Pension Advisory Group – Legal Issues: draft guidance for consultation

April 2018

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Consultation questions

By contrast with the Expert and Valuation Working Group's report, we have not singled out discrete issues in this Legal Working Group report as a focus for consultation.

Instead, we invite consultees to respond to the paper with any points that occur to them, using the pro forma provided, but in particular we ask:

- Generally, do you agree with our account of the law (particularly in Parts 2-5)? Please identify any areas where you do not agree.
- How clear/useful do you find the information provided throughout the document?
- Do you agree with the key best practice recommendations (summarised in the table near the start of the document)? Are there other key points that might usefully be added to this list?
- Are there any areas in relation to which further practice guidance might prove useful?
- Do you consider that the suggested disclaimer letter (Appendix 2) to be used with clients who decline advice to obtain a pension expert's report would be useful or effective?
- Are there any areas not covered in Appendix 3, which collates issues beyond the remit of the Pension Advisory Group (as requiring amendment to primary or secondary legislation or institutional action), that you would like to see added to that list?

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1 Introduction, overview and summary of key recommendations

This guidance seeks to explain the most critical legal issues facing practitioners, the judiciary and the public in the area of pensions on divorce.[1] The objective in this comparatively brief narrative is to inform and to suggest good practice.

It comes as no surprise to anyone experienced in this field that, even 17 years after the introduction of pension sharing, all of the professionals involved (lawyers, the judiciary and pensions experts) are still by no means comfortable with the issues that confront them. This may be due to the diverse nature of pensions and the myriad different regulations that govern them. It may also be due to the fact that there is very little in the way of guidance from the higher courts. Where such guidance does exist, there is no clear consistency of judicial thinking and the decisions relate, in the main, to bigger money cases that are not the mainstream work of the Family Court. Furthermore, for understandable reasons, the majority of reported cases relate to high value claims, whereas the vast majority of applications made or settled in family courts up and down the country are much smaller needs-based cases. All of this may be reflected in the fact that offsetting remains the most commonly adopted remedy.

Pensions are not alone in being an area where family law overlaps with other areas of law: trusts and company law are other examples. However, it remains the fact that for many family lawyers pensions law (and the associated tax implications) remain foreign territory.

It is hoped that this working paper will draw attention to potential pitfalls and provide a good practice guide. Our recommendations, made throughout the body of this document and with key points collated on the following page, include suggested guidance aimed at achieving consistency of approach.

In various places, we refer to the exercise of judicial discretion on particular points – we do so mindful of the fact that the vast majority of cases are, of course, not adjudicated at the end of contested proceedings, but are settled with or (more commonly) without contested proceedings being initiated.

Useful other materials:

- Family Procedure Rules 2010, Part 25 and Practice Direction 25
- Law Society, *Family Law Protocol*
- Resolution, *Guidance Note on Instructing Expert in Financial Remedy Proceedings*
- The Pensions Advisory Service, *When relationships end: pension sharing* www.pensionsadvisoryservice.org.uk/about-pensions/when-things-change/when-relationships-end/pension-sharing
- Pensions Ombudsman decisions, at www.pensions-ombudsman.org.uk/our-decisions/)
- Family Justice Council Guidance on needs www.judiciary.gov.uk/wp-content/uploads/2013/04/guidance-on-financial-needs-on-divorce-june-2016-2.pdf
- There are several valuable articles in *Family Law* on pension-related issues, including:
    - 'Apples or Pears: pension offsetting on divorce' [2015] Fam Law 1485
    - 'Comparing "apples and pears"' [2016] Fam Law 500
    - 'Pension Offsetting' [2017] Fam Law 204
    - 'Critical Timing of Decree Absolute: Unexpected Death' [2017] Fam Law 871

[1] And in the event of civil partnership dissolution – whilst contained in separate legislation, the law is in substance identical. All references in this document to spouses/divorce and related terms should be taken also to refer to civil partnership and its dissolution.

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Key recommendations for practitioners

The numbers in square brackets refer to sections / paragraphs of this guidance

- Try to determine at an early stage whether a case is needs-based or involves sharing (i.e. where the assets exceed what is required to meet needs), to help evaluate the nature of such expert evidence as may be required. This will also enable any letter of instruction to an expert to be focused on the approach the court is likely to adopt, keeping costs to a minimum [2]. Where proceedings are contested, this will ultimately be a matter for judicial discretion.
- In the majority of sharing cases, where assets exceed needs, a capital division by reference to the CEs will be appropriate and no expert evidence will be required [4].
- There are other situations where no expert evidence will be required [4.5].
- In a needs-based case, the appropriate approach will often be an equalisation of incomes, requiring expert evidence. However, the question of whether equalisation of income is appropriate will be very fact-specific and, if contested, a matter for judicial discretion [4.4] and [4.6].
- Where the issue of off-setting is clearly identified as a particular issue in the case, commissioning expert advice will sometimes be justified. [4.2, 4.7] and [5].
- Caution is required where there is an existing pension attachment order and it is possible for the pension holder to take advantage of the pensions freedoms created by the Taxation of Pensions Act 2014 [6].
- Be wary of income gap syndrome [7]. Be aware of possible ways of mitigating the problem [7.2].
- Be familiar with the procedural requirements of obtaining an order [8] and [9] and post-order [14].
- Don't overlook the state pension [10].
- Be familiar with the specific complexities of individual public sector pension schemes [11].
- Be aware of the specific factors that need to be borne in mind where a pension sharing order is made on a variation application [15].

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2 Treatment of pensions in "needs-based" and "sharing" (non-needs) cases contrasted

An important initial question is whether pensions should be handled any differently, according to whether the case is governed by the needs principle (where the assets do not exceed the parties' needs), or the sharing principle (where the assets do exceed needs). The vast majority of cases – including cases involving low £millions – will be needs-based. Given the lifetime allowance, even a "big" pension case will usually be a needs-case – it is non-pension assets that will generally take a case out of the needs bracket. However, it is essential to bear in mind that "needs" and "sharing" are but two strands of the overall search for fairness; they are not mutually exclusive.

In needs-based cases, just as is the case with non-pension assets, the timing and source of the pension saving is not necessarily relevant – that is to say, a pension-holder cannot necessarily ring-fence pension assets if, and to the extent that, those assets were accrued prior to the marriage or following the parties' separation. In a needs case, the court can have resort to **any** assets, whenever acquired, in order to ensure that the parties' needs are appropriately met.[2] By contrast, in a "sharing" case, the question of whether all or some of the pension assets are to be treated as "non-matrimonial property" and so not ordinarily to be distributed pursuant to the sharing principle[3] is a live one.

Pensions are, of course, just one class of asset to be brought into account in the wider s 25 exercise, which is aimed at achieving a fair outcome in light of the s 25 checklist factors and the governing principles derived from case law. It would be wrong to suggest that potential or actual actuarial evidence concerning the pension assets gives greater mathematical guidance to determine the *overall* outcome of any application than is the case with other resources. But such evidence will often be important to ensure that the nature and extent of the pension assets is properly understood, as part of the s 25 determination.

It is recommended that early consideration be given to whether any case is likely to be determined on the needs or sharing principle, particularly in considering whether or not it is necessary and proportionate to instruct an expert.

Readers should also refer to the Guidance for the judiciary on financial needs on divorce published by the Family Justice Council,[4] Annex 3, which deals with pensions.

[2] See *White v White* [2001] 1 AC 596, at 610, *Vaughan v Vaughan* [2010] EWCA Civ 349, [42].

[3] See generally *Miller, McFarlane* [2006] UKHL 24; *Charman v Charman (no 4)* [2007] EWCA Civ 503; *Scatliffe v Scatliffe* [2016] UKPC 36, [25](v)-(x).

[4] www.judiciary.gov.uk/wp-content/uploads/2013/04/guidance-on-financial-needs-on-divorce-june-2016-2.pdf, due to be published in a 2nd edition later in 2018.

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3 Pensions: deferred income or capital?

A second important question is how pension assets should be treated: as (deferred) income or as capital? Does the answer to that question vary according to the circumstances and/or type of pension? If so, when is one approach more appropriate than the other?

The answers to these questions are case-specific rather than pension-specific. There is no difference in approach between defined benefit and defined contribution cases. The treatment of the asset depends on the use to which the pension asset is to be put.

Three basic points can be simply stated:

- If it is clear that either or both parties will draw a tax-free lump sum (whether commuted or not), this should be treated as **capital**.
- The balance of the pension fund, or all of it if no lump sum is to be drawn, should usually be treated as **deferred income**.
- A pension in payment is to be treated as a **current income** stream.

The pension 'freedoms' created by the Taxation of Pensions Act 2014 (discussed later in this guide) do not necessarily impact on this analysis, save in cases where the whole of a pension may be drawn to meet the particular circumstances of a case. However, tax will usually be paid on such a withdrawal and the *net* sum made available should be treated as capital.

Nothing in what has just been said implies that a line between capital and income is always required: the court will wish to ensure that the *overall* provision of money, or money's worth, is fair, whatever form it takes.

Reference should also be made to section 4.2.

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4 Equalisation of pensions between spouses in principle

The next major question is whether the aim should, in principle, be to equalise the spouses' pensions. The answer to that question varies according to the circumstances and in some cases it will be necessary to appoint a Pension on Divorce Expert ('PODE') to give advice – we outline the sorts of cases in which that would be particularly prudent at 4.7 below. Before exploring the basic question further, however, we first issue an important warning.

4.1 Do not lose sight of the overall aim of fairness: this will often entail unequal division

It is important to bear in mind that there can be no universal aim to equalize either income or capital. Leading case law is clear that the aim is to achieve an outcome that is fair overall to both parties. There is no reason why pensions should be equalised to a greater or lesser extent than other resources. As Lord Nicholls noted in *White,* in most cases, a fair outcome will be one that – for good reason – produces an overall division of assets that is *unequal*.[5] So, just as with non-pension assets, there will be many cases in which equality (whether of CE or income) will not be the fair result, whether because of the parties' respective needs, health or ages, or the length of the marriage, or – in non-needs cases – the non-matrimonial nature of the pension assets.

With that important caveat in mind, the rest of this section of the guide explores the contrast between equalisation of pension capital and income. However, readers must not lose sight of the fact that there will be many situations in which particular features of the individual case mean that equality (either of CE or income) is **not** the fair result.

4.2 The nature of pension assets and orders

Pension orders (other than certain pension attachment orders) are "capital" awards in the sense that the case law as applied to capital (rather than income) applies to pensions. This is because they are accrued at the point of separation/trial.

However, pensions are different from non-pension capital in that:

a. Their dominant purpose is usually to provide income in retirement.
b. Different tax considerations apply.
c. By their nature they are difficult to divide "equally". This is true both as a matter of approach (income or capital) and as a matter of practicality (complexities associated with pension funds). This section of this guidance deals only with approach and not practicality – see also paragraphs 31 – 40 of The Valuation and Expert Issues Report.

That said, in the bigger money cases, especially where a pension fund can be converted into cash (see section 6 below), or be the subject of drawdown, the pension may simply fall to be treated in the same way as other capital assets, without the need for any expert input; in this context, we endorse the views expressed by the FJC Needs Guidance Report. This issue is discussed in more detail in the Valuation and Expert Issues Report at paragraph 20.

Pension sharing can only be achieved by court order. Information as to the amount of income that any pension or pension share will generate can be obtained by commissioning an expert's report. In every case, the parties and those assisting them (whether lawyers, mediators or any other advisor) will need to consider whether the commission of a report is appropriate. The test for the instruction of an expert in contested applications is that the instruction must be "necessary" to assist the court to resolve the

[5] [2001] 1 AC 596, at 605-6.

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proceedings.[6] Cases in which it may not be considered necessary are described below, at para 4.5, while para 4.7 attempts to provide guidance on situations where an expert's report is thought good practice.

There are many cases in which the parties will not be considering pension sharing at all: they will prefer to offset the pension assets. This alternate approach is dealt with elsewhere in the guidance. However, note that expert advice may also be "necessary" where offsetting is being considered in order to be confident that the proposed "offset" is indeed appropriate.

4.3 Impact on pension assets of seeking equality of income

A further consideration (that trespasses on the technical aspects of pension sharing) is that equality of income (or at times, CE) may be an approach that diminishes the pension assets. This may be the case with some defined benefit schemes and where there is a Guaranteed Annuity Rate or any other type of guarantee.

4.4 The case for equalisation of incomes?

The lifetime allowance is at the date of writing £1,000,000. This means that, in the majority of cases, pensions are not likely to generate vast incomes. It follows from this that, in most cases, in order to carry out the s.25 exercise the court will need to know what the parties' incomes are likely to be in retirement both before and after the effect of any order the court may make. Furthermore, in so far as the object of the pension fund is to provide income in retirement it will often be "fair", where the pension has been accrued during the marriage **or** where needs are the dominant feature of the case, that the parties should have the same income in retirement. Given the likely level of pension income, a division that pays little or no attention to income-yield may have the effect of reducing the standard of living of the less well-off party significantly. In the majority of cases where (a) pension sharing is appropriate and (b) equalisation is the object (as to which, see 4.1 above), the pension assets should be divided so as to create equality of income.

Other parts of this guidance address the issue of how to create equality of income – assumptions, methods, annuities etc. See, for example, paragraphs 31 – 35 of the Valuation and Expert Issues Report April 2018.

4.5 Cases where division of CE may be preferred

In the situations described below, pension CEs can usually be divided equally without the need for further analysis or an expert report (as to which, see further 4.7 below). These examples are not exhaustive. There may be other scenarios in which, after due consideration, the parties, their advisors and /or the court will conclude that division by CE will do justice. In each of the scenarios below, it is assumed that the fair outcome is equal division. However, as noted at the start of this section, that will not always be the case. Readers should review all of sections 4.5 to 4.7 before deciding how best to approach their current case, as there are several variables that will potentially determine which approach is the fairer one, and whether expert advice is required to discern the better approach.

Case 1

The parties are the same (or almost the same) age and they have a defined contribution scheme or schemes with no implicit guarantees. Exceptionally, guidance may be needed as to the level of income generated, because if it is to be below a certain level this may have an impact on housing provision and/or periodical payment claims.

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[6] FPR 2010 Part 25.4 (3).

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Case 2

The parties are young (approximately under age 40). In this case, the potential minor departure from "equality" through the sharing of CEs would be justified by the number of variables that may occur over the intervening years between division and retirement – essentially, it is not proportionate to strive to create perfect "equality" other than by reference to the CE. This exception would not apply where one of the parties has a significant short career scheme (such as one with the Armed Forces or the Police), or a significant private sector Defined Benefit scheme CE, as equal division of CE can lead to very unexpected outcomes in such cases.

Case 3

In sharing cases (where assets exceed needs) and the pensions constitute only a small proportion of the total assets, there is a level of assets beyond which the analysis by an expert is not proportionate or necessary. For example: *SJ v RA* [2014] EWHC 4054: assets £28,000,000, of which pensions c. £2,500,000:

> "In cases where distribution is being made on a basis which is not guided by need it is, in my judgment, incorrect to distribute a pension fund on the basis of equality of income and there is no need for actuarial reports in the overwhelming majority of such cases".[7]

Case 4

The pension assets are *de minimis* in themselves. Total pension assets of less than £50,000 would be considered too small to justify the cost of an expert's report and even total pension assets of £100,000 might be considered a reasonable proportionality threshold where the couple are of equal or similar ages, even where defined benefit schemes are involved. However, care should be exercised if there is a choice of schemes to be transferred, in case the 'wrong one' is transferred and value is destroyed unnecessarily – see difficult situations listed in para 4.7.

Case 5

The sole pension in issue is a single public sector defined benefit scheme offering an internal transfer only.

Case 6

The pensions owned by both parties are all defined benefit schemes but the CEs are not large and are likely to mostly cancel each other out: e.g. one party has a defined benefit CE of £80,000 and the other a defined benefit CE of £130,000. While combined values are significant, they are both similar types of schemes. The difference between them is only £50,000 and therefore it is unlikely that there would be a significant benefit in obtaining a report. As the difference gets larger and the difference in ages becomes more significant the case for an expert's report becomes more compelling.

[7] [2014] EWHC 4054, [83].

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In many of the cases above, fair treatment of the pensions may literally be as simple as adding the CEs together and dividing by two. However, as the age difference starts to widen, the younger party would be disadvantaged to some degree by that approach, especially where the younger party nears retirement and becomes unable to make up any shortfall.

4.6 Cases requiring a needs-based approach

Whilst a capital approach by division of CEs may be appropriate in the cases discussed in section 4.5, there are certain paradigm needs-based cases where it is possible to suggest when one might prefer to approach the case in terms of sharing pension income or sharing pension capital. Bear in mind, however, that there are no automatic solutions in a discretionary system, and much will depend on the nature and extent of the assets available for division, aside from the pension:

Case 1

In the case of a short marriage with no children, it may be appropriate to make only a limited adjustment, perhaps by way of offsetting. But in some such cases, no pension-related adjustment may be necessary at all, by offsetting or otherwise – for example, if both parties worked throughout the marriage and have their own pension arrangements. See for example the case study in the Family Justice Council guide for litigants in person, *Sorting out finance on divorce*, involving Sally and Raj.[8]

Case 2

Following a short marriage with children whose presence has disrupted earning by one spouse, the primary emphasis will ordinarily be on ensuring that the needs of the primary carer and children are met, rather than attempting to equalise pension resources (either by reference to capital or income) as a matter of principle. The court will bear in mind both: (i) the primary earner's ability to rebuild pension and other capital resources following any division required by the financial orders, and (ii) the primary carer's ability to recover her position and so to establish/rebuild a pension by returning to / increasing hours of paid employment at the appropriate point (given the needs of the children).

Case 3

In the case of a short marriage (with or without children) where significant pre-marital pensions have been built up, much may depend on how close the parties are to retirement. Where the parties are close to retirement, the parties' needs may dictate that recourse must be had to the pre-marital pensions: remember, in a needs-based case it is not usual to ring-fence pre-acquired assets (pensions included) as non-matrimonial and so unavailable for distribution. However, where retirement is still several years away, the court must be alert to each party's ability to recover their position and make pension savings.

Case 4

In the case of a long marriage with children (whether or not they are dependent at the point of divorce), it may be appropriate to equalise pension income where one spouse gave up or reduced paid work for a long time, it is too late to recover her pension position and retirement

[8] https://www.judiciary.gov.uk/wp-content/uploads/2016/04/fjc-financial-needs-april-16-final.pdf

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is only a few years away. Please refer in this regard to paragraph 20 of The Valuation and Expert Issues Report.

The normal approach of the court will be to have regard to pension rights accrued to the date of hearing in terms of the valuation exercise, whilst also having regard (as s 25(2)(a) requires) to both parties' abilities to build/rebuild pension assets post-divorce. This is part of the discretionary distributive exercise. As stressed earlier, the objective is the search for a fair outcome: fairness will not always be met by simple equalisation of CEs.

Issues relating to the equalisation of income or capital from the perspective of the pension expert are dealt with at paragraphs 31 - 40 of the Valuation and Expert Issues Report**.** Additionally, specific valuation points in relation to DB schemes are to be found at paragraphs 21 and 23 of that report.

4.7 So when should a Pension on Divorce Expert (PODE) be instructed?

Family lawyers find it hard to agree about this. There are certainly many situations where enormous value is added by such reports, although this may often not be appreciated at the time by the divorcing couple or the professionals involved. Persuading the parties of the value of such a report can be challenging, especially where costs are escalating. There are a number of situations where such reports are <u>not</u> required, many of which are covered in 4.5 above. However, when dealing with defined benefit CEs in particular, often involving hundreds of thousands of pounds, or even millions of pounds in some cases, the financial cost of getting it wrong for either party can be immense. Even if it costs each party £1,000 to obtain the report (which to most people is still a lot of money), these numbers can fade into relative insignificance compared to the loss of potentially tens of thousands of pounds to either of the parties where an uneducated guess is made in order to mitigate costs.

