Pensions on Divorce

A guide to help you understand your options and what you need to do

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Introduction

Going through the process of separation and divorce is a very emotional time and the resolution of finances can often be very distressing part of it.

It will be a different experience for each person with everyone being understandably concerned for their own financial security and that of their family, so it is not unusual for the financial settlement to end up being the key focus of attention.

It's a time of great uncertainty that can be alleviated by taking advice and getting help and support.

The value of your pensions are likely to be one the biggest assets that need to be taken account in your financial settlement, and with the factors relating to pensions often being complex there is a possibility that settlements are reached where the full range of options have not been properly investigated or analysed.

Therefore, before you enter into any negotiations it is extremely prudent and sensible to know exactly what your pension assets are worth to you, both now and in the future, and also understand what your options are, so you can be as informed as possible during the negotiating phase and can appreciate what any settlement reached truly means to you.

This guide has been put together to help you understand what you ought to do during the various steps of the divorce process, what your options are and how once a settlement has been agreed, the outcome can be implemented.

Our guide is *not* meant to act as a technical document, rather it outlines and provides information to help you gain a better understanding. Whatever stage you are at with your divorce, if you have pension assets, you should seek out professional advice - from both a family lawyer and a pension specialist.

Where possible we've aimed to be write this in plain English, but to assist, you will find an appendix and glossary explaining different terms to aid your understanding.

When it comes to sharing pensions, the rules are the same for a divorce as they are for the formal dissolution of a civil partnership. Where we discuss 'divorce' throughout this guide, the same points and factors will apply to civil partnerships.

Please note: the laws applying in Scotland vary from those in England, Wales and Northern Ireland. Most of the basics are the same but there are some important variations in how the different payments may be treated. This guide focuses on the law applying in England, Wales and Northern Ireland.

Gathering information

Your solicitor will ask for information on all of your pensions as part of the financial disclosure process and depending upon the type of divorce that you and your partner engage with, it is highly likely that you will complete what is commonly referred to as a Form E. This form is used to gather all of your financial information and once completed is exchanged with your partners solicitor as part of the disclosure process.

The Form E is light in information it asks about pensions. The basic information to gather to complete the pension section is:

I. Name and address of the pension scheme administrator or pension plan provider
II. Your National Insurance number
III. Type of scheme
IV. Scheme or Plan number
V. The cash equivalent value of the scheme / plan and the date it was valued
VI. If the scheme is defined benefit, is it currently paying reduced transfer values, if so what is it
VII. Is the pension in payment or drawdown

You can refer to the appendix for helpful information on completing Form E

Financial planning assistance you may need at this point

Pensions can be complex and knowing what information to gather and how to assess it once received can be a daunting exercise. An experienced divorce financial planner will be able to take away from you some of this hard work, by efficiently gathering all of the information you need for your Form E and more.

As mentioned, the **Form E** asks only for basic information, extending the gathering of data to include all of the features, benefits and intricacies of your pensions, will allow for a comprehensive picture of your current position to be created.

A detailed analysis of all pension held and the options available in relation to each, with advantages and disadvantages of each option in relation to both parties can be put together, supported if appropriate with thoughts and ideas, so that you and your solicitor can start negotiations from a fully informed position.

Negotiating your settlement

In order to negotiate, in addition to fully knowing and understanding what you have and what it all means, you need to know what your options are. Your solicitor will explain these all to you, but in brief, as far as pensions are concerned, they comprise of::

Option	What is it??
Pension sharing	You receive a percentage share of any one (or more) of your partner's pensions. This is either transferred into a pension in your name or you may be able to join your ex-partner's pension scheme. If the pension is transferred to you and you don't already have your own pension, you'll have to set one up.
Pensions offsetting	The value of any pensions is offset against other assets. For example, you may get a bigger share of the family home in return for your ex-partner keeping their pension.
Pensions attachment order	You get some of your ex-partner's pension when it starts being paid to them. You can get some of the pension income, the lump sum or both. But you can't get pension payments before your ex-partner has started taking their pension.

