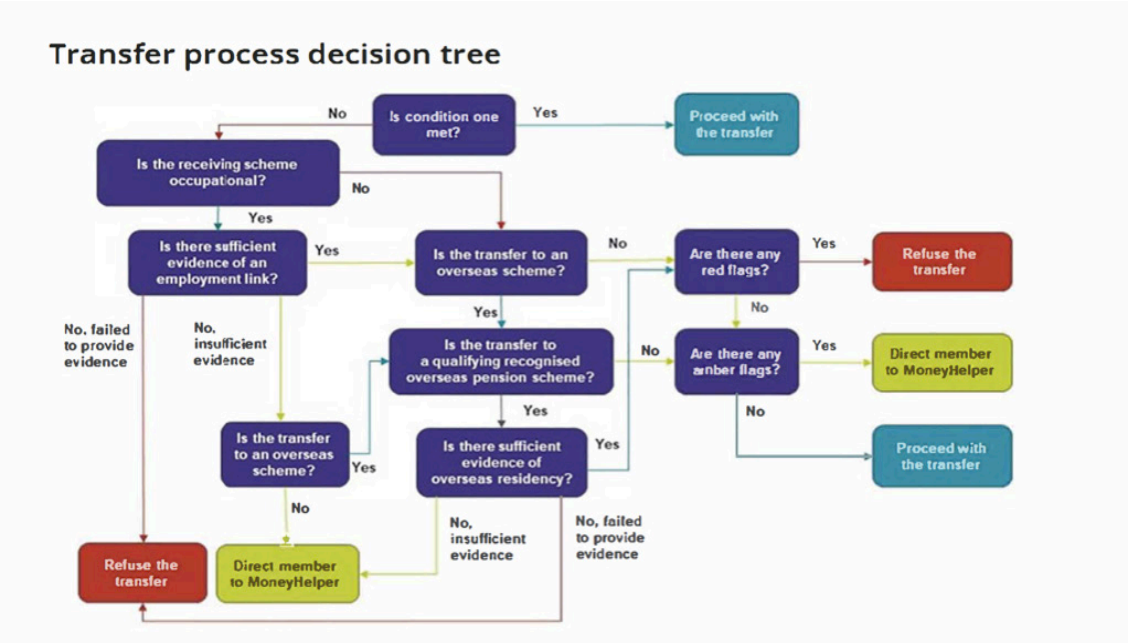
The FCA (Financial Conduct Authority) requires firms advising on pension transfers to have specific permission for advising on pension transfers and opt-outs. If the value of your pension assets in a defined benefit scheme are valued at more than £30,000, the Government rules require your pension provider to ensure that you have taken regulated financial advice. Your suitability to transfer your pension will be based on your own set of personal circumstances and your financial objectives for retirement.

There has been lots of bad press about people falling victims to pension transfer scams and receiving bad advice. It is vitally important you take advice from FCA-regulated pension transfer specialists, so you understand the risks involved when transferring your pension.

New regulations (Nov 2021) - Dealing with pension transfer requests

Anyone thinking of transferring a pension should be aware that there have been some very recent amendments to the rules in relation to pension transfers. From the 30th November 2021, trustees and scheme managers must ensure specific checks are made before complying with a member's request to transfer their pension. The checks will determine whether the request meets the conditions to enable a statutory right to transfer, including whether a member is required to have guidance from MoneyHelper.org.uk.

Most transfer requests are likely to be straightforward and you should be able to complete them well before the statutory six-month deadline. A minority of cases, on the other hand, will require more investigation. There are some receiving schemes to which a statutory transfer can proceed with no further checks. If the receiving scheme is not one of these, further assessments are needed to confirm that you are able to make a statutory transfer. The below diagram provides the framework set out by the Pension Regulator. More information can be found at www.the pensions-regulator.gov.uk



How are Defined Benefit Pensions Calculated?