In para 4.5 above, we considered situations in which an expert need not be instructed because:

- It may be sufficient to work only with the CEs,
- The CE is/are so small that the cost of an expert's report is disproportionate to the benefit of such a report, and
- The CE (small or large) is/are insignificant to the overall size of the matrimonial assets.

However, as always, there are a few traps that could affect even the guidance given in para 4.5, and so where an expert's report might still be proportionately of value and where information might only be revealed is when the right questions are asked of the pension company. They are where a case involves:

- Individual pensions, typically Retirement Annuity Contacts (or s.226 policies) where the policy included implicit guarantees, including guaranteed annuity rates and guaranteed pensions. No new S.226 policies were written after July 1988, but some very early personal pensions (typically those that commenced between 1988 and 1990) also had these guarantees. Where CEs are small the value of the guarantees are often relatively small too; but if the implicit guarantee adds a 30% increase in value to the CE it can quickly be deduced at what level the cost of an expert's report becomes justified. Normally, this information will only be revealed by asking the right questions of the pension company.

- Section 32 Buy-Out policies (also known by a variety of similar names) are individual pension plans designed to receive an occupational pension benefit and protect it in its original form. These plans can often include Guaranteed Minimum Pensions (GMP) for which the receiving scheme has taken on the liability to pay the GMP benefit, irrespective of the cost to them in

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doing so. The value of the GMP is rarely reflected in the value of the CE until the individual reaches their relevant pension age. CEs can, therefore, often significantly undervalue the true value of the GMP. Bear in mind also that it could be extremely damaging to the owner of the s.32 policy to transfer this type of arrangement under a PSO when other more suitable DC schemes could be transferred instead.

- Some older occupational pension schemes set up before April 2006 can have a significantly higher tax free cash entitlement than the standard 25% - even up to 100% in certain cases.

Other cases where it is much clearer that a Pension on Divorce Expert's report would be of benefit are:

- Where one or both parties has significant defined benefit scheme CEs, typically over £100,000. The CEs often significantly undervalue the true value of the pension benefits and this can only be revealed by a PODE's report.
- Where offsetting is being considered and either the pension CE being offset is significant or where defined benefit schemes are once again involved. Two separate defined benefit schemes could have identical pension benefits but completely different CEs (or very similar CEs but completely different pension benefits), one of which will clearly be better value than the other, but neither might be a fair reflection of a comparative value for offsetting purposes. Experts can assist with this.
- Large pension cases – particularly involving defined benefit schemes. Just because the CEs are large does not mean that a report becomes unnecessary, unless as mentioned above the pension assets are relatively insignificant to the value of the overall assets. The defined benefit CE is still likely to be a significant undervalue and the cost of guessing and getting it 'wrong' for one party becomes even more 'eye watering' as the numbers increase in size.

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5 The dominant practice: pension offsetting

5.1 What is offsetting?

Offsetting is by far the most frequently used approach to accommodate pensions in the overall settlement. It is the process by which the right to receive a present or future pension benefit is traded for present capital or "money now". In other words, offsetting allows one party to retain their pension rights, and in lieu, the other party has a disproportionate amount of non-pension assets, e.g. property or cash, achieved by a lump sum or property adjustment order. This is often viewed as an appealing outcome for primary carers who wish to retain the family home, and are prepared to give up some or all of a claim to the future benefit of the pension in order to secure it. Offsetting may also be the only feasible option, for example: where the cost of pension sharing would be excessive relative to the pension's value; where one party wishes to retain a pension because it is invested in commercial property or because that party is close to retirement; where the relevant pensions are overseas pensions or otherwise incapable of being shared.[9]

Offsetting is so popular partly because it is often seen as a quick, simple and/or cheap way of dealing with pensions in financial settlements. But appearances can be deceptive and offsetting can be a complex process. The results achieved by offsetting that has not been carefully considered can be potentially irrational or unfair, depending in part on the nature of the pensions involved.[10]

The critical issue is to identify an appropriate value for the pension(s) to be offset, in order to ensure that the offset is sufficient. The discussion of offsetting here provides a basic introduction to issues that are explored in far greater detail at paragraphs 43 – 71 of the Valuation and Expert Issues Report, in particular in relation to the proper approach to pension valuation for offsetting purposes.

5.2 Offsetting and the search for fairness – key points to note

Offsetting always creates issues in terms of how much one party should provide to the other in non-pension assets in lieu of the first party having greater pension assets.

As discussed at section 4 above, they are two differing currencies – one is capital, and one is largely, a future whole of life income stream. However, the pension freedom rules (see section 6 of this guidance) have blurred this for defined contribution schemes, and most defined benefit schemes (on the basis that, save for unfunded public service schemes, defined benefit pensions can be ported into a defined contribution pension after receipt of appropriate regulated advice). The extent to which non-pension capital should be discounted against pension capital is often a contentious area.

Some of the points to consider are:

- Offsetting can only be used if there are sufficient 'other assets' with which the pension asset(s) can be offset.

[9] Further examples are provided at paragraph 44 in the Valuation and Expert Issues Report].

[10] That irrationality and unfairness is analysed at Chapter 8 of the 2014 report "Pensions on Divorce: An empirical study" by Hilary Woodward with Mark Sefton of Cardiff Law School: https://orca.cf.ac.uk/56700/

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- However, offsetting sometimes is the only possible remedy if there is a desire for one party to remain in the former family home or if the pension cannot be shared (perhaps an overseas pension or an illiquid SSAS).
- It is possible to use a mixture of offsetting and pension sharing if the circumstances of particular cases dictate that this would lead to the fairest settlement.
- The value of the pension assets (and indeed all assets) is very important. The CE is a starting point. However, the CE provided is not always considered to be a fair value of the pension asset. If the case solely involves defined *contribution* funds, which have no guarantees, then the CE may be a good starting point for valuation for offsetting. However, in cases involving defined *benefit* schemes, relying on CEs can be highly dangerous as the case studies below demonstrate.
- The CE is the cost to the pension provider of providing a gross income to a member in retirement. Due to individual taxation, the value of this pension to an individual will differ.
- An individual contributing to a pension arrangement can benefit from tax relief on the contributions made. The party receiving a settlement by way of 'offset' will not be subject to tax on the amount received. Once a pension is in payment, the amounts received are treated as earned income and taxed as such at the individual's current tax rate.

These simple case studies demonstrate the need for particular care in ascertaining pension values for the purposes of offsetting (or other pension remedies):

Case 1: Why CEs are misleading - Defined benefit v Defined contributions

W aged 60 (just before retirement) has Public Sector (DB) pension CE **£300,000**

H aged 60 (just before retirement) has Scottish Widows (DC) pension CE **£300,000**

We have equality of CEs, therefore should there be no offsetting on basis we already have equality of pensions? ***<u>But beware</u>***:

- **W** will receive pension of **£12,800** pa, plus a lump sum of **£38,400**, plus a widower's pension of **£6,400 from her DB scheme.**
- **H** may be able to secure an index linked pension of **£7,800** pa with no lump sum, or pension of **£6,809** pa with a lump sum of **£38,400**

Is a pension a capital asset to be judged on CE (in which case no difference) or is it a future income stream (in which case substantial difference)?

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Case 2: Why CES are misleading – Defined benefit v Defined benefit

H aged 59, member of Defined Benefit scheme, CE **£750,000**

W aged 59, member of different Defined Benefit scheme, CE, **£500,000**

Both parties wish to retain their pensions. So offsetting is chosen remedy, with **W** to receive **£250,000** more of non-pension assets

But beware, because closer examination of schemes reveals:

- Both H and W will receive a pension of c. **£20,000** pa from age 65.
- So these pensions are almost identical – it is just that the CEs have been calculated differently by the two different schemes.

5.3 Valuation of a pension for offsetting purposes

This section aims to provide only a brief overview of a complex topic dealt with at greater technical length at paragraphs 43 – 71 of the Valuation and Expert Issues Report, which provides specific guidance for how the exercise may best be undertaken.

The valuation of a pension for offsetting purposes can be seen as a potentially three-stage process:

1. Arrive at a true and consistent valuation basis for each pension.

   For a defined contribution pension, this *may* be the CE, but one cannot simply assume that that will be the case. The E/V report provides detailed specific guidance on how that valuation should be arrived at.

2. Decide whether, and if so by what amount, it is necessary then to adjust that figure in light of the fact that, on receipt, the pension will be partly tax-free and otherwise taxed at the pension-holder's marginal rate.

   The justification for the tax adjustment is that the spouse who receives the non-pension capital will have an either/or option that will yield a tax advantage:

   - Either they will receive the lump sum by way of offset, and decide to re-invest this into a pension and obtain tax relief, and so potentially, having grossed up the contributions, achieve a pension fund in excess of that of the other party who has retained their pension.
   - Or they will retain their offset capital in a non-pension environment, and arrange their affairs so that the income generated is not all taxable income (e.g. an ISA investment), but some may comprise a return of the capital, the net effect being less tax is paid on the "income" than is paid by the pension member, where all of his pension income will be subject to tax.

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3. Decide what, if any, further adjustment should be made for "utility": i.e. in recognition of the perceived benefit of receiving liquid capital now rather than at some future point.

   Quantifying the utility adjustment is more problematic than the tax discount. Again, guidance on this issue as well as the appropriate approach to tax is provided in the paragraphs 65 – 68 of the Valuation and Expert Issues Report.

5.4 Offsetting: practice point for lawyers

The value of assets that are being offset against pension benefits are rarely if ever recorded in consent orders or supporting documents. As a matter of good practice, it would be beneficial for these aspects of an agreement to be recorded with a brief explanation of the nature of expert advice, if any, which has been taken in assessing the value of the assets to be offset against the pension. In this way, the parties, lawyers and judges will each have a better understanding of the basis on which a settlement involving offsetting is being considered.

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6 The impact of the new "pensions freedoms"

Key points in this section

- Greater flexibility and access to defined contribution pension schemes since April 2015
- Impact on the Money Purchase Annual Allowance could prevent significant pension rebuilding post-divorce
- Opportunities for 'reverse' pension sharing
- Importance of obtaining tax advice

6.1 Background

Changes to UK pension rules introduced by the Taxation of Pensions Act 2014 (the 2014 Act) provide for a much greater degree of flexibility in how private pensions can be accessed for individuals reaching the minimum pension age, currently age 55. These changes took effect on 6th April 2015. For many, the ability to access this additional flexibility has resulted in transfers to private pension schemes from former occupational pension schemes. These changes are frequently referred to as Pension Freedoms. This guidance does not seek to cover these changes in detail, rather to set out the key considerations in the family law context.

Prior to April 2015, individuals wishing to access their private defined contribution pension funds, other than in situations of ill-health and terminal illness, had limited choices. They could take their tax free lump sum, either in whole or in part, and with the remaining fund they could either (i) buy an annuity, (ii) draw down income from the remaining fund (known as Income Drawdown) or (iii) do a combination of these options. Hybrid options such as temporary annuities were also an option, where part of the drawdown fund was used to buy a short-term annuity, which gave a combination of a stable income along with a flexible element.

Deferred members of occupational pension schemes, be they defined benefit or defined contribution schemes, in the vast majority of cases had to transfer their scheme benefits to an individual pension arrangement to access these options. This continues to be the case, except that transfers from unfunded public sector pension schemes to private pensions which allow pension freedoms are no longer permitted, and appropriate independent advice has to be taken before a transfer from a defined benefit occupational pension scheme is allowed for transfer values over £30,000.[11]

6.2 New pension freedom options and family law implications

There are three key changes that have an impact in the family law context and merit further explanation. These key changes are the introduction of Flexi-Access Drawdown, the Uncrystallised Funds Pension Lump Sum and the new Money Purchase Annual Allowance.

Flexi-Access Drawdown is the new post 2015 terminology for Income Drawdown. Whereas previously the amount of income that could be taken from Income Drawdown was capped in a particular year, the amount of income that can be taken under the Flexi-Access rules is uncapped. This means that there is now no limit to the amount of income that can be taken from a private pension fund, so long as the pension provider offers the Flexi-Access option. If the option is not available, then the fund can

[11] See Pension Schemes Act 2015, chapter 2.

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be transferred to another provider that does provide this option. It is standard practice to take the tax free lump sum before taking any further funds as taxable income.

For those who commenced Income Drawdown prior to 6th April 2015, drawdown arrangements were re-named Capped Drawdown and the old rules continue to apply. But Flexi-Access Drawdown can be triggered at any time simply by taking £1 more than the maximum amount of the cap in any year. Some providers will change a Capped Drawdown plan to Flexi-Access Drawdown on request.

By way of an example under the new rules, an individual with a fund of £100,000 and an unrestricted tax free lump sum entitlement could take the maximum tax free lump sum of £25,000 and then draw down anything up to £75,000 as taxable income (no income is also an option). This can be paid as a series of income payments, lump sums, or a one-off amount as the individual chooses, but the income would be subject to income tax in the tax year it is taken and usually at their marginal rate of income tax. For this reason, sensible tax planning is advised.

If an individual over the age of 55 is required by the circumstances of the divorce to raise a lump sum from their pension fund for whatever reason, it is important that they and family law practitioners also understand the impact of the Money Purchase Annual Allowance and when it is triggered (see below), as well as the income tax implications.

Uncrystallised Funds Pension Lump Sum is the option that people would probably select if they had either a relatively small pension fund and they wanted to cash it all in at once, or if they wanted to encash a series of lump sums but did not want or require the flexibility or relative complexity of Flexi-Access Drawdown. 25% of the fund is non-taxable and the remaining 75% is taxable. The 2014 Act specifically makes it clear that the 25% of the lump sum that is non-taxable is not technically a tax free lump sum (or Pension Commencement Lump Sum as a tax free lump sum is technically known). This has potential implications for pension attachment orders where lump sum orders have previously been made against the tax free lump sum.

Money Purchase Annual Allowance (MPAA) is a mechanism devised to prevent people from drawing down on their pension funds under the new freedom rules and then reinvesting in the pension fund with the advantage of further tax relief. The MPAA is currently £4,000 which means that once it has been triggered, individuals who pay more than £4,000 p.a. into a defined contribution pension plan will usually be taxed at their marginal rate on the excess. This can have major implications for individuals wishing to rebuild their pension pots following a pension share on divorce and so it is important to understand what events trigger the MPAA, which are:

- Taking any income whatsoever under Flexi-access Drawdown (FAD)
- Taking an Uncrystallised Funds Pension Lump Sum
- Taking income from Capped Drawdown greater than the cap and triggering FAD

It is worth noting that an individual could take their entire tax free lump sum but so long as they take no income whatsoever from their Flexi-Access Drawdown, they do not trigger the Money Purchase Annual Allowance.

Impact on pension sharing

The pension freedom changes have little impact on pension sharing other than allowing the recipient of a pension sharing order greater flexibility in the way they access their pension fund. However, there can also be opportunities where perhaps one spouse has a pension fund that could be more useful in the context of divorce proceedings if it could be cashed in, but that individual is under the minimum pension age of 55. This might be, for example, to provide further liquidity for re-housing. If the other

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spouse is over the age of 55 then the pension could instead be transferred to them by way of a pension sharing order so that they can cash it in. This might be in addition to any pension share that is being transferred to the younger ex-spouse where the older spouse has greater pension assets/benefit entitlement on divorce. Any pension cashed in does, of course, come with potential income tax consequences. This is in effect a form of reverse pension sharing to allow defined contribution pension schemes to create further liquidity when the spouse with the large pension assets (and from whom there is likely to be a pension share) has defined benefit pensions that are not so readily accessible.

Impact on pension attachment

Pension attachment orders have not been widely used for many years, largely following the advent of pension sharing, but they do still have a place and many such orders have been made. It would have been impossible when these orders were made to foresee the changes that have recently been introduced and there is anecdotal evidence that some devious pension scheme members are trying to thwart the original intention of the order by using this new flexibility, especially the new options that did not exist until quite recently.

Individuals with pension attachment orders against their ex-spouse's pension would be advised to take immediate legal advice as to whether the attachment still provides for what was intended or whether an application should be made to the court to seek to vary the order, or indeed preserve the pension (by injunction or suitable undertaking) from being accessed in a way that was never intended.

It should also be noted that receipts of drawdown funds are reportedly being treated as periodic income by HMRC, resulting in inappropriate tax coding and significant overpayment of tax. This has the effect of netting-down the net value of receipts that are formally attached, and the recipient of an attachment order will not have any obvious legal basis for seeking their proportionate share in the tax which is subsequently reclaimed from HMRC.

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7 Age differential and "income gap" syndrome

Key points:

- There are occasions where a pension share against a pension in payment results in an immediate drop in income for the pension holder with no immediate benefit for the pension claimant.
- Solutions exist to avoid this, but they are not without risk for the pension claimant. Careful financial advice should be sought.

7.1 Causes of the problem

An "income gap" resulting from a pension sharing arrangement on divorce can arise for two reasons:

- There may be an age difference between the parties such that one former spouse can access a pension fund, whereas the other will not reach the minimum pension age for some time, potentially many more years.
- One former spouse may be entitled to receive their pension early following, for example, military or police service, but the other who was not a member of that pension scheme will not be able to access the pension credit until much later.

An individual with the benefit of a pension sharing order (referred to here as the pension claimant) cannot (under current rules) access the pension until age 55, or the minimum age required by the scheme. If that spouse, unable to access a pension fund immediately, is in reasonably paid work, these scenarios may not present a practical problem; indeed, that individual may have the ability to add to their pension funds in the intervening working years. But if the pension claimant has been out of the workplace for many years, they are unlikely to be able to support themselves through working and could be in difficulty without financial support to bridge the period before the pension becomes available to them. The problem is compounded if the age gap between the parties is such that the pension-holder is, by the time of the divorce or shortly afterwards, already entirely reliant on pension income: the effect of the pension share will reduce the pension holder's income, impairing their ability to pay significant spousal maintenance to the pension claimant before that spouse reaches the minimum age to access the pension. Additionally, even if the rules of the scheme permit the pension claimant to access the pension at 55, there is a considerable risk that the pension credit will be inadequate to meet the pension claimant's retirement income needs if income starts to be drawn from the pension fund at that age.

There are some creative ideas that improve the position and these are outlined below.

It should be emphasised to all judges, practitioners and experts that it is necessary to consider in <u>all</u> cases whether there is a potential income gap on divorce and, if there is, what steps can be taken to address or minimise the problem.

First, it is worth bearing in mind the following points:

- The CE of a defined benefit pension or an annuity *in payment* can be misleading in the divorce context as it rarely reflects the replacement cost of the pension being valued. Also, it is necessarily a snapshot in time: the figure then will have eroded by the time a pension sharing order is implemented. If pensions are in payment, it would be helpful for the pension report to include a timeline that sets out the change in the percentage of the pension sharing order

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required to achieve the appropriate income level for the pension claimant as the months march on.

- If the calculation basis of the CE for a defined benefit scheme is not provided, it would be helpful if the pension provider provided information that set out the basis of their calculations.

- Unless the parties worked for the same organisation (eg two police officers) or "shadow membership" of the original pension scheme (i.e. internal membership of a pension scheme as a pension credit member) is available for the pension claimant, the recipient of a pension sharing order from a defined benefit scheme has to transfer the pension credit to a personal pension or similar. This is a very different financial instrument and carries benefits that are necessarily less certain than the originating pension scheme, although greater flexibility is available when it comes to taking pension benefits.

