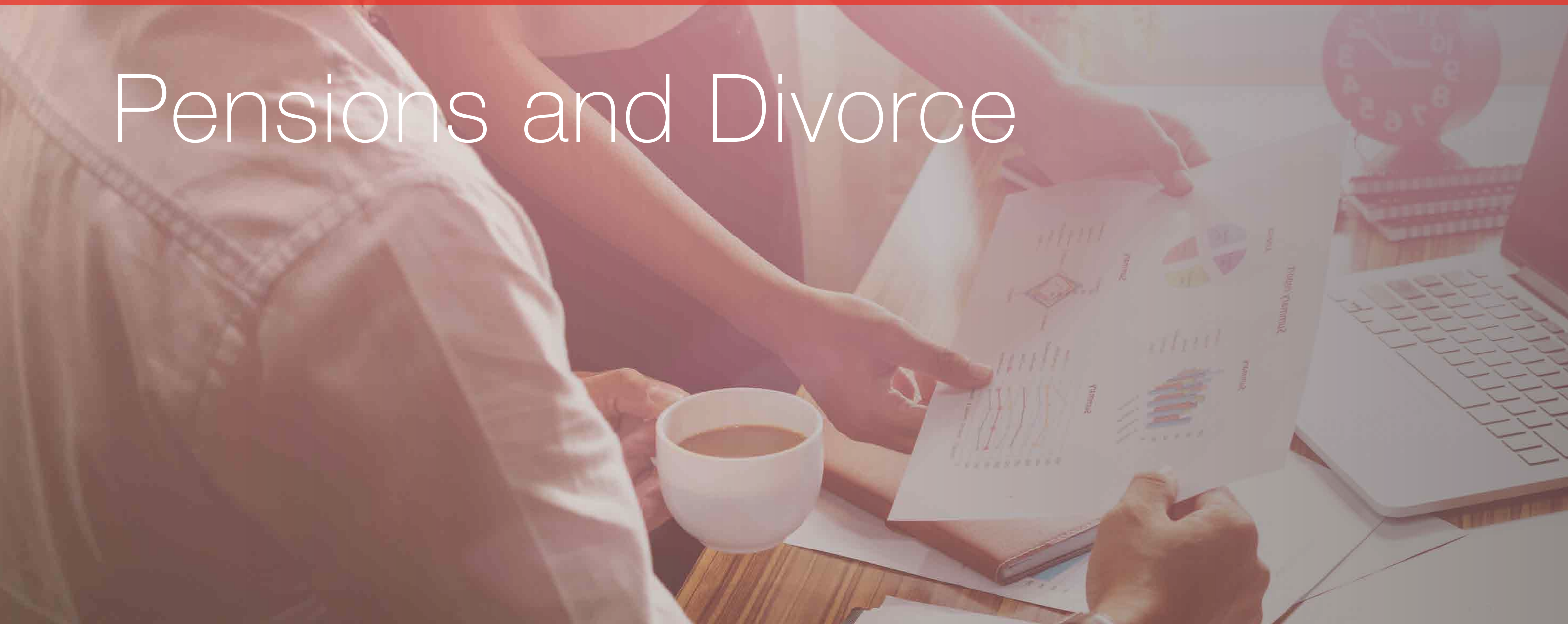
Kingston Smith
Financial Advisers

Your potential, our expertise

Pensions and Divorce



Pensions are a hugely complicated area of personal financial planning and can be a minefield for legal professionals trying to achieve an equitable division of assets.

Specialist pension advice is essential as early as possible in divorce proceedings to:

- Find the pensions
- Value the pensions
- Decide how to share the pensions
- Implement pension orders

KSFA can provide all of the guidance and advice necessary to help legal professionals understand the complexities of a couple's pension arrangements.

Finding pensions

KSFA have relationships with all of the major pension providers and in many cases have dedicated contacts with whom we can liaise.

We can assist in locating pensions and obtain information in a timely fashion from the relevant providers or by using pension tracing services.

Valuing pensions

Pension details are commonly collected as part of the Form E Financial Statement, but the information usually assembled is very basic and focuses on the cash equivalent transfer value of the pension pot, which may be a very poor way of determining the true value of the assets within the context of a couple's financial position.

