

### Summary

- There are mixed reports as to the number of members deciding to transfer out of their DB scheme. Those members with the biggest DB pots are often most open to considering their options.
- Explaining whether a transfer may or may not be in the member's best interests can be difficult, as it depends on so many individual factors.
- Financial advice can help ensure members make the most appropriate decision for their circumstances when deciding whether to transfer out of their DB scheme.
- A partial transfer could give a member a one-off lump sum, whilst leaving some of it in DB, giving them a secure lifetime income.

# Time for a transfer?

## Following transfer values reaching record highs, Louise Farrand asks if this has led to a surge of members moving their money from DB to DC schemes

The start of a revolution, or a storm in a teacup? Statistics about people's appetite for defined benefit to defined contribution transfers present a mixed picture.

Only a very small proportion of those surveyed by the Pensions and Lifetime Savings Association (PLSA) were planning to transfer their money from their defined benefit (DB) pension scheme into a defined contribution (DC) scheme. A mere 3 per cent of people with DB pensions were planning to

access their pension pot by the end of 2015, according to a survey by the PLSA in January 2016 (*Pension Freedoms: No More Normal*).

Yet advisers are reporting a leap in enquiries from DB scheme members who are considering transferring their money. Selectapension, a pension and investment software provider, reported a 66 per cent increase in DB cases analysed by advisers and paraplanners in 2016, compared to 2015. In April 2016, advisers analysed 96 per cent more DB cases than in April 2015.

### Transfer what?

The government introduced its freedom and choice policy in March 2014. In the past, DC savers were required to buy an annuity with their pension savings when they retired. Now, they are free to do what they want with their savings at retirement, whether that's taking them as cash, drawing their money over time whilst leaving some of it invested, or buying an annuity.

By contrast, members of DB schemes receive a guaranteed monthly income for life. Such schemes, whilst typically more generous than their DC counterparts, are less flexible. However, it's possible to transfer out of a DB scheme and into a DC scheme. Indeed, some DB scheme members are thinking about transferring their money into a DC scheme to give them more flexibility.

What accounts for the mixed reports? The fact that it's early days plays a big part. While consumers may be exploring their options, they are not necessarily ready to act.

Opinions on members' appetites for transfers vary from expert to expert. "Anecdotally, it seems it's a damp squib," says the Society of Pension Professionals president Hugh Nolan. "There are various reasons for that. Not least is the fact that many people are stuck in inertia – they might have a lot of ideas but not quite get around to doing them. It's easier to take the pension from your pension scheme."

According to ITM executive chairman Duncan Howorth, the company has seen a growing interest in pension consolidation generally, "with members looking to gather their pots into one and being able to make better decisions".

Hymans Robertson head of consultancy Jon Hatchett thinks the reforms have had a big impact. "Take-up rates have doubled in the year post freedom and choice and they're up another 15 per cent now. But from a low starting point," he qualifies.

Hatchett continues: "We have also seen a real divergence between schemes. Those schemes who are actively





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communicating with members about their choices are seeing much more activity than those who are doing very little.”

#### A difficult balance

Explaining the pros and cons of DB to DC transfers is not an easy tightrope to walk. Whether a transfer is in a member’s best interests depends on so many factors, from their general financial position to the terms of the transfer.

At present, with gilt yields low, transfer values look good value in general. “People tend to get very good value if they want to exit their DB scheme. This probably peaked towards end of last year and since then, transfer values have flattened out a bit,” says PLSA

head of governance and investment Joe Dabrowski.

When it comes to explaining transfers to members, Hatchett thinks schemes should be straightforward and proactive. “The Financial Conduct Authority objective around freedom and choice is that customers should be given the right information, at the right time, to make decisions that are in their best interests. I

think The Pensions Regulator ought to have a similar objective for trustees. Members should be given the right information, and that goes beyond telling them that they have a transfer value.”

Nolan adds: “It’s increasingly popular to quote a transfer value at retirement. That is a difficult balance to draw. Its right to tell your members about with it, but it’s easy to go from informing people to advertising options that might not be in their best interests. A good offering explained in the right way is fantastic.”

Sometimes, it’s a no-brainer to take the transfer. Nolan uses the example of a woman he spoke to when he was helping a client with a transfer exercise. “She had a pension of something like £15 a year that she could claim. We said, ‘if you want, you can have £300 instead.’ To us it was just an admin issue of trying to clear people out of the scheme and not having to worry about keeping the records and tracing them when they are due to retire. She rang up and said ‘you have absolutely transformed my life with that money’”

How? “She said: ‘I broke my glasses two weeks ago and I haven’t been able to afford another pair. I’m going to buy a pair first thing tomorrow and watch *EastEnders* and actually be able to see what’s going on!’”