- If the claimant spouse can become a pension credit member of the pension holder's defined benefit scheme, details of the basis on which this is offered should be clear from the outset, as the benefits provided are not necessarily the same as those available to the primary member.

- Where one party has retired but there are still dependent children of the family, considerable care needs to be taken to ensure there are enough income resources available to cover the needs of those dependent children.

- Care needs to be taken in respect of tax considerations. Payments from a pension may be subject to income tax, and when pension benefits are taken they are usually tested against the lifetime allowance. The lifetime allowance could affect a large pension share (eg one of, say, £500,000 received at the age of 40) if the recipient is relatively young and the spouse who originally had the pension benefits had not taken benefits prior to the pension share. She should take advice about the possibility of lifetime allowance protection. Where pension benefits have already been tested against the lifetime allowance and are then transferred by way of a pension sharing order, the transferred funds can be protected from any further lifetime allowance test by applying for protection from HMRC. Tax considerations also change over time: the ability to make further pension contributions could be affected by changes to pension tax relief, the annual allowance, the lifetime allowance or a combination of all of these.

7.2 Possible mitigation of the problem

There are five ways that might be available to help mitigate the problem:

1. Where the original pension-holder is still of employable age, it might be practicable for them to return to work to supplement the pension income that will be reduced by the pension share. Where this is no longer possible, the pension claimant might be able to help support the pension holder while they are still of working age. Where neither party is likely to work again, then it is important to explore ways in which surplus capital can improve pension income (see below).

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2. The application for a pension sharing order could be adjourned so that the (older) pension holder continues to pay maintenance to the pension claimant using income from all sources, including pension income (not yet reduced by pension sharing), until such time as the pension claimant is able to access pension benefits. It may also enable the pension holder to access a tax free lump sum, undiminished by a pension sharing order, to the potential benefit of both parties. At the point where the pension claimant can access pension benefits, a pension sharing order could be made. This deferral would lead to the reduction in the fund in a defined contribution scheme/personal pension (and a reduction in the eventual CE of a defined benefits scheme). But it would avoid reducing the pension holder's income by reason of a pension share that, thanks to the income gap, yields no contemporaneous benefit to the (younger) pension claimant.

   However, this option carries risks, and should be assessed very carefully with the help of good financial advice.

   - The pension holder might die before a pension sharing order could be made. If the remainder of the financial order had been approved and the decree absolute pronounced, then (depending on the specific rules of the scheme) any death benefits under the pension scheme may not be available to the pension claimant. Some form of life cover would therefore be needed to protect the pension claimant from the potential loss on the death of their former spouse (although this assumes suitable life cover is available at an affordable cost; there are also circumstances, such as suicide, where some life policies do not pay out). It would additionally be possible to obtain a pension attachment order against a death in service lump sum if that is available.
   - There would be complications if the pension holder remarried and then either died or divorced a second time. A pension attachment order against the same pension scheme in favour of a subsequent spouse would prevent the proposed order being made, and a pension sharing order against the same scheme in favour of a subsequent spouse would reduce the fund available for sharing for the original pension claimant.
   - If the pension being shared is a defined benefit scheme that permits shadow membership, the pension claimant's internal pension credit factor is more generous in terms of the eventual pension income they will receive if it is crystallised by virtue of the pension sharing order at a date *before* they reach pension age. While this could be addressed by taking an external pension share if the preference is to adjourn the pension sharing application, an external share would mean the pension claimant would lose out on the security of membership of a defined benefit pension scheme.
   - While the intention to make a pension share in future could be recorded in the financial order, if the financial circumstances of either party materially changed, there is no certainty that a court would approve a pension sharing order in the future; the pension claimant should therefore be cautious about relying on this alone.
   - In any event, the pension sharing order will have to take effect at a date some distance from the original order, and so will have to be approved by the court separately from that order. The CE values will have changed by that time, and so there will be a need for further negotiation and consideration of the appropriate level of the order. The parties would be prudent to agree the principles on which they would carry out that further negotiation as part and parcel of any agreement for an adjournment of the pension sharing application. It is also possible that pension sharing could be abolished, or replaced by another, less helpful, regime in the intervening period.

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3. As well as pensions, re-housing will usually be an important consideration. Where there are insufficient funds to re-house both parties adequately, it might be appropriate – if the older spouse is over the minimum pension age – to transfer the pension fund(s) of the younger spouse to the older spouse by way of a pension sharing order so that some capital could be accessed immediately (either by way of draw-down from a defined contribution scheme or a tax-free lump sum). This is a convenient way of accessing pension funds that would otherwise have been out of reach until the younger spouse reached the minimum pension age, even though the older spouse may own the majority of the pension assets. Although this may come with tax consequences for any non-tax free lump sum taken, if the release of capital enables the parties to re-house without the need for additional borrowing, their monthly outgoings are to that extent reduced. Careful financial advice would be needed.

4. In some circumstances, examples of which are given below, there might be surplus income or capital available to supplement further pension provision. The first three examples below highlight the potential importance of state pensions:

   a. Check the state pension position (see section below in this guidance). State pension entitlement is an important bedrock of pension provision and can be increased by buying missing years of National Insurance contribution credits (using other assets, if available) or by contributing towards future years, either on a voluntary basis or through employed or self-employed NI contributions. Advice should be taken from the Pensions Service on making up missing years, as this has become much more complicated following the introduction of the New State Pension in April 2016.
   b. NI credits are paid to individuals who are not in paid employment but who are in receipt of child benefit in respect of children up to the age of 12. Non-working spouses in higher income tax rate households should therefore claim child benefit in order to obtain these NI credits, but choose not to claim any payment. It is important, if child benefit has not been claimed thus far in such a marriage, that the spouse concerned starts claiming it as soon as possible in order to secure the NI credits going forward. A full NI contribution statement clarifies this point, as well as the one in (a) above, so that the pension claimant's own state pension entitlement is clear.
   c. Where the earning spouse rather than the non-earning spouse claimed child benefit, any missing NI credits in respect of those years where child benefit was payable can be re-allocated to the non-earning spouse for those years where the earning spouse qualified for credits through their own NI contributions. This ensures the state pension entitlement of both spouses is maximised.
   d. If the (younger) pension claimant is a member of a defined benefit scheme, find out if the scheme permits the purchase of "added years", and if so what that would cost. That payment could also come from other assets, if available.
   e. If the (younger) pension claimant is working, spousal maintenance for a fixed term might enable them to increase contributions to a pension scheme and possibly secure higher, matched employer contributions as a result. This may have to be backed up by a life assurance policy for that fixed term period (or, if unaffordable, provision under a will) that would ensure that the plan is not derailed by the premature death of the older party.

5. With the agreement of both spouses and in certain circumstances, deferring either the divorce or the decree absolute itself might enable some financial planning, during which time the (younger) pension claimant might in the meantime continue to be entitled to a spousal

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pension by way of security in the event of the death of the other spouse. This degree of financial planning will usually require a high level of co-operation and trust between the parties.

6. It is not, however, possible to mitigate the problem by attempting to make a deferred pension sharing order or deferring serving the order on the pension provider.

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8 Procedure and essential action points: an overview

This summary provides an overview of the essential stages in a typical case. Part 9 of this document provides more detailed procedural guidance on applications to court for pensions orders, by consent and otherwise. Other sections of this guidance deal in more detail with questions around implementation and enforcement, and many of the "elephant traps" associated with particular types of pension or pension contexts.

A: Gathering information/ disclosure: take comprehensive instructions at the outset re pensions available and client's understanding of them

➔ **Use Form P to gather information re non-state pension entitlements**: Court can direct at FDA, but better to complete Form P at an early stage.

- Ask client to sign Form P in respect of each of the client's pensions and complete state pension statement request in **Form BR19** (as well as **Form BR20**, currently) and send off after first meeting or at start of instruction to proceed
- Request that the other party complete Form P in respect of each of their pensions

Remember, Form P provides:

- the information required by the Pensions on Divorce etc. (Provision of Information) Regulations 2000, reg. 4
- information re pension sharing charges

➔ **Don't overlook state pension entitlements**: (see Part 10 below)

- Complete and send off to DWP Forms **BR19** re state pension income **and BR20** NSP re: CE Valuation of Additional State Pension or Protected Payments
- Request that the other party do the same

➔ **If contested proceedings have been initiated:** serve a copy of the application on the pension trustees (as the person responsible for the pension arrangement)

B: Instructing a Pension on Divorce Expert (PODE): see Para 4.7 for discussion of particular cases in which this may be necessary.

➔ **Evaluate at early stage whether a PODE should be instructed** to provide a pension report, jointly or unilaterally. In some cases, it might be desirable to appoint a shadow expert (i.e. expert appointed by the party to provide pensions advice – cf any SJE appointed by the court)

➔ **Ensure compliance with FPR Part 25** (see Resolution Guidance Note on Instructing Experts for additional guidance)

➔ **Letter of instruction** – use template letter of instruction provided in Appendix 1 to this Report; seek shadow expert advice if unsure what to ask: asking unnecessary questions can incur unnecessary costs.

C: Advising the client and proceeding to negotiation

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- ➔ **Basic issues to consider** in deciding how to approach the pensions issues in the case: type of pension, benefits and risk, retirement age, any benefits lost on sharing, charges
- ➔ **Advise the client on issues such as**: moving target syndrome (i.e. the problem that implementation will operate against a different CE from that used in negotiations or by the court, simply because of values changing over time); clawback in the case of sharing pensions in payment (see 14.5); income gap (see Part 7)
- ➔ Where the client might be receiving a pension share, you need to **consider the destination fund** – where is the pension credit going to go? This is essential for prompt implementation of the order. Is advice from an IFA required on this issue?

D: Reaching agreement (hopefully) and obtaining a pension order by consent:

- ➔ **Take care with the pension annex:**
  - ensure annex completed properly (take care with scheme name and destination fund – see above)
  - any pension sharing order must provide for sharing of a percentage of the pension, not a fixed amount. Avoid any ambiguity to ensure trouble-free implementation: e.g. wording such as "50% of benefits less AVCs" would give rise to difficulties of implementation
- ➔ **Ensure the D81 is completed correctly** and the boxes dealing with pensions are accurate – remember, the Regulation 4 information is required for pension sharing orders.
- ➔ **Where pensions are being offset, set out clearly the basis for that offset in the court papers:** this is not a legal requirement, but as a matter of good practice, it enables the parties, lawyers and judge better to understand the basis of a settlement involving offsetting if a schedule to D81 records this matter, with a brief explanation of the nature of expert advice, if any, that has been taken in assessing the value of the assets to be offset against the pension.
- ➔ **Seeking pension trustees' approval ahead of submitting the paperwork to court:** Note the difference here depending on the type of order:
  - **Pension sharing:** whilst not a requirement of the rules, it is best practice for the pension trustees to approve the terms of the order and the annex before they are submitted to court
  - **Pension attachment:** the rules here require trustee approval of the order.
- ➔ **Don't forget about the charges for any pension sharing:** who is going to pay?

E: Thinking through the timing of decree absolute, and implementation issues (see Part 14)

- ➔ **Timing the decree absolute application**: if a pension sharing order has been made, consider carefully with the client whether to delay applying for DA until 28 days <u>after</u> the pension order has been made. If the DA application is made earlier, the client may lose out in pension terms (if their spouse dies before the pension sharing order can take effect – always 28 days from its being made). But other considerations (e.g. early enforcement of a lump sum order) may favour an earlier application for DA (see 14.3).

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- ➔ **Ensure prompt implementation:** The implementation period does not start until
  - the order and the DA have been provided: Has the court served them, as required by the Practice Direction? Given delays in court, consider whether, in order to achieve certainty, it would be better for the solicitor of the pension-claimant to serve them.
  - the charges have been paid, and
  - destination fund details have been provided
- ➔ **When can I close the file?** Do not close the file until you are certain that the order has been implemented or the client has given clear instructions to retain responsibility for implementation

Remember: there are a lot of "elephant traps" in pensions practice into which you and your client might fall if you do not investigate the pensions issues carefully and take appropriate expert advice. Many of them are explored in this guidance. Here, in brief, are just a few:

- **The impact of pension freedoms** on personal pensions: can the pension-holder withdraw the whole pension to frustrate pension sharing. Possible safeguard: get an undertaking, or provide back-up lump sum?
- **Final salary schemes**: can the pension be transferred out to a personal pension and then taken in cash? Possible safeguard: seek an undertaking/injunction?
- **Value of public sector pensions:** CEs are often not representative of the actual value and scheme may have different tiers of membership. Safeguard: seek advice from a PODE.
- **Closed defined benefit schemes with new defined contribution schemes**. Safeguard: check how the scheme expects pension sharing annexes to be drafted - one or two? It could make a huge difference to the outcome of implementation!

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9 Procedure: the contrast between contested and uncontested cases

The Family Court Practice ("The Red Book", edition for the current year) provides detailed and helpful notes explaining the procedural differences between contested and uncontested cases for both pension sharing order and pension attachment orders, depending on whether Form A has been issued. The following summary provides an outline of that procedural framework for each type of order in turn.

9.1 Pension sharing applications

Where Form A has been issued

1. The application is made in the application for a matrimonial and civil partnership order (petition) or at any time thereafter.[12]
2. The person with pension benefits must apply for a CE within 7 days of notice of the First Appointment, unless there is already one in existence dated not earlier than 12 months before the date of the First Appointment (a 'relevant valuation'[13]).
3. The pension provider must be served with a copy of the application in Form A and given 21 days to provide information including details of any obstacles to a pension sharing order being made.[14]
4. The form of the order must:
    a. be expressed as a percentage of the CE,[15] calculated in accordance with the Pensions on Divorce etc. (Provision of Information) Regulations 2000, reg 3;
    b. state in the body of the order that there is to be provision by way of pension sharing in accordance with the annex(es) (Form P1 (pension sharing annex)) for each pension arrangement.[16] The order must not take effect until 7 days after the time has expired for appealing or the date of decree absolute (whichever is the later);[17] and
    c. direct whether the court or other party is to send the pension sharing order, annex(es) and the relevant decree/order to the pension provider.[18]
5. The final stage is implementation. The court or one of the parties serves the order.[19] The information needed from the parties for implementation to take place is set out in the Pension on Divorce etc. (Provision of Information) regulation 2000, reg 5 et seq.

Consent applications where no Form A has been issued

A special procedural framework for dealing with consent-based pension sharing applications, where there has been no prior service of a formal application (Form A),[20] is provided for by FPR 2010, r 9.32. This procedure will apply where, for example, the parties have been in negotiations and have reached an agreement without any formal application having been made. Unless the information set out in Section C of the Pension Inquiry Form (Form P) has already been provided for the pension arrangement in question, that information must be requested and, on receipt, a copy must sent to the

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[12] FPR 2010, r 9.4.
[13] FPR 2010, rr 9.3(1) and 9.30.
[14] FPR 2010, r 9.31 and Pensions on Divorce etc. (Provision of Information) Regulations 2000, regs 2(7) and 4.
[15] MCA 1973, s 21A; *H v H (Financial Relief: Pensions)* [2010] 2 FLR 173, FD.
[16] FPR 2010, r 9.35.
[17] MCA 1973, ss 24B(2) and 24(C).
[18] FPR 2010, r 9.36.
[19] FPR 2010, r 9.36.
[20] Under FPR 2010, r 9.31.

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other party. It is good practice in all cases involving a pension to serve Form P on each pension provider.

There is no formal requirement to seek the approval of the pension provider to a consent pension sharing order, whether an application has been served under r 9.31 (as will be the case where the case was originally contested) or is made under r 9.32. However, it is good practice to seek such approval to ensure that there are no difficulties in implementation once the order has been made.

As a general point relating to pension sharing orders (whether or not made on a contested application): pension sharing and pension compensation sharing orders are the only type of financial remedy order for which an application can be made even after the pension claimant has remarried.[21]

9.2 Pension attachment applications

Where Form A has been issued

1. The application is made in the application for a matrimonial or civil partnership order (petition) or at any time thereafter.[22]
2. The person with pension benefits must apply for a CE within 7 days of notice of the First Appointment, unless there is already one in existence dated not earlier than 12 months before the date of the First Appointment (a 'relevant valuation').[23]
3. The pension provider must be served with the application and the addresses referred to in FPR 2010, r. 9.33(1). The pension provider may then within 21 days of service request from the pension holder the provision of the pension section of Form E, which must be provided on exchange of Forms E or within 21 days of the date of the request (whichever is the later).[24]
4. Having received a copy of the requested section of Form E, the pension provider may send to the court and to the parties a statement in answer within 21 days of receiving that material.[25]
5. Where the pension provider files a statement in answer, the pension provider is entitled to be given notice of the First Appointment and to be represented at that appointment.[26]
6. The form of the order must:
    a. be expressed as a percentage[27] of the payment which becomes due to the pension holder;
    b. state in the body of the order that there is to be provision by way of pension attachment in accordance with an annex(es) (Form P2 (pension attachment annex)) for each arrangement;[28] and
    c. within 21 days of service, direct whether the court or one of the parties is to send the pension attachment order, annex(es) and accompany documents to the pension arrangement.[29]
7. The court or one of the parties serves the order.[30]

[21] See MCA 1973, s 28(3) and s 21 (definitions of "financial provision" and "property adjustment" orders).
[22] FPR 2010, r 9.4.
[23] FPR 2010, rr 9.3(1) and 9.30.
[24] FPR 2010, r 9.33(2)-(4).
[25] FPR 2010, r 9.33(5).
[26] FPR 2010, r 9.33(6).
[27] MCA 1973, s 25B(5).
[28] FPR 2010, r 9.35.
[29] FPR 2010, r 9.36.
[30] FPR 2010, r 9.36.

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Consent applications where no Form A has been issued

A special procedural framework is created for applications for consent-based pension attachment orders where an application has not been already served under FPR 2010, r 9.33(1) (as will be the case where the case was originally contested). In these circumstances, the parties must serve on the pension provider a copy of the application for a consent order, a draft of the proposed order and pension attachment annex and particulars of the addresses referred to in r 9.33(1). The pension provider then has 21 days from the date of service of the consent order application in which to object.[31]

9.3 Key "best practice" recommendations:

- Before an application for either a pension sharing order or a pension attachment order is made, whether or not by consent, it is best practice (wherever possible) to secure the approval of the pension provider both to the wording of the order and the annex.
- Likewise, before agreeing the wording of either a pension sharing or attachment order and an annex, in most cases, it will be prudent to take financial as well as legal advice. Financial advice will often be required by the pension claimant, and it is wise to consider where the pension share is to be invested before committing to the terms of a particular order and annex.
- It is vital that any pension sharing or attachment order is implemented. Solicitors should be vigilant to ensure that implementation is effected promptly whether acting for the pension holder or the pension claimant. The pension holder may well be concerned to ensure timely implementation not least because the value of the pension may be growing. The pension claimant should be eager to ensure that his or her share of the pension is invested as he or she would wish it to be as soon as possible after the order has been made. See further, the section on post-order implementation issues, below.
- Don't overlook the state pension.
- Agree who is to pay pension sharing charges.

[31] FPR 2010, r 9.34(3).

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10 State pensions on divorce

State Pensions can often be one of the most valuable assets in a divorce and should not be overlooked. Estimates of pension entitlement can be obtained by completing Form BR19. Valuations of shareable rights on divorce can be obtained by completing Form BR20. Completing both forms is the most reliable way of obtaining a full picture of an individual's state pension entitlement.