More on Pension Sharing:

Advantages of sharing	Disadvantages of sharing
They provide a clean break between the two parties	They cannot be varied after the decree absolute. It's therefore important that the sharing is not applied for until the financial settlement has been agreed
Each spouse has control over their own pensions, in relation to the investment decisions and when to access the pension benefits	The order cannot be made on a pension with an existing attachment order. Therefore, if one of the parties has been divorced before ensure there are no exposing attachment orders.
Pension income drawn by the ex-spouse is taxed in their own name	

Pension sharing is available as an option where divorce proceedings began on or after 1st December 2000.

A court order will state the percentage split of the pension assets and the relevant part of the pension fund or benefits will be transferred from the scheme member to the ex-spouse.

The scheme member sees their pension fund or benefits reduced by the value of the amount transferred. This creates what is called a pension debit. The corresponding receipt by the ex-spouse is referred to as a pension credit.

The amount of the pension share is always defined as a percentage of the cash equivalent value (CE) e.g. a pension share of 47% of a pension with a CE of £650,000 will see a pension credit and transfer £305,500 to the ex-spouse and the member's pension would be reduced by the same amount to reduce their CE to £344,500. The pension debit and corresponding pension credit are always the same amount, £305,500 in this example.

Any future pension contributions or accrual of benefits made will be outside of this split, and belong to the individual making the contribution or with membership of the pension scheme. The amount transferred will not be assessed against the recipient's annual allowance, but it will be assessed against their lifetime allowance.

Pensions that can be shared	Pensions that cannot be shared
All rights under defined benefit and defined contribution schemes and plans and this includes pensions in payment.	The new state pension, where divorce proceedings commence on or after 6th April 2016
Some elements of the state pension, either the additional state pension or the protected payment amount	The basic state pension and graduated pension, if divorce proceedings commenced before 6th April 2016
Pension Protection Fund (PPF) compensation	

More on offsetting:

Advantages of offsetting	Disadvantages of offsetting
It allows a clean break between both parties.	One party may end up with no pension assets
It is relatively easy to administer.	Depending on the value of the assets involved, an appropriate split to retain the pension intact may be difficult to achieve
A court order is not required	Determining an accurate and fair valuation of the assets involved can be difficult.
	Death benefits from the pension may be lost and this may be detrimental to the ex-spouse.

On your divorce all of your assets and those of your ex-spouse or partner are taken into account. If you decide to opt for offsetting, each person retains their pension assets, but these are then offset against the other assets – for example, if one person has a large pension pot, the other may receive the house (assuming it has a similar value).

As an example, a husband has a pension valued at £300,000 and the couple jointly own a house valued at £600,000. Offsetting would allow for the pension to be traded against the house and the husband may keep the pension, the wife the house or some other trade-off based on the respective values.

The difficulty though is that £1 pension does not equate to £1 of equity in the home. For this reason, specialist help may be needed to help arrive at a fair outcome.

In this example, if the husband retains all pension assets, the wife would have no future claim on it or share in it.

Advantages of attachment	Disadvantages of attachment
Both parties can benefit from a generous pension entitlement into the future: the nature of earmarking favors a situation where the future pension will accrue with both parties able to benefit.	The ex-spouse has no control and is dependent on receiving their pension entitlement whenever their former partner decides to retire. In addition the scheme may change in future years, the member may choose to reduce benefits or even in an extreme case forego the future pension in favor of other means of saving.
Pension death in service benefits can be earmarked for the ex-spouse.	The income from the pension is payable first to the member and only then paid over to the ex-spouse as part of the court order. This creates a tax charge which is based on the member's rate, which could easily be a higher rate than the ex-spouse's, creating an unnecessary tax liability (compared to other options).
Where a pension is already in payment through an annuity, the ex-spouse can have a proportion of the ongoing annuity payment.	If an ex-spouse decides to remarry the attachment order will cease to apply.
	The ex-spouse will lose all of his/her entitlement if he/she is pre-deceased by the ex-partner.
	Parties will need to remain in contact to 'manage' the ongoing pension situation between them.

As you can see from this extensive list of disadvantages, attachment is rarely considered to be a suitable way of dealing with pension assets on divorce. There are exceptional circumstances where it might be used, but we would expect these to be very unusual.

Pension attachment is an agreement that when a pension comes into payment, a part of it (a set percentage is paid to the ex-spouse (or ex-partner). The relevant pension scheme provider receives a written instruction from the court to make this payment.