The income you'll get from a defined benefit pension is based on three factors:

- Number of years you've been with that employer and a member of the scheme,
- Your pensionable earnings (for final salary schemes, this is your salary at retirement; for career average schemes, this is your mean salary across your career)
- Your pension scheme's accrual rate (the proportion of your earnings you'll receive for each year spent in the scheme, usually represented as a fraction, e.g. 1/80th)

While you have no control over your funds or where they are invested, you are protected from falls in the stock markets because your company must make up any shortfall. This is because the company takes all the investment risk. Irrespective of the performance of the investments, you will receive a pension based on your salary and service. This is a pension paid for life and provides a great deal of security.

If your combined pension benefits are valued in excess of GBP 750,000 and you would like to understand more about your options, please get in touch: Jessica.cook@aesinternational.com

Pension commencement lump sum in final salary schemes

When you retire, the government rewards you for saving into a pension by allowing you to take 25% of your savings completely tax-free. This is commonly called a lump sum, and taking it will reduce the amount of income you receive from your pension. With final salary pensions, the way this is calculated is complicated. It's based on the scheme's 'commutation factor', which represents how much of a lump sum you get for every £1 you give up in income. So if you have a commutation factor of 12, you get £12 of lump sum for every £1 you give up.

What is a CETV? How will a transfer value be calculated?

A CETV is a cash equivalent transfer value. The cash equivalent transfer value is the amount your current pension scheme will offer you if you want to transfer out of your defined benefit pension and into a defined contribution scheme. It's expressed as a lump sum. So you have the option to give up the future annual benefits in exchange for the CETV. Each final salary pension scheme will have its own rules about how it works out the Cash Equivalent Transfer Value. The transfer value will depend on your age, the level of forecast pension when you retire, your retirement date, and the annual increases on your pension.

The CETV is calculated by working out the lump sum that will be required to provide an equivalent pension to the scheme pension at your retirement age. This lump sum is then reduced (discounted) back to today's date to provide the CETV. Ultimately the size of the CETV is at the discretion of the trustees provided they are operating in line with the rules of the scheme.

The importance of guarantees in a final salary scheme

Giving up the benefits from your final salary pension means you will be giving up any guaranteed income for life. These pensions also offer inflation protection and so will increase over time as you get older. By moving to a personal pension you will be giving up any guarantees and any inflation proofing.

When you transfer from a final salary scheme to a defined contribution scheme, your capital will be invested and you as the individual will bear the risk instead of the scheme. Therefore It's crucial that individuals carefully consider their capacity and tolerance for loss as well as their risk appetite.

Final salary pensions must, by law, offer benefits to a surviving widow or widower if you die after reaching the scheme's pension age and this should be another consideration. Although this will typically be 50% of the member's pension. It's important to remember that your pensions need to meet your and your family's income needs for life.

Despite the attractions of defined benefit pensions, They are not as flexible as defined contribution schemes. This is because you can't vary the income you take from it, nor draw out larger lump sums. Typically your final salary scheme will only pay 50 to 60% of your annual entitlement to your spouse. The pension payments will then cease upon the second death.

What are the timelines? How long does a pension transfer take?

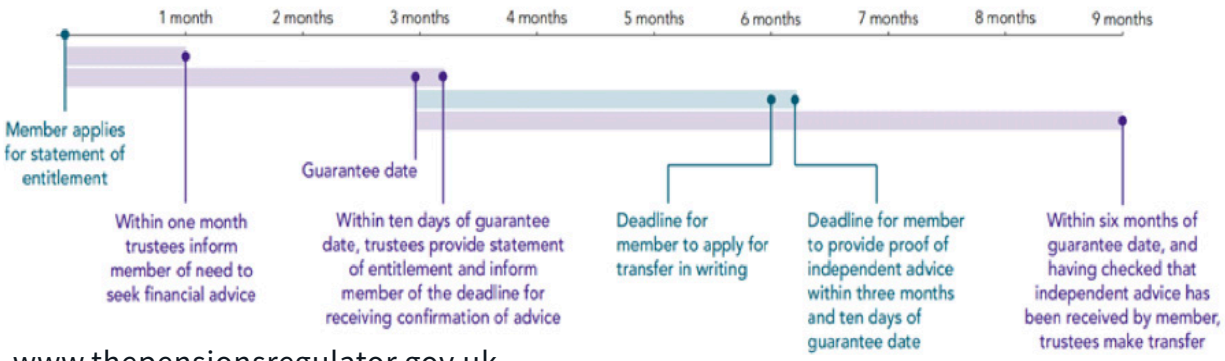
If you are transferring from a final salary scheme where your CETV is valued at more than 30,000 pounds, the transfer process may take considerably longer than if you are transferring defined contribution schemes. The Pensions Regulator sets out the rules and timelines for transfers from final salary schemes.