This section covers the following topics:

- Old State Pension
  - Basic State Pension substitution
  - Additional State Pension sharing
  - Graduated Retirement Benefit
- New State Pension
  - Temporary measures for pre 6.4.16 divorce petitions
  - Sharing of Protected Payment

Key points/recommendations:

- Both parties to complete Form BR19 and Form BR20
- State Pension information to be obtained and considered in all cases
- Individuals in the Old State Pension can still substitute Basic State Pension and share Additional State Pension
- Individuals in the New State Pension can no longer substitute Basic State Pension but can share Additional State Pension in two specific circumstances

10.1 Introduction

The UK's state retirement pension can be broken down into two discrete systems, the New State Pension and the Old State Pension. Individuals who reached their state retirement age prior to the 6th April 2016 are in the Old State Pension and those who reach their state pension age on or after that date are in the New State Pension.

For those individuals who have a National Insurance (NI) contribution history before 6th April 2016 but had not yet reached state retirement age by that date, the New State Pension is calculated on a transitional rate, either through work-related contributions, through various forms of credits, or by paying Voluntary NI contributions. The starting weekly rate in the New State Pension was determined on the 6 April 2016 by calculating the higher of an individual's entitlement under the Old State Pension with their entitlement using the calculation basis for the New State Pension. This was a one- off exercise and individuals with a starting amount lower than the maximum rate of New State Pension can accrue additional credits up to the maximum rate of New State Pension through any of the above means up until the tax year before the tax year in which they reach State Pension Age. Those with a New State Pension starting amount on 6 April 2016 higher than the maximum rate of New State Pension are unable to increase their weekly rate further, irrespective of whether they continue to pay NI contributions.

10.2 Old State Pension

The Old State Pension comprises the Basic State Pension, Additional State Pension and Graduated Retirement Benefit.

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Basic State Pension

Entitlement to Basic State Pension is obtained through one's own NI contribution history, known as a Category A pension, or on a reduced rate basis using the NI contribution history of a spouse, known as a Category B pension. The Basic State Pension cannot be split or shared on divorce. However, individuals in the **Old** State Pension can substitute their ex-spouse's NI contribution history for their own where their ex-spouse has a higher Basic State Pension entitlement. This is known as "substitution" and it increases those individuals' own Basic State pension up to an amount broadly equivalent to the amount of Basic State Pension being received by their ex-spouse with the higher pension, without reducing the latter's entitlement.

To claim substitution, the claimant (i.e. the person with the lower Basic State Pension) would need to send either an original or certified copy of the decree absolute to the Pensions Service, providing their and their ex-spouse's NI number. Where the claimant reaches state pension age before 6th April 2016 but their ex-spouse reaches state pension age on or after 6th April 2016, only the ex-spouse's NI contribution history up to 6th April 2016 can be substituted. This is because no further Basic State Pension was accrued after 6th April 2016 as it is not a feature of the New State Pension.

Should an individual who is considering claiming substitution remarry before doing so then the right to substitute will be lost. By contrast, re-marriage following substitution does not result in a reduction to their pension. For this reason, there could be a significant financial advantage in delaying a planned re-marriage until after a substitution claim has been dealt with.

Additional State Pension

An Additional State Pension can be shared in the same way as occupational and private pensions.[32] Additional State Pension is the composite term for the earnings-related component of the state pension built up under the State Earnings Related Pension Scheme (SERPS) from 1978 and then from 2002 until 2016 under the State Second Pension. Some individuals can have significant amounts of Additional State Pension, particularly those who were relatively high earners and who never contracted out of the Additional State Pension through an employer's pension scheme or their own private pension. The Additional State Pension can be one of the largest assets in a divorce, sometimes worth in excess of £100,000.

An individual can obtain a valuation of their Additional State Pension from the Pensions Service by completing a Form BR20. Paper and on-line versions are available. The weekly amount of Additional State Pension can be found on the state pension statement that the Pensions Service sends each year to those in receipt of their state pensions. Individuals who have deferred taking their state pension will need to contact the Pensions Service for written confirmation of their weekly amount, including the addition for deferral.

For there to be a right to a pension share, only the person whose Additional State Pension is to be shared must have reached State Pension age prior to 6th April 2016, even where an application has been made by that person to defer taking their State Pension. The issue date of the petition is irrelevant for a pension share to be made against the Additional State Pension, unlike the rules for those now in the New State Pension (see below).

[32] This will apply only where the divorce petition was issued on or after 1 December 2000. While this restriction will not affect the vast majority of cases, it would affect some *Wyatt v Vince*-style late applications and some variation applications.

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Graduated Retirement Benefit

Graduated Retirement Benefit can form part of the Old State Pension for those who accrued state pension credits before 1975, although it tends to be a relatively modest amount of money. On average, it is approximately £1.40 per week for women and approximately £5.50 per week for men. It has never been possible to share Graduated Retirement Benefit, either through pension sharing or substitution.

10.3 New State Pension

The New State Pension commenced on the 6th April 2016. In principle, it cannot be shared. There are, however, two limited circumstances where divorcing individuals can receive a pension share against their ex-spouse's **Additional** State Pension where their former spouse is in the New State Pension.[33]

Individuals who reached their state pension age on or after 6th April 2016 and are therefore in the **New** State Pension are unable to increase their pension by substituting their former spouse's NI contribution history for their own. This is because the Basic State Pension does not form part of the New State Pension.

Sharing Additional State Pension for petitions pre-6 April 2016

The first instance is where the petition for divorce was issued before the 6th April 2016, in which case the entire Additional State Pension, if any, can potentially be shared. Once again CEs can be obtained from the Pensions Service using a Form BR20, but the Service would need to be advised of the petition issue date if a valuation is required of the full Additional State Pension in this scenario. The pension claimant would receive a percentage pension share based on the CE of their former spouse's Additional State Pension, and the Pensions Service then calculates at the point of implementation the additional amount of weekly pension to be added to the pension claimant's own state pension entitlement. For those individuals who have deferred taking their state pensions, any pension sharing amount that they are awarded is added to their basic entitlement before the addition of their deferral amount.

Sharing of Protected Payment

The second circumstance in which Additional State Pension can be shared in New State Pension cases is where an individual who reached state pension age on or after 6th April 2016 had such a large Additional State Pension that their total weekly amount of New State Pension exceeds the full amount of New State Pension (£159.55 per week in 2017/18). On the 6th April 2016 a calculation was run to determine the starting amount in the New State Pension for those individuals who reached State Pension Age on or after that date. This compared their entitlement under the old system with their entitlement based on the new calculation basis for the New State Pension. Where an individual's New State Pension weekly starting amount is higher than the full amount of the New State Pension, the difference is known as the 'Protected Payment'. So, for example, somebody with a New State Pension amount of £170 per week in 2017/18 would have a Protected Payment of £10.45.

Unless the divorce petition was issued before 6th April 2016, only the Protected Payment element of a New State Pension can be shared. Individuals can obtain valuations of their Protected Payment amount from the Pensions Service using the Form BR20. The calculation for sharing the Protected Payment has been much simplified compared to the sharing basis under the Old State Pension. The pension share is now based on a percentage of the pension holder's weekly amount of Protected Payment. For example, a 50% pension sharing order against £20 per week of Protected Payment would

[33] Note that there can be no sharing against a New State Pension where there are no pre-April 2016 Additional State Pension credits, i.e. in the case of very young spouses.

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leave the pension holder with £10 per week in addition to their full amount of New State Pension. The pension claimant would receive an additional £10 per week to their own State Pension. To give effect to that example, the figure 50% would be inserted into the relevant box on the pension sharing order Annex as the percentage value of the shared weekly amount.

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11 Complexities inherent in certain public sector occupation schemes

11.1 Introduction

Public sector pension schemes have always contained traps for the unwary divorce practitioner. Most of the public sector employers had more than one section or Scheme prior to 2015. The introduction of all the new Schemes in 2015 has added to the complications and potential pitfalls.

It is important for the practitioner to understand what benefits and scheme or section they are dealing with. It is very dangerous to assume that because a certain solution worked for a previous client; the same will be available for the next case.

Issues that the practitioner should be wary of, outlined in what follows, include:

- Introduction of the new 2015 (Career Average / CARE) schemes and transitional arrangements (sometimes referred to as tapering) for members moving to these schemes
- Issues about whether benefits that an individual has accrued with the same employer (or employers who are all part of the same public sector) can be shared in different proportions
- Variable retirement ages that are dependent on service and can be impacted by the 2015 schemes
- Members in service past the age at which they can retire
- Overnight increase to the Cash Equivalent
- Absence of a late retirement factor in the older schemes
- "Income gap" issues where the pension credit member receives benefits at a later age than the member
- Early Departure Payments in the Armed Forces Pension Scheme
- Re-Settlement Commutation in the Armed Forces Pension Scheme
- Consumer Price Index being unmatchable on the open market
- The effect of Pension Sharing where there is a pensionable salary cap
- Re-employment after retirement

11.2 New Career Average (CARE) schemes and transitional arrangements ("tapering")

New schemes based on Career Average (CARE) have recently been introduced. The Local Government Pension Scheme introduced its new Scheme in 2014, and the other Schemes introduced their new Schemes on 1 April 2015. These schemes have retirement ages later than the Schemes they replaced.

Each Scheme has its own rules about when members have to move into the new schemes for future accrual. Younger members and new members will be in the new scheme from April 2015 (April 2014 for Local Government Pension Scheme). However, different schemes have different rules for older members about how long they can remain in the scheme they were already in and when they have to move to the new scheme. These are variously called "tapering" or "transitional" arrangements or rules.

Benefits will be retained in the original schemes (in the Armed Forces Pension Scheme, known as "legacy schemes") and in most cases will retain the link to the member's pensionable salary for as long as they remain in service. The member will then usually have rights in two separate schemes.

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11.3 Whether different sections within schemes can be shared in different proportions

Each of the schemes has rules about whether the different sets of benefits have to be shared in the same proportion and the practitioner should check carefully when considering an order whether what is proposed is acceptable and feasible. For example, the NHS Pension Scheme requires that the 1995 and 2008 section rights are shared in the same percentage but the 2015 section rights can be shared in a different percentage. The Armed Forces Pension Scheme allows all three sections to be shared in different percentages but if you have two sets of independent rights in the same section, they have to be shared in the same proportion.

11.4 Variable retirement ages dependent on service and the impact of 2015 schemes

There have always been issues with public sector schemes where there is a retirement age for deferred pensions for those who leave after only a small amount of service, but an earlier retirement age is available as long as you have achieved a certain level of service. For example, in the Police Pension Scheme 1987 Section, those leaving with under 25 years' service had a retirement age of 60 but this could reduce to age 48 if the member has achieved 30 years' service. Police, Firefighters and Armed Forces are well known examples, but there are also the Special Classes in the NHS Pension Scheme, Prison Officers (Civil Service Pension Scheme) who joined before a certain date, and in the Local Government Pension Scheme there was a "Rule of 85" that meant if the age at retirement + number of years' service was 85, the member could take benefits without reduction immediately or at age 60 if later. Practitioners should consider obtaining a specialist report in any such cases.

The issue arising in these cases is that if, following a specified period of service, the age at which the member can retire without suffering a reduction in benefits reduces below the Scheme's Normal Retirement Age, then a CE calculated *before* that period of service has expired will be an undervalue. For example: consider the policeman who after 24 years' service is entitled to retire at 60 if he were to leave service – the CE will be based on the accrued income being taken at age 60. However, if the officer accrues one further year's service (to 25 years), the age at which the benefit is payable becomes age 50 and the CE is much higher. (After 30 years' service the pension may be payable at age 48). The same benefit payable for an extra 10 or 12 years has a much greater value and this effect is also reflected in the Pension Sharing calculations that would be made in such a case.

Practitioners should therefore be alert to whether one or other spouse is an active member of such a scheme, and consider obtaining additional evidence of the true value of the benefits available to the active member.

The situation has been made more difficult as a result of the introduction of the 2015 schemes. Policemen with benefits in both schemes (the first being the 1987 scheme) find that although they can retire on an unreduced pension after 30 years' service in respect of their rights in the 1987 scheme (even if some of those 30 years accrued in the 2015 scheme), the benefits that they stand to acquire under the 2015 scheme will be reduced if they retire before the later retirement age in that scheme.

The making of a pension sharing order against such a background makes matters even more complicated. Potentially, the value of the benefits in the 1987 scheme will actually reduce as the officer works past the 30 years' point because of the way that pension debits are treated and adjusted according to the age that the benefits are taken. However, the benefits in the 2015 Scheme will be reduced if the member retires and takes benefits before the Normal Retirement Age for the 2015 Scheme and that reduction will reduce the longer the member serves and the older they get. In addition, the member will accrue further benefits if they remain in service.

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Previous assumptions about the optimum retirement age for such individuals are no longer valid, and it is much more difficult to know when they will retire. Practitioners will often have to consider this on a case by case basis.

11.5 Members in service past the age at which they can retire

This is an issue in a number of cases, but in particular in the Armed Forces Pension Scheme. For example: Officers can retire at age 37 with 16 years' service. Under the Pensions on Divorce etc. (Provision of Information) Regulations 2000, the CE has to be calculated on the assumption that an active member leaves service on the date of calculation, i.e. immediate retirement. It therefore assumes the pension comes into payment immediately and puts too high a value on the pension as it assumes the pension starts to be paid immediately, whereas in practice it will not start to be paid until the pension holder leaves the scheme and therefore will be paid for a shorter period.

As a result, a 50% pension sharing order can wipe out almost the whole of the accrued pension to the date of the divorce if the member remains in service until, say, age 60. This happens because the CE at the time the pension is shared has to be calculated assuming the member leaves service at the time (and therefore where the member can take benefits immediately, it assumes they do) and this creates a debit for the member to repay of a proportion of that CE. The debit can only start to be repaid when the member does actually leave service, so the repayments have to be made over a shorter period and therefore have to be higher than if they were repaid from the date of the calculation.

This is a feature of the Armed Forces Pension Scheme, Police Pension Scheme and Firefighters' Pension Scheme but not all public sector schemes. For example, Special Classes in the NHS Pension Scheme and members of the 1995 NHS Pension Scheme who work beyond the Normal Retirement Age of 60 do not suffer these losses.

Practitioners should take particular care for members who are still in service after the date that they can take benefits.

11.6 "Overnight" increase in the Cash Equivalent

The Regulations also mean that a CE can increase dramatically overnight. An officer in the Armed Forces Pension Scheme 1975 on the day before achieving 16 years' service will have his accrued benefits calculated based on them being paid from age 60 or 65. The day he achieves 16 years' service, the CE has to be calculated based on his leaving and the pension coming into payment so assumes the pension will payable immediately and he may be only age 37. The CE is calculated on it being paid for 23 or 28 years more and therefore it could be two or three times higher than it was the day before.

11.7 Absence of a late retirement factor in the earlier schemes

Some of the earlier schemes, for example NHS Pension Scheme 1995, have the issue that, although retirement age is 60, if the member in fact remains in service until age 65 no actuarial enhancement is applied to the benefits. This can have the effect of overvaluing benefits, particularly for younger members. The individual may not be able to afford to retire at the earlier age and therefore the CE may not be appropriate.

11.8 "Income gap" issues

An income gap issue will occur when the parties are trying to equate incomes but one party receives that income before the other (either in time or because the intention is to equate at a certain age but one receives the income at an earlier or later age than the retirement age proposed in the calculations). As is discussed in the section earlier in this guidance on age differential, income gaps can

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occur in any schemes where the parties are different ages, but in the public sector they can also occur when they are the same age but the Scheme rules mean that they take benefits at different ages.

Issues can arise, for example, where the age at which the pension claimant (i.e. the party with the benefit of a PSO, as pension credit member of the scheme) receives the pension credit benefits is greater than the age at which the pension holder (the original scheme member) can receive their benefits. This is particularly relevant for example in the Police Pension Scheme 1987 and Armed Forces Pension Scheme 1975 Section where a pension sharing order can result in an immediate reduction in a pension that is already in payment but the pension credit member may have to wait for a number of years before they can take benefits from their pension credit under the Scheme rules.

11.9 Early departure payments in the Armed Forces Pension Schemes

Both the Armed Forces Pension Scheme 2005 and the Armed Forces Pension Scheme 2015 have rules whereby if the member leaves after achieving a certain amount of service (and sometimes also a certain age), although their pension is not payable until the Scheme Retirement Age (Age 65 or State Pension Age), they will receive a lump sum and income known as Early Departure Payments (not classed as pension) from the date of leaving until the date when their pension is due (Scheme Retirement Age).

These are not pension and so cannot be subject to a pension sharing order, but are nevertheless payments which are made after leaving as a result of service so have many of the properties of pensions and are an income stream and source of capital for the member.

11.10 Re-Settlement commutation in the Armed Forces Pension Scheme 1975

If the member leaves service *after* the point at which they can take benefits but *before* age 55, they have the option to take a further lump sum *in addition* to the automatic lump sum paid by the Scheme. If they select this option, the pension is reduced between retirement and age 55. It is then brought back to its original amount at age 55. In addition, the pension does not increase between retirement and age 55, but at 55 it is increased to reflect inflation since retirement. This can mean a very large increase in the pension at age 55, and a pension in payment to a member in their early 50s, in particular, can be a lot less than it is due to increase to once they reach 55, and so on face value at that pre-55 stage, it can appear misleading.

11.11 Consumer Price Index being unmatchable on the open market

Public Sector pensions increase in line with the Consumer Price Index ("CPI"). It is often asked how much it would cost to purchase a similar benefit on the open market. But it is simply not possible to obtain a market rate for pensions that increase in line with CPI, so this question cannot be answered.[34]

11.12 The effect of pension sharing where there is a pensionable salary cap

For so long as the salary cap remains in place (in the public sector, it is currently under review), practitioners should be aware of the potential issues with this. For example, suppose the pension holder, a scheme member, has an accrued pension of £20,000 per annum, and there is a PSO against that pension holder for 50%; then although the pension debit made against the scheme member's pension to the pension claimant (which is calculated by the scheme at the time of the order) is initially £10,000 per annum, if the pension holder remains in service but on a salary-freeze or pensionable salary freeze, this can affect the benefit. If inflation is cumulatively 25% over 5 years and there is no increase in pensionable salary, then the pension debit increases to £12,500 per annum leaving only

[34] This is because CPI annuities do not exist in the open market, only RPI ones (because providers can match RPI with gilts but no CPI gilts have been sold).

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£7,500 per annum for the pension holder in respect of the pension rights accrued to the time of the order. This occurs because legislation requires that the pension debit is linked to the scheme benefit, which in this case increases in line with inflation, but the accrued benefit for the scheme member will only be linked to salary, which in this case has not increased.

Although there is not much the practitioner can do about this in many cases, they should be aware of this possibility as it will affect the final outcome for the parties and if known about should be taken into account.

11.13 Valuation and discount rate

Cash Equivalents for public sector pensions are calculated on a basis and tables provided by the Government Actuary's Department ("GAD"). However, the discount rate for the calculations is prescribed by the Treasury. The rate is higher than most actuaries use for calculations in the private sector schemes. This means that the CEs are lower in the public sector than in the private sector for the same type of benefits.

For this reason, practitioners should be very cautious before comparing public sector CEs with private sector ones on an equal basis. Currently, the benefits from a public sector scheme are likely to be higher for a given CE than in a private sector scheme with the same CE.

11.14 Poor health no enhancements

The schemes perform calculations using standard actuarial tables prescribed by the GAD. There is only one set of tables for each retirement age for pension credit members. Therefore, if the potential pension credit member (i.e. the pension claimant) is in poor health, pension sharing will result in a loss of the value of the benefits as the pension credit member will receive benefits based on the assumption they will live for average life expectancy. If their life expectancy is in fact reduced, the actual value of what they will receive is less and there is a resultant loss in the value of the combined benefits. This is because the benefits are calculated as being paid for a longer period but will in fact be expected to be paid for a shorter period.