In England, Wales and Northern Ireland, the payment can be taken from a pension and/or cash lump sum.

If you are also entitled to a lump sum payable on your death, the Court can also instruct that some, or all, of this is payable to your ex-spouse or partner or vice versa to you. Although the proportion of your pension payable to your ex-spouse or partner is set at the time of your divorce, each party can apply to the Court for the amount to be varied.

An attachment order does not give any ownership rights to the pension, as would be the case with a pension sharing order. If the member subsequently decides to transfer pension benefits which have an attachment order, the order must be passed to the new pension scheme and the ex-spouse must be advised of any transfer within 14 days of the date of the transfer taking place.

What can be covered by an attachment order	Pensions that cannot have an attachment order
Pension Income	State Pension benefits
Pension commencement lump sum (tax free cash)	Dependents pensions payable on death (either before or after retirement)
Lump sum payments on death before retirement	

A focus on pension sharing

So, financial disclosure has taken place, you have discussed your options with your solicitor and the sharing of your pensions is one that you wish to explore and pursue further, what happens next?

A pension differs to all other matrimonial assets, in that it is something that is designed to provide you with an income in retirement, yet, as a result of a recent change in legislation access to all of a pension fund in one go is now available from age 55. Importantly, though, this change only applies to defined contribution schemes and not defined benefit schemes.

The introduction of these pension freedoms has re-focused attention on how pension assets are treated for divorce purposes, is it best to view them as a capital item, in the same way as a property or savings held in a bank or building society or are they best treated as a source of regular income.

The issue arises because different ages of married couples and civil partners, combined with different life expectancies of men and women mean that two pension pots of the same value may produce very different incomes in retirement.

The most common held view is that pensions remain a source of income in retirement and when considering a pension share, a settlement is best based on a division of income.

In order to calculate the pension division necessary to provide equality based upon income and not capital, it is usual for your solicitor to instruct a pension expert, an actuary or experienced financial planner, to prepare a pension report for you, based upon the potential settlement you are looking to achieve. Guided by instructions from your solicitor, the report will set out some recommendations as to how best to share the pension assets that exist.

These reports will state what percentage of the capital value (CE) of a pension (s) will need to be shared to create the equality of income sought, as per your solicitors letter of instruction.

Financial planning assistance you may need at this point

You are at a point, where you have been negotiating for a fair and reasonable settlement and close to agreeing an outcome. It can be difficult to picture at this most important time what your financial future will look like post-divorce, based upon the pension share that is likely to be agreed and how other matrimonial assets are going to be divided.

A financial planner can help you test drive your financial settlement and predict the long term financial effects of different potential settlements, showing you the financial effect on your lifestyle; In addition, they can explain the advantages and disadvantages of the various options when including pensions in the settlement.

The money you receive from your settlement is not a means to an end in itself. It is what you can and want to do with the money you receive that is most important.

Your future plans may include a new house, and paying for your children's university fees. In retirement, you may aspire to travel and also conscious of the need to think about life events like your children getting married and your own long term care.

Being able to picture how a financial settlement can work out for you may just give you the confidence you need to progress.

Implementing a pension sharing order

You've reached an agreement and it has been approved by the Court, and you have been awarded a pension credit, which now needs to be implemented.

It may be possible for you to retain the pension credit in your ex-spouses scheme (this is known as the 'in-scheme' option or it may be necessary, or preferable, for the pension credit to be transferred out to another pension arrangement. The scheme trustees/scheme provider will need to decide which of the two options they are prepared to offer.

'In-scheme' option:
Your ex-spouse scheme retains the pension credit or offers that option. A scheme may say that pension credits must be kept in-scheme and once in the scheme, the ex-spouse enjoys similar rights to those of a normal member, including the option to transfer the benefits out. A common phrase for this type of scheme membership is a shadow member.

'Transfer out' option:
Your ex-spouses scheme may decide that pension credit benefits cannot be retained in the scheme. This means that you will need to choose a scheme to transfer the pension credit into. This could be an existing pension scheme that you are a member of or you could establish a new pension scheme to accept the pension credit.

With an occupational pension scheme, if the ex-spouse does not notify the trustees where they wish the pension credit to be transferred, the trustees may nominate a default option to receive the pension credit.