There are various parts to the statutory process of transferring from a final salary scheme that must be adhered to by both the trustees of the new scheme and the old scheme. As well as member and financial adviser obligations.

- Upon receiving the CETV the member has a maximum of 6 months to apply in writing for the transfer and to provide proof that they have received adequate advice on the transfer.
- Within 6 months of the guarantee date of the CETV, the trustees must make the transfer to the new receiving scheme.
- Members with safeguarded benefits have a statutory right to request a statement of entitlement once in every 12 month period. Some schemes may allow more frequent requests.

Where a member requests a transfer there are a number of steps in the process that must be followed. The timeline below sets out the main steps for a statutory transfer where the £30,000 exemption does not apply.

Timeline for statutory transfers over £30,000



www.thepensionsregulator.gov.uk

Will I still be eligible for the Pension Protection Fund (PPF) if I transfer?

Some people have cited concerns about their scheme going bust as a reason to consider transferring away from their final salary pensions and all the benefits that it can bring. However, to protect members of insolvent employers where there is a shortfall in the pension scheme, the Pension Protection Fund (PPF) was established by the government to cover schemes that fail from April 2005 onwards.

You are only eligible for the PPF if you are still a member of a final salary scheme. Defined contribution schemes such as a SIPP or QROPS are not protected by the PPF. If you transfer away from a final salary scheme and the previous scheme enters the PPF you are not entitled to this protection.

What does a pension transfer cost?

The fees for financial advice relating to pension transfers will vary. Often it will depend on the complexity of the case, whether it is a final salary or defined contribution scheme you are transferring from and whether there is more than one scheme. Typically you will pay a fee for the advice and then an upfront fee and ongoing annual management fee, based on a percentage of the transfer value.

The Lifetime allowance and pension transfers

An additional pension tax to watch out for is the lifetime allowance charge. The lifetime allowance on UK pensions limits how large your pension savings can grow. The lifetime allowance is currently £1.073100 (as of writing Jan 2022) If you exceed this, you will pay a 25% additional charge if you take the excess as income or 55% if you take the excess as lump sums. The UK Lifetime allowance is the total value of pension savings that can be accumulated without a tax charge. We have previously seen the lifetime allowance fall from 1.8 million, down to 1.5 million down to 1.25 when it was reduced yet again to £1 million from 6 April 2016. It has since increased slightly to try and keep pace with inflation.

And the lifetime allowance can be a very important consideration of pension transfers. It is important to note that the lifetime allowance is calculated differently depending on what type of scheme you are in. For final salary schemes, the LTA is calculated as 20 x your expected annual pension. For defined contribution schemes it is the value of the pot. So it is necessary to see what the LTA implications are if you transfer from a DB scheme to a DC scheme. Furthermore, savers should be aware of possible LTA implications that are dependant on the receiving scheme. For example, if you are transferring from a final salary scheme to a SIPP, LTA tax charges will not be due on the transfer. Conversely, a transfer to a QROPS evokes an immediate test against the lifetime allowance. So if you have a larger pension pot, you might be hit with a lifetime allowance charge upon transferring.

Protecting Yourself from the Lifetime Allowance

There are two forms of protection in place, that will allow you to increase your Lifetime allowance limit (based on certain requirements)

Fixed protection 2016

Fixed Protection Provides a higher lifetime allowance (LTA) than the standard LTA, It's aimed at those whose pension benefits will, or are likely to, exceed the LTA when benefits are taken offering valuable protection against LTA tax charges. You can still apply for fixed protection 2016 (there's no deadline). Previous versions are no longer available. Regardless of fund size or benefit value, you could apply for fixed protection as long as you don't have enhanced protection, primary protection or an earlier version of fixed protection. Applications for FP2016 are made online (a Government Gateway account is required). If successful, FP2016 will apply retrospectively from 6 April 2016, regardless of when it's granted.