The converse is also true. For example, if the pension holder is in poor health and has reduced life expectancy, then it will be better for the combined wealth of the parties to share the pension 100% to a healthy spouse, because the pension holder is unlikely to receive the full value of the benefits if they do not live to normal life expectancy.

11.15 Re-employment after retirement

In public sector schemes, sometimes members retire and take a lump sum and the pension becomes payable, and then the pension holder resumes employment within the same public sector. This will often lead to a reduction or ceasing of pension payments until the pension holder retires again. There are different rules in different schemes about whether the salary link is removed on re-employment. Practitioners should take care with this issue. They should also take care that information can be misleading because where a pension in brought into payment and then the member resumes service, the pension might be abated due to rules about the maximum amount the individual is allowed to receive. Therefore, a payslip of the pension might give a misleadingly low figure about the true value as when they finally retire, the pension will resume at the higher level.

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12 Small Self-Administered Schemes (SSAS)

12.1 What is a SSAS?

A SSAS is a type of pension scheme, typically found in owner-managed businesses, often family run. When considering the responses to a Form P, it may not be spelled out that the scheme is a SSAS, but words like "XYZ Ltd Directors Retirement Scheme" will give a clue that you are dealing with a SSAS.

The scheme will comprise of anywhere between 1 and 12 members. Membership is at the discretion of the business owner and is open not only to owner-managers, but also to key staff, family members and even those not involved in the business. A SSAS can make a secured loan to the sponsoring employer up to a maximum of 50% of the scheme's net assets; similarly, a SSAS can borrow up to a maximum of 50% of its net assets.

Assets within a SSAS are only notionally apportioned as between the members. Provided written confirmation is given by all member trustees, it is possible to allocate funds paid in for a particular member to specific investments made with these funds, so that that member's share of the SSAS is determined by the performance of these investments.

12.2 What to do when confronted by a SSAS – key issues and problems to spot

It is in both parties' interests to discuss how they propose dealing with a pension sharing order over a SSAS at an early stage. It must be stressed that burying one's head in the sand about the problems that can be caused by sharing a SSAS, and deciding to worry about the implementation of an order only once it has been made by the court, is a recipe for disaster for both sides. Once an order has been made and served on the pension provider, they have just four months in which to implement it. If the parties only start thinking through the issues at that late stage, there is a very good probability that the pension provider will be in breach of their legal requirement to implement the order in that four-month window.

Problems with valuations

The calculations as to the percentage pension sharing order required are usually pretty straightforward, once the valuation of assets is agreed, but in the case of a SSAS this in itself can be contentious. Often, a SSAS will comprise different asset classes, including commercial property, managed investment portfolios, bank accounts, loans to companies, and insurance policies.

When confronted by a SSAS, the first step is to ensure all of these assets have been recently valued. It may be that a set of scheme accounts is produced, in which the values of the assets are stated. This can be misleading even if the accounts are relatively recent; they may be taking property at a historical value. If so, fresh property valuations will be requested.

Problems with illiquidity, and how to get around them

Since a SSAS can include property and loans as an asset, some SSASs are very illiquid, and would struggle to discharge, in the normal way, a request for a pension debit. Very serious problems will be encountered if it is agreed that any pension sharing order should be for an amount exceeding the immediately available liquid assets, and it is vitally important that these issues are addressed *prior* to any order being made. Problems with liquidity can be further complicated if there are other members of the scheme, besides the divorcing member, who have issues with seeing illiquidity eroded.

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If liquidity remains an issue, there are a number of options. However, often none of the options is palatable, or indeed workable, and the least bad option needs to be identified. Both sides need to discuss the options, and how they intend to implement the order, *prior* to its being made by the court.

The options for dealing with a pension sharing order that requires a pension credit to be granted to the pension claimant in excess of the available liquid assets within the SSAS are:

i. The scheme can try to persuade the pension claimant to retain the credit in the SSAS. In so doing, they need not create any liquidity. However, unless both parties are entirely confident of their ability to work together as trustees post-divorce (a beneficiary of a SASS must also be a trustee), this solution is rarely attractive. Although this internal option (the pension claimant retaining the credit in the scheme) may appear initially attractive, often all it does is defer the problem caused by lack of liquidity.

   Many SSASs rules do not allow the pension claimant to become a member of the scheme, precisely for fear of scheme paralysis. Indeed, some schemes refuse to allow the scheme rules to be amended to admit an ex-spouse as a member.

   Conversely, although the scheme may well try and persuade the pension claimant to retain her credit in the SSAS, it cannot force her to do so; the pension claimant can insist on external implementation.

ii. If the pension claimant were to insist, as she is entitled to, to have a pension credit transferred out, the scheme can look at ways of creating sufficient liquidity. This could potentially be done in one of three ways:

   a) one or more of the properties could be sold
   b) a mortgage / finance could be raised against the property portfolio
   c) the sponsoring employer could make pension contributions to create liquidity.

iii. If the scheme were unable to create sufficient liquidity, and the pension claimant refused the option to retain the credit in the scheme, one possibility would be for one or more of the properties to be transferred *in specie* into a pension arrangement for the claimant.

   For example, if the claimant were to receive a pension credit equating to £500,000, then it might be possible for the claimant to establish a Self-Invested Personal Pension (SIPP) in her own name, and a pension credit comprising one or more of the properties could be transferred into her SIPP.

   This might not be an ideal solution: it could be dependent on the dynamics of the relationship and involvement of the parties in the business (if it is a family business) post-divorce. But if the pension claimant is not part of the business post-divorce, this

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arrangement will mean that the pension claimant, via her pensions, is the landlord of properties let out to the other party's businesses. It is also the case that, were the pension claimant, via her SIPP, to own these premises, she could sell them at any point to a third party; that may not be appealing to the husband if he remained, via the business, a tenant of the properties.

It is also the case that, were the pension claimant to establish her own SIPP into which the properties are transferred *in-specie*, stamp duty would be payable, as the properties would need to be re-registered in the name of the SIPP trustees. A variation on this solution might get around this problem, whereby a separate sub-trust of the existing SSAS is created into which the properties are transferred. This option would not, however, get around the underlying problem of the pension claimant's being the landlord and the pension member, via his business, potentially being the tenant.

As can be seen, there are disadvantages to all of the solutions. The extent of the difficulties would plainly be reduced if the pension holder has other pension benefits outside the SSAS which could be shared in favour of pension claimant instead, thereby reducing the quantum of the pension sharing order required over the SSAS. Alternatively, consideration should be given to whether the case could be resolved by offsetting instead, or at least in part, restricting pension sharing to the extent of liquid assets in the SSAS, and offsetting dealing with the balance.

Plainly, there is often no ideal solution. What is essential is dialogue between the parties *before* the court seals any order, and creative thinking that may entail a combination of the suggested solutions above.

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13 Death in service benefits not related to a pension

Where defined benefit schemes are involved, it is always worth having an eye to whether the death in service benefit component of the scheme is integral to the main pension scheme or whether it is set up under its own separate trust. This is a relevant enquiry to make when analysing pension scheme benefits at the information-gathering stage.

It is not possible to have both a pension sharing order and a pension attachment order against the same pension arrangement. But where the pension provider has established the death in service scheme under a separate trust, then it should be possible to have a pension sharing order against the main pension scheme and, if appropriate, a lump sum pension attachment order against the death in service benefits. This can be a way of providing much needed life cover for no additional cost, particularly where the establishment of a new and separate life insurance policy is cost prohibitive for the parties.

It would be important that any pension attachment order is made against "the Trustees of the [*insert correct name of scheme*] Death in Service arrangement". It should be pointed out to the Trustees when the order is served that the specific insurer is advised of the existence of the attachment order in the event they end up settling any claim. The Trustees should also be advised that it is their responsibility to advise any new insurer in the future should there be a change of insurer.

It is worth noting, however, that death in service benefits are a poor substitute for a properly established life insurance policy separate from the pension scheme. Were the scheme member to leave the employment of that particular company, then the death in service benefit would immediately cease. At that point it might no longer be possible to obtain life insurance, for reasons of health or simply because the person whose life is to be insured may no longer cooperate. With that in mind, it might be sensible if contemplating such an arrangement that an undertaking is obtained from the pension holder that they would co-operate in a life insurance application in the event they left the company and the death in service benefit ceased during the period that life insurance was still required.

Advice should be sought from an appropriately qualified and experienced adviser as to any taxation implications of payments from a Death in Service policy as the amounts of death benefit paid can be large.

Taxation issues (e.g. lifetime allowance) have been ignored for the purpose of this section.

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14 Post-order implementation issues

This section covers the following essential issues related to the implementation of a pension order once it has been made by the court, in order to ensure that the order is indeed implemented as intended:

- Checking the pension order
- Who should serve the order and when?
- Applying for decree absolute
- Undertakings and protecting pension benefits
- What is required to implement a pension sharing order?
- Ensuring a pension sharing order is implemented
- Payment of fees
- Death benefits once a pension order has been made
- Pension provider practice

Key points/recommendations:

- Serve pension sharing orders as soon as possible and follow up with DA once pronounced
- Pension claimant (or their solicitor) should serve the court documents
- Obtain scheme approval that the proposed order is acceptable
- Discuss with parties delaying applying for DA until 28 days after consent order is approved so that PSO can take immediate effect on pronouncement of DA and preserve death benefits in meantime
- Consider undertakings to protect pension sharing order
- Ensure pension holder is warned about possible clawbacks and their potential impact

14.1 Checking the pension order

When making an application for a consent order for pension attachment, the draft order and annex must be sent to the pension scheme for checking before it is submitted to the court for approval to ensure that the pension scheme has no issue with the order and is able to implement it.[35]

Whilst this is not a requirement with a pension sharing order annex, it is good practice to do so anyway. This will help to avoid problems arising once the order has been approved by the court, in particular issues that delay a pension order being implemented.

14.2 Who should serve (send) the order and when?

It is the court's duty to send the pension sharing order or pension attachment order to the pension provider, or direct one of the parties to send it. In practice, the court should not be relied upon and it would be sensible for the lawyer representing the pension claimant (transferee in the case of a PSO) to send it, or the recipient if they are representing themselves. It is also good practice to request written confirmation from the pension scheme that they have received the order and that it is implementable, or that they have no problems with it. If the order has been checked with the pension scheme before it was made then such problems should not arise.

Traditionally, a pension order is sent to the pension scheme once the decree absolute has been pronounced (see below) because without the decree absolute the pension order cannot take effect.

[35] FPR 2010, r.9.34.

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However, it might be considered good practice to serve the pension order on the scheme as soon as it has been made and then send the decree absolute once it has been pronounced. The rationale for this relates to avoiding potential dangers arising from the new pension freedoms that make pensions more readily accessible, e.g. allowing the entire pension scheme to be taken as a lump sum. Sending the pension order to the pension scheme at the earliest opportunity puts the pension scheme on notice that the order has been made, even if it is not yet effective. Given that knowledge, personal pension providers are likely to think twice before allowing pension benefits to be taken or transferred without at least checking that a decree absolute was not imminent. Trustees of occupational pension schemes are likely to take legal advice (which might take sufficiently long for the DA to be produced in the meantime) but that advice could reasonably be that the Trustees have no right to prevent a scheme member exercising their statutory right to transfer in the absence of an effective PSO. Alternatively, on receipt of a sealed PSO the Trustees may view the pension claimant as a potential beneficiary of the scheme and may find it hard to allow any action that might thwart that person's interest.

One way to prevent a pension share being thwarted by a last minute transfer or by a partial taking of benefits is to obtain an undertaking from the pension holder that they will not transfer or otherwise interfere with the pension until the PSO has been implemented. Another option, which might be more appropriate where there are genuine concerns that an occupational pension scheme might be transferred, is to make an application under s 37 MCA 1973 against the pension holder and serve a copy of this on the Trustees so that they too are aware of it.

14.3 Applying for decree absolute

A pension sharing order takes effect on the later of 7 days following the period for appeal, or the date of the decree absolute. As the period for appeal is currently 21 days, the earliest a pension sharing can take is effect is 28 days after it is approved by the court. It is therefore considered sensible practice to delay applying for the decree absolute until after the 28 days so that the pension sharing order takes effect immediately on the date of the decree absolute. This ensures that the recipient of the pension sharing order remains the legal spouse during the 28-day period: crucially, this means that if the scheme member unexpectedly dies in that period, the pension sharing order would not take effect and the scheme would instead find itself dealing with a death claim from a surviving spouse. See also the suggestion below of a corresponding undertaking from the pension-holder. However, in taking this decision about timing, the client needs to be advised about countervailing considerations: for example, the need to obtain decree absolute so as to be able to enforce a lump sum order may be of greater importance to the client than the possibility of the spouse dying after decree absolute and before 28 days have passed.

14.4 Undertakings and protecting pension benefits

It would be good practice, particularly given the new pension freedoms, to obtain an undertaking from the scheme member that the pension benefits will not be interfered with or otherwise changed until a pension order has been served.

Related to the point made in the preceding section, in order to secure the recipient's position, it would be prudent to include a further undertaking in the consent order by the pension holder that they will not apply for the decree absolute until 28 days following the date the order is approved by the court. This would may reduce the possibility of financial disadvantage to the pension claimant should the pension holder unexpectedly die before the order can take effect.

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14.5 Pensions in payment and clawbacks

Where the pension that is to be shared is in payment, there will usually be a clawback (calculated and apportioned on a daily basis) of some of the pension income from the date the pension sharing order took effect. This is because the pension claimant had an entitlement to some of that pension income from that date, not from the *later* date of implementation being completed. The pension claimant ex-spouse then receives this entitlement via the transfer value once the pension sharing order has been implemented. Some pension schemes will pre-empt this problem by amending the pension holder's payments as soon as the scheme is in receipt of an effective order, but these schemes are in the minority. Most pension schemes continue to make the full pension payment to the pension holder until the order is finally implemented, resulting in overpayment to the pension holder that has to be clawed back. While schemes are generally quite good at warning about this in their initial disclosure packs, it still seems to come as a surprise to many individuals.

An even greater problem can occur where the pension holder is required to pay interim maintenance to their pension claimant ex-spouse either until a pension sharing order has taken effect or until it has been implemented. It should be noted that there can be a dramatic difference in time between these two events, and lawyers drafting consent orders should give careful consideration to which is intended. If interim maintenance is to be paid until the pension sharing has been implemented, then not only is the pension holder likely to suffer a clawback situation (described above), but the pension holder will suffer a clawback from those very payments that are allowing the maintenance to be paid. To avoid or mitigate against this problem where the scheme member is required to pay interim maintenance payments until the pension sharing order has taken effect, consideration could be given to imposing some form of time limit on such payments, say, for 2 or 3 months to allow the pension claimant ex-spouse time to take advice and get the order implemented and with an appropriate incentive to do so.

14.6 What is required to implement a pension sharing order

When pension schemes send out the information pack with the CE, they must set out their requirements for the implementation period to begin. Such requirements can vary from a simple on-line request from the receiving scheme and nothing else, to forms requiring completion, fees to be paid, age to be evidenced and current health position to be checked out. In the majority of cases, especially where there has to be a transfer out to a pension scheme of the ex-spouse's choosing, it is hard to complete this process without the assistance of a regulated pension adviser, and ideally one that has experience in the area of pensions and divorce. Mistakes are frequently made by the transferring scheme and an adviser experienced in this area is most likely to spot any mistakes.

14.7 Ensuring a pension sharing order is implemented

The longer it takes to get a PSO implemented, the more likely that problems will arise. This is particularly the case where schemes have not been served with the court documents and so are unaware that the order has been made in the first place. Lawyers are encouraged to put systems in place to ensure that, as far as possible, the PSO gets implemented so that they can close their file on that case. This could include recommending an appropriately qualified adviser and requesting updates from the adviser once the adviser has been instructed. Recipients of the PSO are well advised to seek advice from an appropriately experienced financial adviser at the earliest opportunity.

In a minority of cases, individuals who have been awarded a PSO fail to engage in the process. Lawyers' files should be well-documented to demonstrate they have done all that is reasonably required. Once an adviser has been appointed, in order to reach the point at which the file can be closed it would be

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sensible to request that the lawyers are notified once the order has been implemented, or that the lawyers are alerted if no action has been taken.

The importance of the pension claimant choosing a destination scheme for their pension credit where there is to be an external transfer cannot be over-emphasised. If the pension claimant has been alerted to the need to choose between an internal and external transfer and the further need to choose a destination payment for an external transfer where that route is chosen, the scheme must select a default option if they fail to do so. This will either be by transferring the credit to an alternative arrangement or internally.[36] That said, it is arguable that the trustees may not have to select a default option because, until a destination for the credit is available, the implementation period does not begin to run.[37] This point is capable of operating to the disadvantage of the pension claimant because the credit may be placed in a less advantageous scheme than would have been the case if the claimant had taken proper advice as to the best destination scheme. It may also operate to the disadvantage of the pension holder because the provider may be reluctant to commence benefits in circumstances where there is a pension share which has not been implemented. For all of these reasons, it is crucial for both pension claimant and pension holder to ensure that a pension sharing order is implemented in a timely manner.

14.8 Payment of fees

A pension scheme is entitled to make a charge for PSO services and particularly the implementation of a PSO. These fees frequently range from nothing at all to large sums running into thousands of pounds. Schemes are allowed to set the fees that they feel appropriate, but these generally fall within a range recommended by the Pensions and Lifetime Savings Association. Once the fees have been quoted they can only be increased each year by inflation, unless another CE is requested by the pension holder, in which case any increase in charges since the last CE quotation can now be advised.

As a matter of best practice, the lawyers should identify in advance of the order being made the funds from which the implementation fees should be paid and by whom. If the fees are to be paid by the pension claimant, this could be done from the pension share itself, if the scheme is willing to facilitate this. If the fees are to be paid by the pension holder, they usually have to be paid in advance of the order being implemented. Consideration of the percentage split and the source of the funds should be considered when drafting Heads of Agreement or drafting the consent order in court, where a copy of the pension sharing annex is often not immediately to hand and this particular aspect can easily be overlooked.

In default of the split being covered in the pension sharing annex, the pension holder is liable for all the fees.

It is common for the charges to be shared between the parties. In most cases, the implementation period will not start until both parties have paid their fee. If one party delays the commencement of the implementation period by failing to pay their share of the fees, it is important that that party is made aware that by not paying the fee they are preventing the pension scheme from implementing the order, assuming all other requirements have been met. Rules around how the non-payer's fees can be met will differ from scheme to scheme, but the court would be likely to take a dim view were this matter to come before the court for enforcement.

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[36] Welfare Reform and Pensions Act 1999, s35(1), Sch 5; Pension Sharing (Implementation and Discharge of Liability) Regulations 2000 (SI 2000/1053), regs 7-9.
[37] Ibid, s 34(1)(b); Pensions on Divorce etc (Provision of Information) Regulations 2000 (SI 2000/1048), reg 5(c).

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14.9 Death benefits once a pension order has been made

Once a PSO has been approved by the court, it cannot take effect for at least 28 days, or until the date of the decree absolute, whichever is the later (see above).

It is important to protect the financial position of the pension claimant during this period, and the easiest way to deal with this is to avoid applying for the decree absolute until the 28 days has expired.

Should the pension holder die before or during the 28 period then the PSO cannot take effect and the scheme benefits that would otherwise have formed part of the pension share now form part of the death claim. Death benefits are distributed by the scheme Trustees according to the rules of the scheme.