Pension trustee's/manager's obligation
Pension trustees/managers paying a pension credit have to ensure that they have dealt with the payment within the 'implementation period'. This is a period of four months from the day on which the order takes effect or, if later, when the trustees/managers are in receipt of all relevant documents to proceed with the order (i.e. the order/provision, the matrimonial documents, details of the scheme to which the pension credit is to be transferred, and other scheme requirements).

Failure to act within the 'implementation period' may result in a fine from the Pensions Regulator (TPR).

Financial planning assistance you may need at this point

Your financial planner will be able to find out for you and explain to you what pension sharing options are available, be it in-scheme, transfer out, or both.

They will be able to talk you through the advantages and disadvantages of each option and where and if necessary look at recommending the most appropriate new home for the pension credit.

In doing this, this could well be inclusive of reviewing any and all other pensions you hold, as well as fully understanding your views on investing money so, where, the pension credit is placed into a defined contribution plan it is invested in a manner that matches your attitude to investment risk.

Once the most appropriate solution has been sought and agreed, your planner can help with all of the administration needed to successfully implement the sharing order, this including communicating with all pension providers / administrators on your behalf.

It may be that you will benefit from ongoing and regular reviews of your pensions and other assets to make sure you are on and remain on track to achieve all the future plans that you have. Your planner should be able to construct a planning service to suit your ongoing needs and requirements.

About the author

This guide has been put together by **Paul Gorman**. Paul is a Chartered Financial Planner and has been accredited by Resolution as a specialist in financial planning on divorce. Paul is the leading adviser at Beaufort Financial.

Paul's specialism is planning and advice to individuals going through divorce and separation.

Beaufort Financial has been providing financial planning and advice to our clients since 1999 and have been part of and members of the *Beaufort Group* since 2013.

Our approach to financial planning and advice means, that you can be assured, we will:

- *listen, until we fully understand what you want your money to do for you,*
- *talk, in plain and simple language.*
- *put together solutions to help achieve your needs and objectives.*
- *communicate regularly to manage what we put in place and help keep you on track.*

Our financial planning service

Financial planning is a very personal matter. No two people have identical circumstances, ambitions and needs. What's more, needs often change over time and everyone's financial situation is different. The financial plan we produce for you is also unique and individually tailored to suit your particular needs.

Appendices

Helpful Information for completing Form E:

Type of Scheme

The pensions you have will typically be one of two main types:
Defined Benefit (also known as final salary or superannuation schemes):

These schemes provide you with an income in retirement that is based upon the numbers of years you have worked with a particular employer and been a member of their pension scheme and your salary during your period of employment. Your pension builds with each year of service *e.g. your pension may be based upon 1/60 of your salary for each year of service, so after 20 years of service you will have amassed a pension entitlement of 1/3 of your salary.*

The pension that you are a member of through work, or any previous employment you may have held, could be a defined benefit scheme.

Defined Contribution (also known as money purchase pensions):

With a defined contribution pension you build up a pot of money that you can then use to provide an income in retirement. Unlike defined benefit schemes, which promise a specific income, the income you might get from a defined contribution scheme depends on factors including the amount you pay in (and maybe how much your employer pays in), the fund's investment performance and the choices you make at retirement. Whilst, not exhaustive, below we list different types of defined contribution schemes:

- Personal Pensions
- Self Invested Personal Pensions (SIPP)
- Small Self Administered Schemes (SSAS)
- Retirement Annuity
- Section 32 buy out plans

In the appendix you will find a useful form to help you gather the initial information you need.

The Cash Equivalent value (CE):

The cash equivalent value of a defined contribution pension is the generally easily identifiable as it is the value of the assets in the plan. Note, that seeking both a fund and transfer value is wise as this will identify any potential penalties that may arise if the plan is shared on divorce.

The cash equivalent value of a defined benefit scheme is calculated by the pension scheme actuary on behalf of the scheme administrators of the scheme and is essentially what they believe the capital value of the pension that you have accrued to date to be and if for a current employer's pension scheme, is based upon you leaving service at the valuation date.

The form E asks for whether the scheme is paying reduced transfer values. This is important as it will give an indication about the schemes funding position.