For others, the decision to transfer



will be more complex. Nolan thinks of members in three tiers. The first tier is those with very small DB entitlements – in which case, it often makes sense to take the money as a lump sum, as the woman did in Nolan's example. The second tier have mid-sized pots. Their DB pot is typically a significant asset to them. Therefore, the choice of either cashing in all their money or keeping it in the DB scheme is a large one. Therefore, most are currently leaving it in their DB scheme.

Those with the biggest DB pots are often most open to considering their options. "For people at the top end, it's a great bit of flexibility," says Nolan.

People with weighty DB entitlements are often higher earners, who are typically more financially sophisticated. "This is the group who often want to release capital, and perhaps buy a buy-to-let property or pay off a big mortgage if they haven't done that already. They are likely to be more financially open to opportunities and able to take advantage of those," explains Nolan.

### When advice is right

Schemes will be impacted in different ways if large numbers of members decide to transfer out, depending on the degree of investment risk they are taking, as well as the types of assets in which they are invested.

Even if it is advantageous for a DB scheme to see a mass exodus of members, the hope is that employers will be

honourable in the way that they explain transfers.

For instance, Howorth says the main messages for schemes to communicate to members are for them to make a transfer decision based upon their personal circumstances and goals, and whether they can afford to take the risk that goes with losing the fixed annual income.

However, it would be very easy for companies to talk up the benefits of transferring out to members.

"Financial advice is the protection against that," says Nolan. "I'm hoping it will only be on the fringes of the industry, but you can imagine the desperate employer who happens to be the managing director and hired two of the trustees on the scheme; the member-nominated trustees are outvoted, and there's an aggressive attitude to trying to clear off liabilities that are less than the fair value to members. Members aren't in a position to judge that."

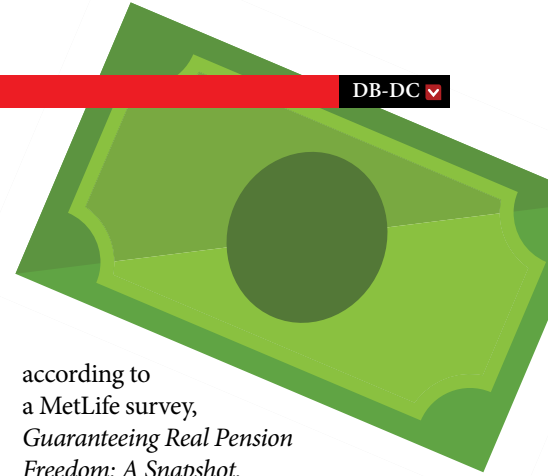
Yet some pensions consultants are concerned that there is a lack of suitably-qualified independent financial advisers (IFAs) who can help members who are pondering complex quandaries. Hatchett says: "It's hard in the retail space to find advice, and the advice is quite expensive because there's a high demand on advisers."

The issue has attracted the attention of the FCA, which published a note entitled *Advising on pension transfers – our expectations in January 2017*. The note cautions that IFAs should take a thorough approach to advising on pension transfers, considering the assets in which their clients' funds will be invested.

The note reads: "We are concerned that consumers receiving this advice are at risk of transferring into unsuitable investments or – worse – being scammed."

### What members want

Ultimately, most retirees want security. Three quarters of over 45s agree that guaranteed income for life is important,



according to a MetLife survey, *Guaranteeing Real Pension Freedom: A Snapshot*.

That's why partial DB to DC transfers could give members the best of all worlds, say Nolan and Hatchett. A partial transfer could give a member a one-off lump sum, whilst leaving some of it in DB, giving them a secure lifetime income.

Nolan says: "Partial transfers haven't been embraced by the industry, but I think they are a definite possibility. If you give people the opportunity to take part of the money out and leave part of the money in, that's easier."

Hatchett adds: "People are very comfortable with the idea that people can commute cash at retirement. If it was straightforward to take a partial transfer, I think people would take it. It could be the best of all worlds: you get some cash, you get drawdown, and you get a partial DB pension."

At the moment, partial transfers are relatively nascent. Administrators and schemes are not always making them available to members. However, Hatchett is optimistic that this will change. "Technology has a big role to play in terms of education and communication. In the modern world, this is all doable."

Written by Louise Farrand, a freelance journalist