Should the pension holder die after the 28 days has expired and after the decree absolute has been pronounced, then the PSO has taken effect. In this event, the pension claimant is entitled to the benefits awarded by the PSO and the order must still be implemented. Only benefits remaining after the PSO has been implemented would be subject to payments from the death claim available under the terms of the scheme.

In the case of a pension attachment order: should either party die after the order has been made then no further payments are due to be made.

14.10 Pension providers: points to watch out for

Pension providers or administrators should be encouraged to invest in more training for those administrators involved in this particularly complex area. Mistakes are sadly all too common and it is also a concern that mistakes often go unchecked. Those organisations that have established national or centralised pension on divorce teams should be applauded and other large organisations encouraged to follow suit. It is not uncommon to see good practice from one department and poor practice from another of the same organisation.

Some common mistakes that are all too frequently observed are:

- Incorrect CE or calculation of pension holder's benefits
- Incorrect information being provided relating to pension holder's benefits and related scheme rules
- Lack of understanding of how CE at the point of implementation are calculated, i.e. CE calculated during the implementation period based on the benefits that existed when the PSOP took effect (Valuation Day).
- Misunderstanding about when the Valuation Day is and that it has to be some point during the implementation period – valuations are often, incorrectly, made in advance of the implementation period commencing
- Misunderstanding about what is being valued on the Valuation Day
- Not understanding the definition of the Transfer Day, i.e. the day on which the PSO takes effect.
- Generally misunderstanding the entire pension sharing process
- Trying to enforce external transfers from a final salary scheme when a CE has been reduced due to scheme underfunding
- Scheme Trustee's/administrator's failure to understand that 'original' court orders do not exist, only original copies that have been sealed by the court

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The importance of understanding the interaction between the Transfer Day and Valuation Day becomes particularly important in a post- pension freedoms world, where significant defined contribution benefits can be drawn down from a defined contribution scheme.

Where mistakes have been made, or where there is concern that a mistake has been made by the transferring scheme, this should be taken up with the scheme. If this does not resolve the problem and where the scheme is an occupational pension scheme, the Pension Holder or Pension Claimant should first complain to the scheme under what is known as the Internal Dispute Resolution Procedure (IDRP). Only once that route is exhausted can the complaint be taken to the Pensions Ombudsman. However, individuals would first be encouraged to seek help from The Pensions Advisory Service which has a dispute resolution team equipped to assist with such complaints. [This service is due to be merged with the Pensions Ombudsman's office in mid-2018] There is no cost for this service.

14.11 Pensions and enforcement of other financial remedy orders

It should be remembered that pension sharing orders are not presently available as a *direct* method of enforcement. The Law Commission's report *Enforcement of Family Financial Orders*[38] contained a headline proposal that pension sharing should be available as an enforcement method. This recommendation has not been implemented. However, it should be borne in mind that judgment creditors can enforce against a debtor's pension following the procedure in the Chancery case of *Blight v Brewster*.[39] This procedure has application for people who are owed monies under a financial order made in family proceedings and may be summarised as follows:

> 1. The respondent may be ordered to delegate his power of election for drawdown of pension benefits to the applicant's solicitor (by way of mandatory injunction);
>
> 2. The applicant's solicitor may then be authorised to make the election for drawdown of the tax free lump sum directly to the pension provider;
>
> 3. A third-party debt order can be made, which takes effect when the election is made and attached to the debt now due from the pension fund to the respondent. The third-party debt order has the effect of channelling the tax-free lump sum directly to the applicant.

In addition to the procedure in *Blight v Brewster*, in the case of *Amin v Amin*,[40] the Court of Appeal upheld Moylan J's decision to adjourn the wife's application for a pension sharing order pending the payment of a lump sum. On the husband's failure to pay the lump sum, Moylan J made a pension sharing order in the wife's favour. In this way, pension sharing may be used as an *indirect* enforcement/policing mechanism

[38] Law Com No 370 (HMSO, 2016).
[39] [2012] EWHC 165 (Ch).
[40] [2017] EWCA Civ 1114.

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15 Pensions where an application has been made to vary the original order

The role that pensions play in variation applications is problematic. The breadth of judicial discretion is such that it is difficult to advise clients with any certainty of the outcome of variation applications. This is demonstrated by the following example:

The parties (H and W) to a 25-year marriage with two now adult children divorced in 2001.

A compromise was reached such that:

- The £1.6m non-pension capital was divided equally between them.
- Pensions were divided such that W received a pension share of H's money purchase scheme and H retained entirely a Public Sector pension. The CEs at the time were broadly equivalent. The certainty of the return and prospects for growth of the different pensions were very different.
- H was to pay W maintenance of £50,000 on a joint lives basis from his earned net income of £150,000.

In 2016, H opens a discussion with W as to how a clean break might be achieved on his imminent retirement. Their respective financial positions are:

H:

- He lives in the former matrimonial home which is now worth c£3.5m and is subject to a £1.7m mortgage.
- He has additional non-pension assets worth in the region of £1m.
- The element of his retained money purchase SIPP is now worth £400,000. His Public Sector pension now has a CETV of £3.2m and will produce a guaranteed index-linked income in retirement of £120,000 gross per annum.

W:

- She lives in an £800,000 property free of mortgage.
- She has an ISA with a value of £120,000.
- She has a SIPP with a value of £700,000.

The leading authority relevant to this set of facts is *Pearce* v *Pearce*.[41] A pension sharing order was not available on Mrs Pearce's application to vary a periodical payments order because her petition long pre-dated 1 December 2000 (so, unlike in the example being explored here, the court lacked any jurisdiction to make orders over the parties' pensions at any stage). However, Thorpe LJ opined as follows:

> *Of course I recognise that it is likely to be many years before the typical case invoking the court's jurisdiction under section 31(7B) [the power of variation] has cleared the restriction imposed by section 85(3)(b) [which prevents pension sharing orders being made ancillary to petitions issued before 1 December 2000]. That is regrettable. In this outpost of the ancillary relief territory the task of the*

[41] [2003] EWCA Civ 1054.

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> *practitioners and the judges would be much eased by the option of providing for the former wife a personal pension carved out of the former husband's pension portfolio.*[42]

Thorpe LJ concluded his judgment as follows:

> *There are advantages and possible dangers in attempting in a paragraph to summarise the message of this judgment. What follows is therefore not intended to be a substitute for a full reading where necessary. But my essential general conclusions are:*
>
> *i) On dismissing an entitlement to future periodical payments the court's function is not to reopen capital claims but to substitute for the periodical payments order such other order or orders as will both fairly compensate the payee and at the same time complete the clean break.*
>
> *ii) In surveying what substitute order or orders should be made first consideration should be given to the option of carving out of the payor's pension funds a pension for the payee equivalent to the discharged periodical payments order.*[43]

The breadth of the court's discretion on the above example set of facts is such that it is conceivable that awards could be made at the following extremes following a contested hearing:

A W receives a pension share against H's Public Sector Scheme that provides her with a guaranteed index-linked pension that, when aggregated with the income generated by her SIPP on an equivalent basis, would meet her reasonable income needs.

B A clean break could be imposed between the parties on the basis that W would treat her SIPP as a *Duxbury* fund such as to meet her reasonable income needs as assessed by the court and there would be no share of H's pension.

These divergent possible outcomes would leave H and W in radically different financial positions in retirement. A would be far more attractive to W and B to H. However, sight must not be lost of each party's broader financial circumstances when advice is given in relation to a variation application. Pension "tunnel vision" must be avoided.

Recommendations and reminders for dealing with variation applications:

- Pensions must not be viewed in isolation on variation applications. It is important to consider them alongside all the other factors which the court is required to balance on a variation application
- Pension sharing orders are not available on variation applications that relate to petitions which were issued before 1 December 2000.
- Pension sharing orders are not available twice against the same pension relating to the same marriage. Accordingly, if a pension sharing order has been made against a pension on divorce, the same pension cannot be the subject of a pension sharing order on a variation application

[42] Ibid at [45].
[43] Ibid.

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relating to the same marriage. But an order could be made against another pension against which no order has yet been made.

- A pension sharing order cannot be made against a pension in respect of which a pension attachment order subsists. However, a pre-existing pension attachment order can be discharged on the variation application, thus permitting a pension sharing order to be made instead against that same pension even if it relates to the same marriage.
- It should be remembered that all species of pension attachment orders are capable of variation <u>except</u> for an order attaching a member's death in service, which cannot be varied after the death of one of the parties.

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16 Pensions and international issues

Two main areas need to be considered:

1. where a pension remedy is required in this jurisdiction against an overseas pension, and
2. where a pension order is required in this jurisdiction against an English/Welsh pension following an overseas divorce.

16.1 Pensions orders against overseas pensions

Given the very real difficulties which can exist in enforcing orders against overseas pensions and the fact that a pension fund may be one of the largest marital resources, the location of the pension may well be a very important issue in deciding the most beneficial forum for proceedings.

The anti-alienation restrictions contained in UK pensions law preventing the transfer of the funds away from the pension holder do not apply to all overseas pensions, although some jurisdictions have comparable restrictions. Where no such restrictions exist, it will be possible to use the flexibility of such pension funds to make a conventional lump sum order as an alternative to a pension sharing order either immediately or on deferred terms (on the basis the pension holder can withdraw funds from the pension to comply with the order) with suitable life cover to protect the intervening period.

It is not possible to make a pension sharing order (or a pension attachment order) against any foreign pension.[44] Alternative strategies are required, depending on the other jurisdiction concerned. Scottish pension providers will usually implement an English pension sharing order. If necessary, an application may have to be made under the Civil Jurisdiction and Judgments Act 1982, Sched 6. In certain circumstances (eg in the USA), it may be possible to implement the sharing of an overseas pension by incorporating in a consent order a recital, backed by undertakings, by means of a Qualified Domestic Relations Order (QDRO) obtainable in the state where the pension is held. This solution involves invoking a freestanding jurisdiction abroad equivalent to the Matrimonial and Family Proceedings Act 1984, Part III. In some jurisdictions (eg Australia), pensions may be split by an agreement as opposed to a court order.

A further possibility, only available with the agreement of the pension holder, might be to transfer the overseas pension (depending on the law of the jurisdiction concerned) into an English pension arrangement so that it will become amenable to a pension sharing order.

Where there are sufficient assets, off-setting may also be a possibility. Other solutions for dealing with an overseas pension might include the use of periodical payments, a variation of settlement order,[45] or a conventional (non-attached) lump sum order.

It must also be borne in mind that in certain jurisdictions, eg Germany, pensions are divided administratively on divorce under a prescribed formula regardless of where the divorce proceedings are taking place. It is important that the English court is aware of such an administrative division of pensions so that no off-setting order is made, resulting in double relief.

16.2 Pensions orders and overseas divorce

English pension providers are not prepared to recognise and implement pension sharing orders made by a foreign court. An English pension sharing order will, therefore, be required to mirror the overseas order.

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[44] *Goyal v Goyal* [2016] EWFC 50.

[45] This possibility was left open by *Goyal*.

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Where a divorce has been granted overseas, such an order may be made under the Matrimonial and Family Proceedings Act 1984, Part 3 (financial relief in England and Wales after an overseas divorce). However, jurisdiction to make such an order only exists on the basis of the domicile of either party or either party's habitual residence in this jurisdiction for a period of one year prior to the application. The existence of the former matrimonial home in this jurisdiction will not found jurisdiction for the purposes of making a pension sharing order. The jurisdictional position is complicated further by the EU Maintenance Regulation.

Where the English court does not have jurisdiction under Part III, the overseas pension sharing/splitting order/agreement may remain unenforceable. Alternative routes may be off-setting (where this is feasible both procedurally and in terms of available assets) or the restructuring of the original overseas order (by way of appeal or variation). Other solutions might include transferring (part of) the English pension to an overseas pension arrangement, against which the overseas order/agreement would be enforceable or by taking advantage of the pension freedoms created by the Taxation of Pensions Act 2014 (where possible and subject to due consideration of the tax consequences). A further (but less satisfactory) solution might be to adopt a form of deferred implementation once the pension is in payment, ie by a type of maintenance order made in the overseas proceedings akin to pensions attachment.

It might, exceptionally, be possible to found jurisdiction to obtain a pension order in the English court by reliance upon s 15(1A) of the 1984 Act and the EU Maintenance Regulation, art 7 (*forum necessitatis*) which confers jurisdiction where proceedings cannot reasonably be brought or conducted or would be impossible in a third State with which the dispute is closely connected (eg where the divorce proceedings have taken place). The dispute must have a sufficient connection with the member state of the court seised (eg the pension scheme being administered in England and Wales). The pension sharing order would need to recite that the pension sharing order was made for the purposes of maintenance/needs so as to bring the order within the jurisdiction of the EU Maintenance Regulation.

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17 Underfunding of defined benefit schemes and reduced CEs

17.1 Background to scheme underfunding

The vast majority of the UK's private sector final salary related pension schemes are underfunded and are likely to remain so for many years. An employer that sets up a pension scheme for its employees, where the pension payable in retirement is linked to the salary (however defined) that the employee earned while at the company is then responsible for ensuring that there is sufficient money in the 'pot' to meet that future liability. In other words, they must ensure the pension fund has sufficient money in it to pay the pension of the former employees however long they live.

Regular valuations of the pension scheme are carried out by the scheme actuary to ensure that the pension fund has sufficient money to meet those liabilities. If there is a shortfall, the employer must make up that shortfall by paying additional contributions over a period of time. If a company goes bust before any shortfall is made up, there is a government lifeboat scheme called the Pension Protection Fund that may step in and take over the running of the scheme (see next section).

Pension schemes become underfunded for a variety of reasons and often for a combination of these reasons. Examples include insufficient employer contributions or contribution holidays when funds are performing well, poor fund performance or an increase in the cost of providing the pension.

If a member of an underfunded pension scheme who has not reached retirement wanted to transfer their benefits to another pension scheme, their transfer value may be reduced. This reduction prevents them from taking a greater share of the scheme than the scheme trustees can afford. So, for example, if a scheme only had sufficient funds to meet half of its future liabilities, then one might expect the transfer value to be only half of what the full value would have been had the scheme been fully funded.

17.2 Impact of scheme underfunding for Pension Sharing transfers on divorce

On divorce, where a pension claimant is to receive a share of the pension holder's final salary pension scheme, the fact of the scheme being underfunded means that the scheme trustees can reduce the transfer value that is due to be paid to the pension claimant. However, most private sector final salary pension schemes (underfunded or not) insist on pension claimants taking their pension transfer to a pension scheme in their own name. It would be unfair, in these underfunded cases, if the scheme could insist on a transfer out of the scheme and then reduce the transfer value due to scheme underfunding; by contrast, the pension holder has a choice as to whether to accept a reduced transfer value (which would arise were he or she to leave the scheme) or stay in the scheme. And so, in order to avoid this unfairness, the law requires scheme trustees who reduce transfer values on divorce either:

- to offer the pension claimant an internal transfer option, which would mean no loss of benefit unless the scheme eventually went into the Pension Protection Fund (see next section), or
- to require a transfer out of the scheme but on a *reduced* basis, where an internal transfer on an unreduced basis has been refused.

The decision for the pension claimant in this situation is a tricky one, especially if there is also a concern the company might go into liquidation. Do they take the internal or shadow membership option knowing the scheme is underfunded (which may not in itself be a problem), or do they risk taking what can often be a substantially reduced transfer value (CE)? It is important for advice to be sought from an appropriately qualified adviser in this situation so that all the relevant factors can be discussed and considered. Lawyers acting in such cases would be well advised not to be drawn into being seen to

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give guidance or advice. This is a specific situation where the advice around these two options is considered by the FCA to be regulated transfer advice, as opposed to just regulated advice. There are much more stringent requirements for advisers engaged in this type of activity.

17.3 Offsetting against reduced transfer values

A final salary scheme CE rarely reflects the true value of the pension scheme benefits. This makes it incredibly difficult to compare this value with an equivalent amount of cash or, say, the value of the family home. Pension experts are often required to report on a fairer value.

In cases where final salary scheme Cash Equivalent Values are reduced owing to scheme underfunding it is important not to use the lower, reduced value for offsetting purposes: it is the full unreduced value that more closely reflects the value of the pension holder's pension benefits. The reduced transfer simply reflects the fact that there is insufficient money *at present* to allow the trustees to meet all of their liabilities. Unless the company has already gone into liquidation, it is reasonable to assume that the company will have a scheme deficit reduction plan in place to reduce the amount of the funding deficit and transfer values will eventually increase again.

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18 The Pension Protection Fund and divorce

18.1 Overview

The Pension Protection Fund (PPF) is a fund of last resort, set up to pay compensation to members of eligible defined benefit pension schemes that fail and cannot meet their liabilities where the failure arose after 5 April 2005. (For pre-5 April 2005 failures, see the Financial Assistance Scheme, discussed in the next section.)

Entitlement and payments made by the PPF are referred to as compensation rather than pension entitlements or payments. The PPF provides compensation in situations where there is a (qualifying) insolvency event in relation to the scheme's sponsoring employer and there are insufficient assets in the scheme to provide at least PPF levels of compensation.

Some very small pensions schemes, for example those with fewer than 12 members, all of whom are trustees of the scheme, or those with just one member, are not eligible. Public-sector schemes including the Local Government Pension Scheme are not eligible. In part, PPF compensation is funded by a levy paid by all eligible pension schemes and in part from the funds of schemes that transfer into the PPF. It succeeded the Financial Assistance Scheme, payments under which the PPF now administers.

To qualify for entry into the PPF, the scheme's sponsoring employer must be in a situation in which it cannot pay the shortfall in the scheme funding, often because it is insolvent. Therefore, an insolvency practitioner will usually be appointed to deal with winding up of the employer. One of the insolvency practitioner's responsibilities is to notify the PPF of the insolvency event. If a pension scheme member or any other party makes the PPF aware of the insolvency of an employer, but an insolvency practitioner has not been appointed the PPF has the power to regard an insolvency event as having occurred.

When such an insolvency event occurs, the PPF has a period of 28 days in which to decide whether the scheme is eligible. If it is, an Assessment Period commences, an extremely lengthy process that can take many years. During the Assessment Period, the scheme trustees are responsible for paying pensions but at PPF compensation levels.

If at the end of the Assessment Period an actuarial valuation confirms that the scheme cannot pay benefits at or above PPF compensation levels, it will transfer into the PPF. The transfer process can take around six months to be completed and only when it is completed is the scheme formally regarded as being in the PPF.

Schemes will not necessarily complete all stages of the PPF process. Some schemes may not proceed beyond the assessment process, for example, if the sponsoring employer is rescued as a going concern or the business is sold and another body takes responsibility for the pension scheme liabilities.

18.2 Pension scheme underfunding and insufficiencies

Pension schemes are under a statutory obligation to meet minimum funding objectives that are designed to ensure that schemes have sufficient funds to meet their current and anticipated liabilities. If an actuarial valuation shows that a scheme cannot currently meet those objectives, it is said to be underfunded, and the trustees are required to work with the sponsoring employer to put a recovery plan in place. That may involve the employer making exceptional contributions over several years and may also include changes to the benefits provided to reduce the liabilities.

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Pension scheme trustees can act to protect an underfunded scheme from members transferring benefits by reducing transfer values. Before they can take that step, the scheme's actuary must have provided an insufficiency report; but trustees are not obliged to reduce transfer values even if such a report is produced.

Although pension scheme underfunding may be cause for concern, the underlying consideration must be the strength of the employer's covenant and its ability to improve the scheme's funding over time. It would be incorrect to assume that every underfunded pension scheme, even those which are reducing transfer values, are necessarily heading for the PPF.