The state pension:

A new State Pension was introduced for people reaching State Pension age from 6 April 2016. The intention is that people should build up the pension in their own right and that it should be a foundation for private pension saving. For this reason, it will no longer be possible for spouses or civil partners, whose National Insurance (NI) record starts in the new scheme to be awarded a shared pension based on the other party's NI record by the courts. The new State Pension will not be available to the courts as a sharable asset in divorce settlements.

In brief, under the old state pension rules, what is termed the additional state pension is shareable and under the new system, what is termed the Protected Payment is shareable.

As a result of these changes, there is a transition period for some aspects of the new State Pension and this includes the sharing of pensions on divorce, with there being substantial differences between the old and new arrangements.

Whether the old or new arrangement will apply to you will depend on the date on which the divorce proceedings start. To avoid disrupting proceedings that have started under the existing rules but will not be finalised until after the new rules come into force from 6 April 2016, where divorce proceedings start -

Before 6 April 2016, then the existing arrangements apply and the additional State Pension is shareable; or

On or after 6 April 2016, then the new arrangements apply and the Protected Payment is shareable.

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On or after 6 April 2016, then the new arrangements apply and the Protected Payment is shareable.

Glossary

Scheme	Brief Explanation
Personal Pension	A personal pension is primarily aimed at individuals who are not eligible to join an employer's pension scheme or wish to top up their retirement savings. Personal pensions are not restricted by a cap on charges and therefore tend to offer a wider range of investment opportunities and retirement benefit options than stakeholder pensions. This flexibility provides greater scope to tailor your pension plan to your circumstances.
Self Invested Personal Pension (SIPP)	A SIPP is a personal pension primarily aimed at individuals who require greater control and choice over where their pension assets are invested. You can invest in a range of assets directly via a SIPP including company shares, government bonds (gilts) and commercial property.
Small Self Administered Scheme (SSAS)	Small self-administered pension schemes (SSAS) are generally set up to provide retirement benefits for a small number of a company's senior or key staff. A SSAS can invest in assets that aren't generally available for many other types of scheme to invest in. As an example, a SSAS is able to purchase the company's trading premises and lease these back to the company.
Retirement Annuity	A retirement annuity provides income for either a fixed term or for life. The level of income provided is dependent upon age, state of health and certain lifestyle choices, the prevailing annuity rate, the size of your pension fund, and the options and benefits selected at outset.

Section 32 buy-out plan	These are special schemes as they were able to receive transfers which included contracted out benefits known as Guaranteed Minimum Pensions (GMP), these broadly represent pension income that you would have received from the State Earnings Related Pension Scheme (SERPS) had you not contracted out. There is a requirement placed upon these schemes to pay out at least the GMP at retirement and the provider should make up any shortfall in the policy.
Annual allowance	The annual allowance is a limit to the total amount of contributions that can be paid to defined contribution pension schemes and the total amount of benefits that you can build up in defined benefit pension scheme each year, for tax relief purposes. The annual allowance is currently capped at £40,000 although a lower limit of £10,000 may apply if you have already started drawing a pension. The annual allowance applies across all of the schemes you belong to, it's not a 'per scheme' limit and includes all of the contributions that you or your employer pay or anyone else who pays on your behalf.
Lifetime Allowance	The Lifetime Allowance is a limit on the amount of pension benefit that can be drawn from pension schemes – whether lump sums or retirement income – and can be paid without triggering an extra tax charge. Its current level in the 2020-21 tax year is £1.07m having been reduced from £1.25 million.
Pension Credit	In relation to pension sharing orders, Pension Credits are either by way of internal or external transfer within the member spouse's pension scheme. An internal transfer, if permitted, allows the non-member to join the existing scheme. An external transfer will be a calculated proportion of the member's scheme benefits to be transferred out of the existing scheme into a new scheme.
Pension Debit	Pension Debit is the amount that the pension fund or benefits are reduced by when the agreed split is transferred to the ex-spouse.

Beaufort Financial Birmingham offices:
Suite 46 Hilton Hall, Hilton Lane, Essington, Staffs. WV11 2BQ
27 Waterloo Place, Leamington Spa, Warks. CV32 5LA
Tel Number: 01902 863494
Email: birmingham@beaufortfinancial.co.uk