Understanding the finer details and nuances of the pensions is essential to provide a full understanding of how they could be valued and this in turn will provide guidance on the most appropriate means of dividing the assets.

Examples of some of the difficulties inherent in valuing a pension:

A defined contribution pension may have a transfer value of £100,000. However, it may also include a guaranteed annuity rate of 9% that would be lost on transfer; arguably, the true value would be considerably greater than £100,000 as the annuity or sustainable drawdown income that could be generated from this would be far lower than £9,000 per annum.

Pension funds may have **exit penalties** so that if they were transferred, the value to the ex-spouse is lower than the face value if retained by the member.

For defined benefit schemes, the **actuarial assumptions** used to arrive at the cash equivalent transfer value can be challenged. Actuaries will use different figures for interest rate assumptions, RPI and other discount factors. Challenging these assumptions could result in an alternative valuation that may be higher or lower than the scheme actuary's estimate.

Some pensions may have **protected tax-free cash** that is in excess of 25%, which would be lost on transfer. This may increase the value of the pension to the member above its face value to the ex-spouse.

If the Court order is intended to create income parity, the poor health of one of the couple may mean that an enhanced annuity could be purchased, requiring a smaller amount of pension fund to generate a given level of income.

Pensions and Divorce

Understanding the impact on the member or ex-spouse's **Lifetime Allowance** is essential to ensuring the best outcome.

A pension credit will count against the ex-spouse's lifetime allowance (LTA), unless it was implemented before 6 April 2006 or derives from a pension in payment, in which case an enhanced lifetime allowance will apply.

However, the corresponding pension debit will not usually count against the LTA of the member, allowing the member to rebuild his or her pension rights to the maximum possible extent following a divorce. Some exceptions apply where members have primary or enhanced protection.

How to share the pensions

There are now four options for dividing pensions. KSFA can help clarify which may be appropriate, based on the type of pensions owned and the specific features.

Pension offsetting - the value of a pension is set against other assets, e.g. one party gets the house, the other the pension.

This is the oldest and simplest form of pension division, but may deprive one party of a source of income in later life. Understanding couples' wider financial planning is essential to determine if this is appropriate.

Pension attachment (earmarking) - the Courts earmark the member's pension rights for the provision of benefits to his/her ex-spouse in the future. Rules vary slightly between Scotland and the rest of the UK.

This method is rarely used: it does not provide a clean break, the member retains control of the assets, the benefits are taxed on the member's income position not the recipient's and the earmarking order is terminated if the ex-spouse remarries or the member dies.

Pension sharing – alongside offsetting, this is the most common practice. The ex-spouse receives a pension credit that may be transferred to a new or existing scheme, or it may remain in the existing scheme.

Members' benefits are divided as a percentage of the pension transfer value or, in the case of defined benefit schemes, as a percentage of the retirement income.

Uncrystallised Fund Pension Lump Sum (UFPLS) – introduced as part of the pensions freedom legislation in 2015, a Court could order pension rights be shared as a lump sum drawn from a money purchase arrangement. This is only available for those over 55 and with a pension fund capable of making such payments.

This may well have unwelcome tax consequences for the member and result in less than anticipated going to the ex-spouse: 25% of the fund would be paid tax-free, but the remainder would be taxed on the member's income at their highest marginal rate. It would also restrict the member's ability to fund future pension contributions.

Implementing pension orders

KSFA are a chartered firm of independent financial advisers regulated to give advice on even the most complex of pension transfers.

We can provide guidance on the likely costs and the options available to the member to help them understand how this may fit into their overall financial planning.

Cash Flow Modelling

KSFA use cash flow modelling, which can be beneficial to the construction of a financial plan for both parties. It illustrates to clients how their financial situation and a proposed settlement may impact on their future goals.

The model can also act as the foundation on which to build future planning.

We use very powerful, visual and flexible cash flow modelling software that helps us to:

- Assess an individual's current financial situation
- Highlight shortfalls and risks to their financial security
- Build custom 'what-if' scenarios/simulations to illustrate various settlement outcomes
- Present complex information in a visual and easy to understand format.

Contact us

To find out more about KSFA's bespoke services and to see how we can help you, please email **advice@ksfa.co.uk** or visit **www.ksfa.co.uk**

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