18.3 The PPF on divorce

Search facilities on the PPF website can be used to establish whether a pension scheme is in the Assessment Period or has transferred into the PPF. Separate searches on the PPF website do have to be made for both schemes in the Assessment Period and Transferred Schemes. Those schemes that have notified the PPF of an insolvency event and those in the Assessment Period are the most problematic in divorce cases owing to the inevitable uncertainty that will exist until the Assessment Period is concluded. During that period, the scheme will still issue CEs and pension sharing orders can still be made and implemented by the scheme, but CEs are likely to be reduced.

Those who were over the scheme's normal pension age when the Assessment Period started, or in receipt of a dependant's or ill-health pension will usually receive 100% of their pension as PPF compensation. Any PPF compensation relating to service before 5 April 1997 in the original scheme does not increase. In contrast, PPF compensation relating to post-5 April 1997 service goes up at the rate of inflation subject to a cap of 2.5% per year, irrespective of what the original scheme would have provided.

If a scheme transfers into the PPF, members not in receipt of pension when the Assessment Period commences will receive compensation payments commencing at age 65,[46] again irrespective of the normal pension age in the original scheme. Such compensation is at 90% of the original pension and subject to a cap (at April 2017, this was £38,505.61, which equates to a maximum compensation of £34,655.05). For those with 21 or more years' service in the original scheme, the cap is increased. Increases in the cap are at the rate of inflation limited to 2.5% per year. Compensation can be taken early, in which case it will be subject to actuarial reduction, or deferred, in which case it will be increased.

PPF compensation can be shared or attached on divorce by making a compensation sharing or attachment order.[47] The PPF will provide CEs on request. Contrast compensation under the Financial Assistance Scheme (see next section), which cannot be shared or be subject to an attachment order.

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[46] Note the PPF rules here are not related to state pension age.
[47] See MCA 1973, ss25E-G.

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19 The Financial Assistance Scheme and divorce

19.1 Overview

The Financial Assistance Scheme (FAS) is another compensation scheme for those who have lost out on their pension. Eligibility for the FAS is limited to defined benefit pensions schemes which meet all the following criteria:

- The scheme was underfunded and started to wind-up between 1 January 1997 and 5 April 2005,[48] and
- The scheme did not have sufficient funds to pay members benefits, and
- Either
    - The sponsoring employer cannot pay because it is insolvent, no longer exists or no longer has to meet its commitment to pay its debt to the pension scheme

      or
    - The scheme started to wind-up after 5 April 2005 but is ineligible for compensation from the Pension Protection Fund owing to the employer becoming insolvent before that date.

The FAS closed to Notification and Qualification of new schemes on 1 September 2016, consequently only those schemes which have already been notified to the FAS will be accepted into the scheme. Some schemes are still under assessment by the FAS and consequently their eligibility has not yet been determined.

For the scheme to qualify for the FAS, it was necessary for the application process to be started by notifying the FAS of the event. Trustees, scheme managers, professional advisors, a surviving spouse or civil partner of a member of the scheme who has died or members of schemes that met the eligibility criteria were able to notify the FAS of the insolvency event. In the case of fully wound-up schemes, the former trustees, scheme managers or professional advisors of schemes were able to start the application process by notifying the FAS. All schemes that have completed the initial notification are named on the FAS web site and the scheme status (within the FAS process – see below) is given.

Once the FAS has been notified of the event, there is a qualification process during which the pension scheme provides the evidence required by the FAS Scheme Manager and eligibility for the FAS is checked. The FAS qualification process could take six months or more. Not all schemes complete the qualification process: some are unsuccessful. There are eight scheme codes ranging from *Notified – Unsuccessful* through to *Acceptable – final data received for all members*. If a scheme successfully completes the qualification process, the members will become entitled to FAS compensation.

If the scheme is still in the winding-up process, the final amount of FAS compensation due to eligible members can only be calculated once that process has been completed. This can take several years. The FAS Scheme Manager has the discretion to award initial payments to those members of schemes that have successfully completed the qualification process

Unlike the PPF, the FAS is a top-up arrangement and therefore those entitled to FAS compensation may receive it in addition to the benefits the pension scheme pays or will pay.

[48] For failures after this date, see the Pension Protection Fund, discussed above.

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19.2 The FAS on divorce

The FAS website lists all schemes which have been notified to the FAS together with the schemes' current status.

Those schemes that have successfully notified the FAS but have not yet progressed through to Qualification are the most problematic in divorce cases owing to the inevitable uncertainty that will exist until the qualification decision has been made.

During that period, the scheme will still issue CEs and pension sharing orders can still be made and implemented by the scheme, but CEs are likely to be reduced.

Those who are eligible for FAS compensation will receive a maximum of 90% of the pension accrued in the original pension scheme, subject to a cap for any one FAS member. The cap applies to the combined total of any pension from the original scheme and the FAS compensation. For members whose entitlement begins between 1 April 2017 and 31 March 2018, the cap is £34,229 a year. The cap is revalued each year according to the increase in the Consumer Prices Index.

Compensation is paid from the normal retirement age of the original pension scheme but not before age 60. From the date the scheme winds-up to the normal pension age, any part of the accrued pension which was entitled to increases in accordance with the original pension scheme rules will increase from wind-up date to 30 March 2011 at the rate of the increase of the Retail Prices Index, up to a maximum of 5% per year. From 31 March 2011 to the normal retirement age, increases are at the rate of increase of the Consumer Prices Index up to a maximum of 5% per year. Once compensation is in payment, only that part of the original scheme pension which accrued from April 1997 increases each year by the rate of increase of the Consumer Prices Index capped at 2.5% per year.

If a pension sharing order is made and it takes effect before the scheme winding-up is completed or before the scheme has transferred into the FAS, it should be implemented by the original pension scheme trustees. If a pension sharing order is made and it takes effect after the scheme wind-up is completed or transferred to the FAS, the trustees of the original scheme are <u>not</u> required to implement the order by sharing the pension holder's pension rights.

FAS compensation <u>cannot</u> be subject to pension sharing, compensation sharing or attachment orders but the FAS compensation can be considered when determining the extent of any orders against shareable pension rights and / or PPF compensation or as a resource generally.

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Appendix 1: Draft letter of instruction to a pensions expert (PODE)

SPECIMEN LETTER OF INSTRUCTION TO A PODE

Mr Smith

Smith's Pension Consultants

1 High Street

Uptown

UP1 3YH

Dear Sir/Madam

Pension Report for the Purposes of Family Proceedings - Mr and Mrs Jones

This letter is written on the joint instruction of Mr and Mrs Jones, who are involved in divorce and associated financial proceedings in the Family Court sitting at Uptown – Reference VVF17XXXXXXX

Mr Jones is represented by Mr White of A Firm LLP and Mrs Jones is represented by Ms Green of Law & Co Solicitors of 65 New Street, Uptown, UP13KT Tel 050 1234 9876 email green@lawco.net (Ref: SG).

[It has been agreed] / [An order has been made] by District Judge Smith in the Family Court sitting at Uptown on [ ] that a report should be prepared by a single joint expert about [Mr Jones'][Mrs Jones'][the parties'] pension provision and pension sharing [or attachment orders]. [A copy of the order is enclosed.]

The purpose of this letter is to set out your formal instructions to act as the Single Joint Expert in this matter.

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Overall the aim of the instruction is for the court and parties to understand [*insert brief explanation as to what is trying to be understood]*

Background

Mr Jones' date of birth is [ ] and he works as a [ ].

Mrs Jones' date of birth is [ ] and she works as a [ ].

Both parties are in good health and neither party is a smoker.

The parties started cohabiting on [ ]

The parties married on [ ]

The parties separated on [ ]

The petition was issued on [ ]

The decree nisi was issued on [ ]

The decree absolute was issued on [ ]

The parties' respective pension resources are summarised in the table below:

Pensions	**Mr Jones (CE) £**	**Mrs Jones (CE) £**
Pension 1		
Pension 2		
Pension 3		
Total CEs		

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We enclose the following documentary evidence:

[NB This list is not exhaustive. The expert may have their own list of information that needs to be provided at the outset, but provision of the following information should be considered.]

- Paragraph 2.13 from each party's Form E and supporting documents, including evidence of CEs
- Form P for each policy and the response from the pension provider
- State Pension forecasts for each party

We anticipate that you will need to obtain additional information and letters of authority from both parties to enable you to obtain that information directly from the pension providers are also enclosed.

Nature of instructions

[NB Consider carefully what the expert is being asked to report on. This list is intended to cover common requests, but is not exhaustive.]

You are therefore instructed, as a single joint expert, to provide a report advising on:

- the pension sharing order or orders that would achieve equalisation of pension benefits in retirement, both in respect of income and lump sum (where possible), based on the current CEs of the parties' pensions; and/or

- the pension sharing order or orders that would be required to achieve capital equalisation of the parties' pensions based on an assessment of the 'true value' of the parties' respective pensions; and/or

- *[NB consider whether the report should consider offsetting or attachment orders.].*

- *[If offsetting is required]*

- Please provide an analysis of the offsetting options available here and, if possible, suggest the approach you favour most in this instance, and why. You may find it helpful to refer to the Pension Advisory Group report which describes the various approaches which might be deployed.

- We would be grateful if you would consider the issue of how tax may impact upon the calculation but we do not require you to give any adjustment on account of any perceived "utility" as that will be a matter for the parties or the court.

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- Please advise on the approach to be taken if there is to be some pension sharing and some offsetting.

It should be assumed for the purposes of your report that:

[NB These are just examples of assumptions that may be relevant. Again, it is important that the purpose of the report, and therefore the basis on which it is being requested, is considered carefully in each case. Before committing to a joint report, it may be appropriate to take advice from a shadow pension expert. These may or may not be relevant and are not exhaustive or in any way standard assumptions.]

- The benefits are to be equalised at the following date(s) *[see explanatory notes below on the selection of a date or dates]*

- State Pension will be taken into account;

- Pensions should increase in payment at equivalent rates (or an explanation given as to any differences). *[NB this will not be the case where there are guaranteed annuity rates attaching to a pension, or the payments are index linked]*

- There will be no income from other sources (so that income tax treatment will be equal).

As you will be aware, the instruction of experts in family proceedings is set out in Part 25 of the Family Procedure Rules ("FPR"). Please note in particular Part 25.14, which sets out details of the contents of an expert's report and the statement required at the end of your report under Part 25.14 (2).

We are attaching a copy of Part 25 and of the relevant Practice Directions to Part 25, known as PD 25A, B, D and E.

We also attach a document produced by the Pensions Advisory Group which sets out a number of matters which should be subject to self-certification in your report, including in relation to a number of core competencies. We expect that your report will contain appropriate self-certification of these matters.

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As a jointly instructed expert you should not enter into correspondence or engage in conversations with one party or their advisers without copying it to the other party or their solicitor, as your role in the proceedings is an impartial one.

If there is any aspect of this letter which is unclear, please write to both A Firm LLP and Law & Co Solicitors to raise any issues or questions which may arise, including proportionality, lack of clarity or completeness in the instructions and/or the possible effect on fees of complying with the instructions.

You should be aware that, although it is very unlikely, you may be required to give evidence in person to the Court following your report, by attending a hearing in the case. If this eventuality arises we will contact you further to ascertain your available and non-available dates.

Timing

[The court has ordered] or [It has been agreed] that this report should be produced by no later than [ ].

If you believe that you cannot prepare your report within that timescale please let us know as soon as possible and provide an indication of the timescale that you would consider realistic to complete your report.

We will keep you informed of any changes to the court dates.

Your fees

Mr and Mrs Jones accept that they will each be responsible for 50% of your charges and each solicitor should be invoiced for one half of your fees [or alternative details as agreed or ordered]. Separate invoices should be addressed to [each firm of solicitors] [each client].

[NB Consider what the appropriate costs position should be for the costs associated with raising questions after the report. These costs will usually be in addition to the costs of the main report and therefore how they are to be paid should be dealt with at the outset. A request for this to be included in the directions made by the court is suggested, e.g.: If either party raises questions about your report, the party who raises those questions will be

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responsible for your costs of answering the questions and a separate invoice should be raised for that purpose [or alternative details as agreed or ordered].]

You have indicated that you envisage your fee will be [£] plus VAT for the production of your report [inclusive or exclusive of expenses/disbursements]. [Please do not start work on your report until you have provided us with your costs estimate and that estimate has been accepted by both parties.] [Please advise us if having now received the letter of instruction your fee estimate has changed]

Please also indicate what your fees will be for attendance at a hearing, in the unlikely event that this is required.

Law & Co Solicitors have confirmed their agreement to these instructions by countersigning this letter/writing to you direct.

Could you please send one copy of your report to each solicitor and one additional copy to us for filing at court.

We look forward to hearing from you.

Yours faithfully

A FIRM LLP LAW & CO SOLICITORS

Dated:

Explanatory notes for draft letter of instruction

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Due to the complexity of pension schemes, particularly defined benefit schemes which each have their own nuances, detailed information is often required. It is strongly recommended that Form P has been obtained before requesting the pension report from the pension expert.

The ability to obtain detailed information can lead to extensive delays in preparing pension reports.

The draft letter of instruction is based on a core standard of information that will be included within a pension report.

Additional instructions can be added to the standard but such additions are likely to have an effect on the cost of the report and possibly the length of time to be able to produce the report.

Retirement age

When an 'equalisation of incomes' report is to be produced it is important that careful thought is given to the date towards which the expert is being invited to target his calculations. Although the PODE may be able to provide some comments on the choice of date (for example, if it is a date prior to relevant benefits being payable without discount from a particular scheme), the choice of date is primarily for the selection of the parties. The choice of this date will depend on issues such as the normal retirement date in relevant pension schemes, state pension age, the ages of both parties and the difference between these ages, income gap issues and the asserted future work plans of relevant parties. It may be possible for the parties to agree the target date, but sometimes the parties will differ, seeing some advantage to them in a particular selection. If so, the expert can be invited to provide calculations for two or more target dates. Parties should be made aware that the more calculations the PODE is being required to make, the greater will be the cost, and potentially the delay in production, of the report. Accordingly, parties should be cautioned against too great an array of dates, although sometimes a range of target dates and thus possible outcomes can be useful.

Offsetting

If a request for off-setting calculations is to be included within the letter of instruction then the parties should give thought to the parameters of this investigation in the context of the part of the report of the Pensions Advisory Group on off-setting issues. For example, the expert might be asked to provide a range of outcomes for off-setting purposes (e.g. realisable

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value, replacement value or net actuarial value). The expert will usually be asked to consider taxation issues, but probably not ‘utility’ issues.

Lifetime Allowance/Tax Implications

The expert(s) can be asked to comment on the extent to which the Lifetime Allowance may affect either party. This may include the impact if either party has any form of protection against the Lifetime Allowance and comment on the protections that may be applied for in order to minimise or mitigate the effect of the Lifetime Allowance.

Apportionment for period of marriage

If it is a “needs” case then it is unlikely that a court will be assisted by the production of calculations which exclude pension rights accruing from pre-marital or post-separation contributions and these should rarely appear in letters of instruction to PODEs.

In a case where the assets exceed the needs then there might be justification for including separate calculations which exclude pension rights accruing from pre-marital or post-separation contributions. The simplest and therefore cheapest methodology for this is for the PODE to apportion the benefits on a straight timeline basis, but this can lead to an unfairness in some circumstances and the PODE might be asked to consider calculations based on other methods, for example calculating the CE of the fund at the beginning and end of the marriage.

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Appendix 2: Draft disclaimer letter for potential use with client who declines advice to seek expert report

It has been suggested to us that some practitioners are concerned about professional negligence potentially liability arising in cases where a client, contrary to advice, has not obtained a formal pension expert report.[49] The draft letter below, slightly amended by the PAG drafting team mainly in order to use the terminology deployed in these reports, has been devised and shared with the PAG as a response to that situation:

> *"I, [client's name] of [address] confirm that I have been advised by my solicitor that I should obtain a pension expert report in relation to my husband/wife's/our pension(s) with XXXXXXXX.*
>
> *I confirm the instructions that I have given my solicitor are pursuant to my own free will and I have not been placed under any pressure or undue influence, and that I am not in any way under duress.*
>
> *My [husband/wife] and I have been negotiating directly between ourselves/attended mediation/been in negotiations via our respective solicitors [XXXX & YYYY]/are currently engaged in court proceedings for a financial remedy order in the Family Court at [XXXXX] issued under Case Number: [ZZZZZZ].*
>
> *Whilst I have details of the transfer value of mine and my [husband/wife's] pension(s) I expressly confirm that I do not wish to obtain a pension expert report in relation to our pension funds and how they should be dealt with following the breakdown of our marriage.*
>
> *I confirm that I do not wish to make a claim against my [husband's/wife's] pension.*
>
> *I entirely accept that without a pension expert report in relation to the issue of pensions, my solicitor cannot advise me in relation to this specific issue and therefore cannot advise me on the terms of the financial settlement which I have agreed with my husband/wife.*
>
> *I accept and agree that no liability will attach to my solicitors, [XXXX] as a consequence of any direct or indirect or consequential, financial loss and/or other prejudice financial or otherwise I may suffer as a consequence of me not obtaining a pension expert report in relation to mine and/or my [husband's/wife's] pension. I understand that the loss to me of not taking this advice could run into [tens or even hundreds] of thousands of pounds"*

[49] We are grateful to Debra Frazer for sharing this draft disclaimer.

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Appendix 3: Issues beyond the PAG remit for the attention of responsible bodies

The primary purpose of the Pension Advisory Group is to produce a good practice guide to pensions on divorce for the benefit of judges, divorce practitioners, experts, mediators and ultimately the divorcing public. PAG has no authority to change the law. However, in the course of its discussions, PAG has encountered various issues which, although outside its remit in that they require changes to primary or secondary legislation or court forms, it considers could help improve practice if addressed by the responsible bodies, such as government departments, pension providers and professional organisations. These issues are summarised below.

A. Primary legislation

A. 1. Pensions and Enforcement

On 15 December 2016, the Law Commission published its report on the Enforcement of Family Financial Orders (Law Com No 370). The government provided an interim response on 2 August 2017, which indicated that a full response would be provided in the context of the government's broader thinking on the Family Justice System. Amongst the Law Commission's recommendations were a number that impact upon issues being considered by the Group. It was recommended that the court should be able to obtain information from inter alia the Department of Work and Pensions and pension providers. The inclusion of pension providers was deemed necessary given the Law Commission's recommendation that enforcement should be possible against a debtor's pension assets. Chapter 9 of the report states that pension orders (pension sharing orders and pension attachment orders) may provide an effective means of enforcement where there are no other assets available and may ensure that the creditor receives what is owed, albeit possibly at a later date. The current inability to enforce against a pension is viewed as undesirable because a pension may be one of the most significant assets held by a debtor. It is, therefore, recommended that a pension order should only be available on a general enforcement application rather than on a standalone enforcement application for a pension order. The Law Commission's view is that this approach strikes the correct balance between the interests of all those who would be affected by the making of pension orders for enforcement purposes without restricting their use to cases where no other assets are available.

The Group endorses the Law Commission's conclusion but expresses no detailed commentary in view of the fact that this area is outside the remit of the Group as requiring primary legislation.

A. 2. Pensions and International Issues: implications for domestic enforcement of overseas orders

Paragraphs 9.58-9.69 of the Law Commission's Report on Enforcement of Family Financial Orders (Law Com No 370) are devoted to giving effect to foreign orders against pensions administered in this jurisdiction. The Report recommends (para 9.66) the introduction of a new ground of jurisdiction under the Matrimonial and Family Proceedings Act 1984, namely, that one of the parties has an interest in a pension arrangement situated in this jurisdiction. In such circumstances, it is proposed that the court's powers under the 1984 Act be limited to making an order against that party's pension. It is recognised in the Report that, in contested cases, or where one party only seeks an order here, caution will be required to ensure that the foreign court has not already taken into account the lack of provision from the English pension (for example, by way of off-setting). It is to be noted that the

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additional ground of jurisdiction is by way of amendment to s 15(1) of the 1984 Act, inserting a fourth ground. It will, therefore, only be of relevance in pension sharing cases which do not involve a maintenance obligation, where the wider grounds of jurisdiction currently contained in s 15(1A) and the EU Maintenance Regulation may apply.