Individual protection 2016

Individual protection 2016 gives individuals a protected lifetime allowance equal to the value of their pension savings on 5 April 2016, subject to an overall maximum of £1.25 million. The value of any pension savings above the protected lifetime allowance will be liable to the lifetime allowance charge. IP gives individuals who think that the value of their benefits will be over the lifetime allowance when they come to take their benefits, a personalised lifetime allowance based on the value of their pension savings. IP 2016 allows someone whose pension rights are valued over £1 million (the lifetime allowance between 6 April 2016 and 5 April 2018) to protect those rights, subject to an overall maximum of £1.25 million. For example, someone with pension rights worth £1.2 million at 5 April 2016 will be able to have £1.2 million as their personal lifetime allowance through IP 2016. Someone with pension rights worth £1.3 million will be able to have £1.25 million as their personal lifetime allowance. This personalised lifetime allowance will not increase unless the lifetime allowance increases to a level greater than the individual's personalised lifetime allowance

A crucial difference between Individual Protection 2016 and Fixed Protection 2016 is that with the former an individual can still be an active member of a pension scheme, whereas with the latter (Fixed protection) the individual needs to have stopped contributing to a pension or accruing benefits as from 6 April 2016

Non-Resident Enhancement Factor

In addition, an alternative mechanism of protection, which is less well known. Is the opportunity for those individuals who were still benefiting from their UK scheme whilst non-resident to apply for an Enhancement factor, also known as a Non-Resident Factor. If you have spent time outside of the UK and contributed or received benefits during that time, you might be able to have your LTA increased, thus saving a lot of money on the related tax charges. There is no cap, and so it is possible for people with very long tenures overseas to get a a large enhancement. Bear in mind though, that the tax free cash available will still be based on the current standard LTA and not your enhanced amount.

Sometimes depending on your position, a transfer can help you to possibly mitigate future LTA taxes. A qualified adviser can help you understand your options.

Thinking of transferring to a SIPP?

A SIPP is an acronym for a Self Invested Personal Pension. It is a UK government-approved pension scheme, sometimes referred to as a pension wrapper. A SIPP allows an individual to make their own investment selection and decisions. A SIPP can offer a much wider investment selection than most stakeholder pensions allowing you to take much more control over your pension pot, whilst offering more flexibility than employer pensions or other private pension plans.

At what age can I access my SIPP?

Pension flexibility was introduced in the UK in 2015. You can now access your SIPP From the age of 55 (at the earliest) unless you are in serious ill-health. You will be entitled to 25% of the fund value of your as a tax-free lump sum (up to the lifetime allowance). The remaining fund should then be used to provide you with regular income throughout your retirement. This income can be taken in various ways and in varying amounts. But this is an important consideration as you do not want your pension to run out and you must consider the tax implications of withdrawals. Please note the increase in the retirement age from 55 to age 58, due to come into force in 2028.

How much of my SIPP can I access?

The new pension flexibility rules mean that SIPPs can be extremely flexible. Once you reach 55 you can access your whole pension pot however you decide. This can sometimes be useful if you have a large debt such as a mortgage you want to pay. The balance can then provide you with a pension via income withdrawal (drawdown) from your SIPP or can choose to purchase an annuity. The introduction of pension flexibility has seen a sharp rise in the number of people cashing in their pension pots. Remember this is your pension income and needs to last your lifetime! This may be an option if you have other pensions or assets, or retirement income but if it is your only income in retirement, care must be taken to ensure you don't take out too much too quickly.

Are there any tax advantages to a SIPP?

There is no difference in the tax treatment of a SIPP compared with other forms of personal or occupational pensions. Whatever you put in qualifies for tax relief at your highest rate but be aware of the maximum you are allowed to contribute that will be eligible for tax relief. There may also be limitations if you are subject to the money purchase annual allowance. There is also no Capital Gains Tax payable on any growth in the value of investments held within the scheme. You cannot make additional contributions if you live abroad.

What will happen to my SIPP when I die?

