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FINANCIAL SERVICES

YOUR GUIDE TO DEFINED BENEFIT TRANSFERS

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MAKE THE RIGHT CHOICE, NOT A RUSHED CHOICE:
YOUR GUIDE TO DB TRANSFERS

Since the introduction of pension freedoms in 2015, there has been an increase in the number of people considering transferring their pension from defined benefit (DB) to defined contribution (DC) schemes. Whether this is right thing to do or not will depend on your individual circumstances. You should always start by assuming that it is not the right thing to do.

DB AND DC: WHAT'S THE DIFFERENCE?

WHILE BOTH DB AND DC SCHEMES PROVIDE INCOME FOR PEOPLE IN RETIREMENT, THERE ARE SOME IMPORTANT DIFFERENCES BETWEEN THE TWO.

WITH A **DB SCHEME:**

- You (the member) receive a regular income from your company's DB scheme based typically on how many years you worked for the company and the salary you earned.
- This income generally goes up with inflation and is guaranteed for your lifetime – regardless of how long you live or how the investments in the scheme perform.
- The lifetime guarantee is funded by the amount of assets the scheme has under investment and your employer's promise to make up any shortfall.
- Since the DB scheme and your employer take on all the investment risk associated with the pension scheme, you can plan for your retirement with a high degree of certainty.
- There is typically little flexibility in terms of how you can take your retirement benefits. For example you maybe able to take retirement benefits from age 55 and there would normally be a reduction for early payment. If you think this might be relevant to you then you should obtain further details from the scheme.

WITH A **DC SCHEME:**

- You and your employer can both pay into the scheme – the size of your benefits at retirement will be influenced by the contributions made.
- It is uncertain how much money you will have to retire on since the value of your pension will depend on how the investments you have chosen to invest your contributions into have performed over time.
- You take on the investment risk associated with the scheme meaning your investment could go up or down over time and there are no guarantees.
- There is a lot of flexibility around how you can take money out of your pension following the introduction of the pension freedoms. You can take all or part of your pension fund as cash from the age of 55 onwards, this may be subject to a tax charge. When you begin to take your benefits, you can choose to move your pension into flexi-access drawdown (to keep it invested) or to buy an annuity (which provides a guaranteed income for your lifetime).

Each DB scheme will have it's own rules, and the above is just a generic example. You should check out the specifics of the scheme rules with the administrator, before making any decision.

PEOPLE WHO CHOOSE TO TRANSFER THEIR PENSIONS FROM A DB TO A DC SCHEME TYPICALLY WANT TO TAKE ADVANTAGE OF THE PENSION FREEDOMS.

CASH EQUIVALENT TRANSFER VALUE

People who choose to transfer their pensions from a DB to a DC scheme typically want to take advantage of the pension freedoms and have more flexiblity with their pension savings. By transferring your benefits to a DC scheme, you would have a pool of cash that you could invest as you see fit and/or take as a lump sum.

If you are interested in transferring to a DC scheme you can ask your scheme provider to issue a statement of entitlement telling you your pension's 'cash equivalent transfer value' (CETV). This is the lump sum the pension scheme will offer you in exchange for you giving up any future claims to your DB pension benefits. To calculate it, the scheme provider will consider factors like inflation, investment and longevity forecasts, as well as other assumptions.

Once a CETV has been issued, you generally have three months in which to accept it and to give notice to the scheme trustees of your intention to transfer. If the deadline is missed, the provider may charge you for issuing a new CETV within 12 months. The new CETV could be a different amount (it could be higher or lower than the previous CETV).

SEEK FINANCIAL ADVICE

Deciding whether to transfer your benefits from a DB scheme to a DC scheme is a very important decision, which will affect the rest of your life. So it is crucial that you research the decision fully and take qualified financial advice. You should speak to an adviser before requesting your CETV.

Your adviser will need to talk to you about your personal circumstances, so that they can make an informed recommendation about whether you should stay with your DB scheme or switch to a DC scheme. They may request extra information from your DB scheme provider.

A good financial adviser will invest a lot of time and effort in coming up with the recommendation that is right for you. Remember that it is better to pay for the right advice than to make an expensive mistake.

If your CETV is £30,000 or more, the DB scheme trustees will not be able to release the CETV unless they see you have received financial advice from an appropriately qualified financial adviser.

YOUR PERSONAL CIRCUMSTANCES WILL DETERMINE WHETHER IT IS A GOOD IDEA FOR YOU TO TRANSFER YOUR PENSION BENEFITS.

EDUCATE YOURSELF ON RISK

Probably the biggest advantage of DB schemes – provided you have a reputable and solvent sponsoring employer – is that they insulate you from risk. Even in the event that the sponsoring employer of your DB scheme becomes insolvent, and there are insufficient assets in the scheme to cover all of its pension commitments, you can still claim compensation from the Pension Protection Fund **(www.pensionprotectionfund.org.uk).**

Once you move to a DC scheme, you personally take on all of the following risks:

- Inflation risk (the risk that you have less money to live on in real terms because the cost of goods and services has gone up).
- Longevity risk (the risk that you outlive your savings).
- Sequence of return risk (the risk that your investments perform worse than expected).
- Volatility risk (the risk that your investments change dramatically in value, down as well as up).

ASK YOUR FINANCIAL ADVISER TO SHOW YOU SOME CASH FLOW MODELS THAT DEMONSTRATE HOW YOUR INCOME COULD BE AFFECTED BY THESE DIFFERENT RISKS.

THE RIGHT DECISION FOR YOU

Ultimately, your own personal circumstances will determine whether it is a good idea or not for you to transfer your benefits out of a DB scheme. Key considerations include:

- your health
- your marital status
- whether you have children or other dependants
- the health of your spouse or dependants
- ongoing financial commitments, for example a mortgage or school fees
- other sources of income, for example part-time employment, or rental/dividend income
- other pension provision.
- other investments, for example buy-to-let property or shares
- your experience of investing
- your attitude to risk and capacity for loss
- your plans for retirement
- how much money you will realistically need to live on in retirement.

While transferring benefits from a DB scheme to a DC scheme can be the best outcome for some people, it is not appropriate for everyone. Don't be blinded by the size of your transfer value or allow yourself to be pressured by family and friends. Take your time to weigh up your options and to reach the decision that is right for you.

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