This will depend on a number of factors. Namely, if you have entered into drawdown yet and whether you have reached the age of 75. If you die while receiving income from a drawdown contract, your dependents options are as follows:

If you die before age 75, any drawdown benefits can usually be passed on free of tax. They can be passed on either as a remaining lump sum or as Flexi access drawdown (FAD). Note the benefits must be passed within a 2-year window and the benefits will be subject to a test against the lifetime allowance. If you die on or after age 75, any benefits will be taxed at the beneficiary's marginal rate. Your chosen beneficiary/s can continue the drawdown and carry on taking an income from it, in which case they'll pay tax on the income at their marginal rate. There is no further lifetime allowance text after the age of 75.

Thinking of transferring to a QROPS?

A QROPS is a Qualifying Recognised Overseas Pension Scheme. It was devised for those who live overseas as an expatriate or those who are planning to leave the UK. Alternatively, a person who is born outside the UK having built up benefits in a UK-registered pension scheme can move their pension offshore if they want to retire outside the UK. The Finance Act 2004 made it possible from April 2006, for UK pensions to be transferred to an overseas pension scheme that is registered with HMRC as a QROPS.

QROPS taxation

How your QROPS is taxed will depend on where you are resident in retirement. Where the QROPS is based, and whether there are any double taxation treaties in place. It is, therefore, possible in some cases, to pay less tax than you would pay if your pension remained in the UK. Previously, QROPS were only exposed to tax on 90% of pension income for UK residents. This has now been increased to 100%.

Once in a QROPS, funds are sheltered from UK taxes on income and gains. They also no longer count towards your lifetime pension allowance (LTA), so can grow unlimited without attracting LTA penalties of 25% or 55% when accessing your money. While QROPS funds become taxable once you start taking benefits in your country of residence, many expatriates can receive favorable tax treatment depending on where they are based. The country-to-country tax relationship is governed by the rules of any tax agreements between the governments. If they have DTAs, then the terms of the treaty detail how much, if any, income tax is paid on pension benefits.

Important!

From 9th March 2017, transfers to QROPS may attract an additional 25% tax charge upon transfer, known as the OTC – Overseas Transfer Charge, but there are exceptions. You will still be able to make a transfer tax free if one of the following applies:

- You are resident in the country where the QROPS receiving your transfer is based
- You are resident in a country in the European Economic Area (EEA) and the QROPS you are transferring to is based in another EEA country
- The QROPS you are transferring to is an occupational pension scheme and you are an employee of a sponsoring employer under the scheme
- The QROPS you are transferring to is an overseas public service scheme and you are employed by an employer that participates in that scheme
- The QROPS you are transferring to is a pension scheme of an international organization and you are employed by that international organisation

Note however that If you are exempt from the charge on transfer but then your circumstances change within 5 years, such as moving to another country outside of the EU, or moving your QROPS to another country, then you may have to pay the 25% tax charge at that point.

If I transfer to a QROPS from a UK scheme will my benefits be tested against the lifetime allowance?

A transfer from a UK tax-relieved pension scheme to a QROPS will be treated as a Benefit Crystallisation Event, known as a BCE. A transfer to a QROPS is BCE 8. Therefore transfers of both crystallised and uncrystallised funds from UK pensions to QROPS are subject to a lifetime allowance (LTA) test upon transfer. The LTA charge is 25%. The scheme must carry out the LTA check and calculate any LTA charge before calculating any overseas transfer charge. Only once all taxes due have been paid may the funds be transferred.

Think about a pension transfer carefully

Giving up a Final Salary pension is not a straightforward decision and certainly not one to be taken lightly. The value of your pension could be the biggest asset you have, worth even more than your house. There is no going back, as transfers out of Final Salary schemes are not reversible.

There are a few things you should think about that can help you decide if it's the right choice for you:

- **Your retirement income needs:** There's no guarantee that your retirement income will be better after transferring your pension. That's why it's best to weigh up your options carefully to make an informed choice. If you don't have any needs that can't be met by your final salary scheme, then there is little reason to transfer and accept the risk of being worse off in retirement. However, if you do have some needs that a money purchase scheme would provide that can't be met by the scheme then a transfer may be beneficial.

- **Your benefits and guarantees:** Your existing pension may give you benefits or guarantees that the new plan might not offer. That's why final salary schemes were often called 'gold plated' because of the guaranteed income for life. Ask yourself how important is a guaranteed income to me? Perhaps if your income needs can be met by other sources, it may not be so important, as if you solely rely on one scheme.
- **Cost:** The cost of a final salary scheme is covered by the employer. When you transfer away from that scheme you will need to cover any costs for the new pension scheme.
- **Your other assets.** If you have other assets – such as property, other pension schemes, cash in the bank etc. – this could be a positive point towards a recommendation to transfer. This is providing you're happy to rely on these assets if the benefits of a transfer turn out to be lower than expected. On the other hand, if you don't have much in the way of other assets then a transfer is unlikely to be suitable for you, especially if you are solely or mainly reliant on your final salary scheme.
- **Life expectancy:** A shortened life expectancy, perhaps due to a medical condition, may form part of a decision to transfer. You may get more value from your pension from transferring than you would from drawing it for only a short number of years. Or perhaps you feel more confident knowing any remaining funds will pass on to your spouse, without a reduction in the annual pension.
- **Your risk appetite and capacity for loss** – If you are extremely risk-averse or have a very low capacity for loss then it is unlikely a pension transfer will be suitable.

A few additional pointers when seeking pension transfer advice:

- You should receive a full explanation of the options open to you for the new pension fund that you could move into. Ask for a full explanation of the pension and cash lump sum benefits you will leave behind if you leave your final salary pension. Including your options for early and late retirement. You need to fully understand the guaranteed benefits you may be giving up alongside any potential tax-free cash.
- Ask for a full explanation of the key risks associated with transferring into a personal pension fund, as well as the risk of remaining in your current scheme.
- Your current scheme may be in deficit and this could be a concern. Looking at the new scheme, you need to fully understand all potential risks such as investment risk or inflation risk.

- If you have a larger transfer value you may need to apply for an enhancement on your lifetime allowance. Ask for an explanation as to how the Lifetime Allowance impacts your pension fund and how it will impact you if you transfer. You should seek guidance on the various forms of protection in place that you can apply for.
- If you are married, it is important to involve your spouse in the decision-making process from outset. This decision is likely to affect the financial future of both of you.
- If you do transfer away from your scheme make sure your financial adviser helps you to complete nomination beneficiary forms. These should also be updated regularly to avoid any ambiguity.
- Make sure you are clear at the outset what costs are involved in the pension transfer process. There will usually be an advice fee whether you decide to transfer or not. Plus a fee for the pension transfer report, which is noncontingent on the pension transfer taking place.

Any potential pension transfer should be given serious consideration. The process is time-consuming but that is generally a good thing. It leaves plenty of time to carefully consider the benefits and risks of a transfer and the potential impact on personal circumstances. And always seek advice from a pension transfer specialist.

About the Author

I'm Jessica Cook Wealth Adviser to International professionals and families across the globe. Featuring in the 2022 Times Newspaper Guide to the UK's Top Rated Financial Advisers. My background is law, and a former career with the Financial Times. I am also a regular financial columnist for multiple publications. I am a Pension Transfer Specialist and for the last 10 years have successfully helped numerous clients around the World, to transfer their pensions (where suitable).

Any information provided is for information purposes only and does not constitute actual advice. It is intended to provide general information only and does not attempt to give you advice that relates to your specific circumstances or requirements

vouchedfor

Warning - Pension scammers

Pension scammers are currently targeting people with Defined Benefit pensions schemes.

Always take your own steps to verify the identity of those contacting you, the Pension Regulator has produced a guide called 'How to spot a scam', you can access it here.

Schedule a complimentary 15 minute discovery call

If your combined pension benefits are valued in excess of GBP 750,000 and you would like to understand more about your options, please get in touch:

Email – **Jessica.cook@aesinternational.com**

Visit my website - **aeswealthadviser.com**

UK HEAD OFFICE

7 Bell Yard
London
WC2A 2JR
United Kingdom

UAE OFFICE

Level 2, Exchange Tower
Al Mustaqbal Street (Future Street)
PO Box 191905
Dubai
United Arab Emirates