A.3. Pension Attachment Orders and Qualifying Recognised Overseas Pension Schemes (PAOs and QROPS)

Legislation is needed to prevent the transfer of a pension which is subject to a PAO to a QROPS.

Alternatively, there could be a requirement that a notice be given to the former spouse/ pension claimant under the Divorce etc (Pensions) Regulations 2000 reg 4 prior to the transfer so that an application can be made, if appropriate, under MCA s37. Currently, notice only has to be given to the ex-spouse within 21 days of the transfer. However, this alternative would be problematical if the pension provider did not have up to date contact details for the former spouse. In this case they might still find the transfer had gone ahead by the time it was discovered, unless some further provision provided for the former spouse to have to confirm their current contact details or acknowledge receipt before a transfer to a QROPS could proceed.

A. 4. Pension attachment: commutation

It is suggested that consideration be given to amending MCA 1973, s 25B(7)-(7A) as the word "commutation" suggests a power restricted to defined benefit schemes and arguably does not provide the same power to the court where there is an option for the pension member to take a Pension Commencement Lump Sum (PCLS) or tax free lump sum under a defined contribution scheme.

Further consideration might also be given to how to deal with the non-taxable element of an Uncrystallised Fund Pension Lump Sum (UFPLS), which is not a PCLS.[50] It is believed that the power to make an order against UFPLS benefits is contained within MCA s.25B (4), but the current version of the Pension Attachment Annex does not reflect this (see below).

A. 5. Pension attachment – death benefits – children of the family

It is recommended that MCA 1973, s 25C is amended so that it is possible to make a pension attachment order in relation to death benefits in favour a child of the family.

A.6. Pension attachment – allow conversion to a Pension Sharing Order for pre-2000 petitions

See B2 below

[50] Taxation of Pensions Act 2014 Schedule 1 s.57 (4A)(1)(d)

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A. 7. Pension Ombudsman

Could provision be made requiring the Pension Ombudsman to consider complaints in respect of PODEs by way of amendments to the Pension Schemes Act 1993 Part X and regulations made under that Act?

A. 8. MCA 1973, s 28(3): The Remarriage trap

This subsection prevents applications for a financial provision order or property adjustment order being made following remarriage. A pension attachment order is included within the definition of a financial provision order. However, a pension sharing order is outside this provision and it is, therefore, possible for an application to be made for a pension sharing order following remarriage unless there is some other impediment to a pension sharing order being made. There is no logical reason for pension sharing to be excluded from the remarriage trap. It is believed that the omission of pension sharing by way of amendment from the subsection may result from an oversight on the part of the draftsman."

B. Secondary Legislation

B. 1. Set Aside regulations

New rule FPR 9.9A requires an application to be made for set aside where there is a supervening (eg *Barder*) event and no error by the court. Previously this would have been dealt with by way of appeal. The Pension Sharing (Implementation and discharge of liability) Regs, reg 4 requires that where a scheme has been notified that an appeal has been started the implementation period must be postponed until the outcome of the appeal (regs 4(1) (a) and (b). No such provision has been made for the situation in which a set aside application has been made. The regulations need to be amended to include a requirement for implementation to also be postponed pending the outcome of a set aside application.

B. 2. Pension Attachment Orders and Pension Freedoms

Need for new regulation/ guidance for pension providers in cases where pension holder/ member seeks crystallisation under the Pension Freedom provisions and a pension attachment order has been made.

The drafting of some attachment orders, especially those that were incorporated into the main body of the court order in the late 1990's, often conflicts with current options for those taking pension benefits after the age of 55. There is often confusion among those responsible for administering pension schemes as to how to interpret old attachment orders, especially in the wake of the pension freedoms legislation where there is often a mismatch between what the order intended and the options now being taken. This has led to some scheme members taking advantage of this uncertainty to their own advantage and the non-member spouse only discovering what has happened when it is too late to do anything about it.

The FCA consulted on this issue in CP15/30 which concluded with PS16/12 (4.27 – 4.35). No substantive action was taken to further protect the interests of the non-member spouse, leaving it to the DWP. The DWP also consulted on this subject (Nov 2015) and responded in March 2016[2]

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where it concluded "Due to the complexity of the issues, the government has decided that it will delay the introduction of the notification requirement until a later date, in order to allow more time to consider these complex issues, balancing the expectations of both members and former spouses, and explore the possibility of guidance, including who would be best placed to issue it."

It is hoped that the government will not delay too long in introducing suitable protections for non-member spouses.[51]

Other changes in legislation such as the introduction in 2006 of the Lifetime Allowance have also led to unintended consequences. Some scheme members with significant pension benefits have and will continue to find themselves genuinely conflicted when it comes to determining the order in which pension benefits are crystallised. Those who are less well intentioned could favour themselves over their ex-spouses by first crystallising pension schemes that are not subject to the Attachment Order and causing the ex-spouse's pension perhaps to be subject to a 55% Lifetime Allowance charge.

While minor amendments could be dealt with by miscellaneous amendments, perhaps the time has also come for a change to primary legislation to enable those individuals (member spouses and non-member spouses) to discharge their attachment orders, thus allowing a pension sharing order to be made, even where petitions were issued before 1st December 2000.

B. 3. Requirement for PSOs to be checked and approved by pension providers before order is made

It is already a requirement for PAOs to be approved by the pension scheme, but not for PSOs. It has been suggested that a change should be made to secondary legislation to require PSOs (as well as PAOs) to be checked and approved by the pension scheme prior to being filed with the Court. However, the point has been made that when a settlement or order is made at court, this change could cause serious delay, unless the order can be made by the court, subject to approval by the scheme of the 'scheme specific' detail (name, address etc.) to be entered in the annex. Currently, we recommend, as good practice, checking scheme approval in advance whenever possible.

C. Court forms

C. 1. Form P

Pension on Divorce Experts would like to see schemes required to provide more information in Form P, which might encourage Form P to be used more frequently than it currently is. Further information requested includes:

i) the latest annual benefit statement for DB schemes

[51] www.gov.uk/government/uploads/system/uploads/attachment_data/file/505678/government-response-misc-regs-consultation-23-nov-2015-and-call-for-evidence-on-gar-valuation.pdf

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ii) for deferred pension rights in DB schemes, ask at B (3) for the pension at the date of leaving
iii) for DC pensions, add in section C, "Does the policy contain any form of guarantee?"
iv) the date of the latest triannual valuation?
v) whether any material changes to the CE valuation basis are anticipated?
vi) current Commutation Factors at Scheme Retirement Age
vii) details of early retirement options and factors.
viii) Clear definition of rate of inflation used eg CPI, RPI, LPI etc.

C. 2. Form E: State pensions

State Pensions can often be one of the most valuable assets in a divorce and should not be overlooked. Estimates of pension entitlement can be obtained by completing Form BR19. Valuations of shareable rights on divorce can be obtained by completing Form BR20. Completing both forms is the most reliable way of obtaining a full picture of an individual's state pension entitlement. To this end, Form E should be changed to require provision of BR19 and BR20 information.

C. 3. Form D81 statement of information to support draft consent order

A number of improvements could be made to D81, including on income and capital. However, the quality of financial disclosure on pensions is particularly poor[52] and could be improved by a requirement to:

i) provide the information from State Pension forecast (BR19)
ii) list all other pensions separately
iii) specify the name of the pension provider in each case
iv) specify the type of pension in each case
v) say whether the pension is in payment or not
vi) provide the CE of each pension and the date of the CE
vii) say whether an expert has been involved; if so, and if the expert has provided a Defined Contribution Fund Equivalent (DCFE) state the DCFE.

C. 4. Form P2 Pension Attachment Annex

In order to address the potential ambiguities which have arisen in relation to PAOs since the introduction of pension freedoms, we recommend amending 5A(i) of the Form P2 to read: "To be completed where an Order is made under s.25B(4) of the Matrimonial Causes Act 1973",

and in place of the remainder of that paragraph, put:

"The specified percentage of any <u>income</u> payment due to the party with the pension rights that is to be paid for the benefit of the other party:
The specified percentage of any <u>Pension Commencement Lump Sum</u> payment due to the party with the pension rights that is to be paid for the benefit of the other party:
The specified percentage of any <u>Uncrystallised Funds Pension Lump Sum</u> payment due to the party with the pension rights that is to be paid for the benefit of the other party"

---

[3] See Woodward HD with Sefton M, Pensions on Divorce 2014 Ch 4, in which inter alia it was found that pension disclosure was inadequate or unclear in more than two thirds of the 130 cases assessed by the expert.

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5A. (ii) could remain as it is as it reflects the separate power the court has under S. 25B(7).

C. 5. Form P1 Pension sharing annex

Relating to PSOs in respect of additional state pension benefits, PAG recommends amending paragraph C (vi) by adding the words '*percentage of*', to read as follows:

> "Where State Pension is to be shared, if the transferor reaches his/her state pension age on or after 6 April 2016 and divorce or dissolution proceedings start on or after that date, then insert the *percentage of* shared weekly amount of State Pension which is payable. For the definition of the shared weekly amount of State Pension please see section 49A(3) of the Welfare Reform and Pensions Act 1999."

and add '%' by the box.

Further consideration should be given to the removal of discretionary section F. It requires either the lawyer or the non-member spouse to tick the box to inform the pension scheme whether, upon the making of the PSO, the non-member spouse (transferee) receives an internal or an external transfer, where both options are available. Given the complexity of this issue, the availability of internal transfer options generally and the pension scheme's legal obligation to offer an internal transfer if a scheme reduction factor is imposed, which could be after the annex has been sent to the court for approval, then the non-member spouse couldn't possibly be in an informed position to make this decision.

There is an FCA dispensation for regulated financial advisers dealing with PSOs where schemes insist on an 'external transfer only' option in that the PSO transfer is not deemed to be a regulated transfer. However, where an internal transfer option is available then the full, regulated transfer advice rules come into play with the adviser first having to undertake an analysis of the client's options and compare these with the benefits being given up.

If a family lawyer ticks the external or internal transfer box on behalf of their client then they could have inadvertently given regulated transfer advice, which they are not authorised to do. Family Lawyers would be well advised in the meantime not to tick either boxes in section F to avoid that trap.

As the situation could in any event have changed by the time it comes to implementing the PSO, at which point a regulated financial adviser is likely to be involved anyway and would need to check the options available at the point of advice, it is suggested this section is removed from the annex as this is not the time to be making that decision.

D. Post-order implementation issues and miscellaneous

D. 1 Better training for scheme administrators

Recommend that scheme administrators be better trained in Pensions and Divorce law and practice and larger firms (insurers/administrators) to be encouraged to set up specialist Pensions and Divorce units to ensure consistency across firms: Pension providers or administrators should be encouraged to invest in more training for those administrators involved in this particularly complex area. In the PAG's experience, mistakes are sadly all too common and it is also a concern that mistakes often go unchecked. Those organisations that have established national or centralised pension on divorce teams should be applauded and other large organisations encouraged to follow suit. It is not

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uncommon to see good practice from one department and poor practice from another of the same organisation.

D.2. PSOs and failure of pension claimant spouse to name the destination fund

Is a new regulation/ guidance required for pension providers where a pension is subject to a PSO but the pension claimant has failed to nominate the destination fund and the pension holder is due to draw benefits?

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Appendix 4: Glossary

Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
Additional State Pension	ASP	The part of the Old State Pension originally known as SERPS and, later, S2P that provided an earnings-related tier of State Pension. ASP rights can be subject to PSOs but where the pension holder reaches SPA post 6 April 2016 a PSO is only available in certain circumstances.
Annual Allowance	AA	The total of contributions or benefit accrual which an individual can make to pension schemes in any tax year before incurring a tax charge. The current (2017-18) limit is £40,000 per annum or 100% of earnings if less, although there are circumstances in which it could be significantly less for higher earners. See, also, Tapered Annual Allowance and Money Purchase Annual Allowance.
Annuity		An insurance-based income received on a regular basis, most commonly for life or for a contractually determined period. Income can be guaranteed or investment linked, level or increasing, and may or may not continue to a surviving spouse or dependent after death.
Auto Enrolment		A method of compulsion of employers by government to provide pension schemes for employees to which both employers and employees pay.
Basic State Pension		The basic part of the Old State Pension related to a person's National Insurance contribution record accrued prior to 6 April 2016.
Buy Out Plan (s.32 contract)	S.32	Insurance based annuity contract introduced by Finance Act 1981, section 32 to transfer the liability from an Occupational Pension Scheme to the insurer of an individual pension arrangement.
Capped drawdown		See Drawdown
Career Average Revalued Earnings (CARE) scheme	CARE	A type of DB scheme under which the benefit earned in any one year is calculated as a

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		specified fraction of that year's pensionable pay. That year's pension accrual is then 'revalued' every year up until retirement, usually in line with inflation subject to a predetermined ceiling, to ensure it maintains its value in real terms. The pension at retirement is then the sum of all the years' accruals and therefore reflects the member's career average earnings rather than their final earnings (as occurs with a 'final salary' type scheme).
Cash Equivalent	CE	A term meaning the capitalised value of pension benefits. Sometimes referred to as the Cash Equivalent Value (CEV), Cash Equivalent Transfer Value (CETV) or Cash Equivalent of Benefits (CEB), they are all essentially the same. For a Defined Benefit pension scheme the CE is the value placed on the member's benefits by the scheme actuary, using assumptions such as future investment returns, inflation and life expectancies. In the case of an active scheme member, the calculation assumes they left service on the date of the CE. For a Defined Contribution pension scheme the CE is usually the fund value, but this may be adjusted, for example, because of an insurance company's transfer penalty charges or, in the case of a 'with profits' fund, market value reductions or additional final bonuses.
Clawback		Repayment requirements for over paid pension income falling on the pension holder due to the delay between a PSO taking effect and the date it is actually implemented.
Commutation		See Pension commutation
Consumer Price Index	CPI	The measure of inflation most commonly used now by DB pension schemes where pensions are fully or partially protected against inflation.
Contracted-out		A Contracted-out pension scheme is one that enables the scheme member to be (or previously have been) contracted out of SERPS

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		or its successor, S2P. The Contracted-out member will have paid reduced rate National Insurance contributions (or had them rebated in the case of a DC pension) and will have nil or reduced entitlement to Additional State Pension. A Contracted-out pension scheme has to meet certain provisions or provide certain minimum benefits, e.g. Guaranteed Minimum Pension (GMP) in the case of DB schemes or 'Protected Rights' in the case of DC schemes, to which certain rules apply. Contracting-out ended in April 2016 and DC Protected Rights was abolished in April 2012, when Protected Rights benefits were converted into normal DC or money purchase benefits. GMP benefits continue to apply for those DB scheme members who were Contracted-out prior to April 1997.
Crystallisation		The commencement of pension benefits payments from all or part of a pension scheme, either as pension income and/or lump sum. At any point in time pension savings are either 'uncrystallised', 'crystallised' or 'partially crystallised'. Crystallising DC funds can often trigger the Money Purchase Annual Allowance.
Deferred member		A member of an Occupational Pension Scheme who has left service with deferred pension benefits i.e. no immediate pension rights, and has not yet reached the scheme pension age nor (if permitted) begun to take the pension under the scheme's early retirement provisions.
Defined Benefit scheme	DB	A pension scheme where the pension rights are related to a formula at retirement, usually related to the final salary or the career average salary of the pension holder.
Defined Contribution scheme	DC	A pension scheme where the pension rights are related to the amount of money contributed to the scheme and any investment return.

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		Sometimes also called a money purchase scheme.
Defined Contribution Fund Equivalent	DCFE	The value of a DC fund a spouse would need, to match a member's DB pension. Sometimes also referred to as a gross replacement value. Figure based upon assumption that DC fund would be used to purchase annuity to provide the same security of income as the DB holder.
Destination Pension Scheme		The pension scheme utilised by the pension claimant and to which the Pension Credit from the PSO is transferred. This may be the same scheme as the one from which the pension share is derived, or another scheme (new or existing) set up for the former spouse.
Discount/Deferment rate		The % discount rate (per annum) used by actuaries and financial experts to calculate the present value of an asset which will not be realised until some date in the future.
Drawdown		Generic term to describe the taking of 'income', normally from a Personal Pension Plan/SIPP and often by making regular withdrawals from the fund. Regulations applicable to Drawdown depend on which of the following classifications it falls into: **'Flexi-access Drawdown'**, introduced from 6 April 2015, allows individuals the freedom to take any amount they wish from their pension plan (providing the plan's rules so permit). **'Flexible Drawdown'**, available prior to April 2015, allowed individuals who satisfied a minimum income requirement from other sources, to draw down unlimited amounts from their pension plan. **'Capped Drawdown'** commonly known prior to April 2015 as **'Income Drawdown'**, was the only drawdown option available before April 2015 for individuals who did not meet the minimum income requirement. It continues to

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		be an option for those who were in income drawdown prior to 6 April 2015. The maximum income that can be drawn down is capped at 150% of the notional income calculated using the relevant annuity rate set by the Government Actuary's Department (GAD).
Earmarking		See Pension Attachment Order.
Enhanced Protection		See Lifetime Allowance
External Transfer		A PSO implemented by transferring rights to a Destination Pension Scheme that is not the same as the scheme from which the Pension Credit is derived (see also Internal Transfer).
Family Procedure Rules 2010	FPR	Rules governing procedures in the family courts in England in Wales. Particular FPR rules or Practice Directions are referred to in this paper as, for example, FPR r 25.1 or FPR PD 25D.
Final Salary scheme		A type of DB scheme under which the pension at retirement is defined by a formula related to salary at or near retirement (or earlier death) and length of pensionable service with the employer e.g. 1/60th of Final Pensionable Salary for each year (or part year) of service.
Financial Conduct Authority	FCA	Regulator for financial services firms and markets in the UK.
Financial Ombudsman Service	FOS	Resolves complaints against financial services providers and advisers in the UK.
Fixed Protection 2012, 2014 and 2016		See Lifetime Allowance
Flexi-access drawdown	FAD	See Drawdown
Flexible annuity		An annuity, the income payments from which may increase or decrease in value over the term of the annuity.
Flexible drawdown		See Drawdown
Government Actuary's Department	GAD	Department of government providing actuarial services across government, including public service pensions.

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
Graduated Retirement Benefit		An earnings related way of accruing. State Pension rights between 1961 and 1975.
Guaranteed Minimum Pension	GMP	Between April 1978 and April 1997, a DB scheme had to provide a pension at least equal to the (revalued) GMP in order to be 'Contracted-out of SERPS/S2P. If a member left Contracted-out employment the GMP had to be 'revalued' (i.e. increased each year up to State Pension Age) on one of a choice of bases such as fixed rate revaluation (the fixed rate depends on the date of leaving service) or in line with Statutory Orders (in effect in line with National Average Earnings). Changes to the Contracting-out legislation were made from April 1988. Any GMP earned prior to that date did not have to include pension increases after retirement. GMPs earned after that date had to provide increases to the pension in payment in line with RPI capped at 3% each year.
Individual Pension plans		Pension schemes in which an individual has contractual rights to benefits. These include Stakeholder schemes, Retirement Annuity Contracts, Personal Pension Plans and SIPPs.
Individual Protection 2014 and 2016		See Lifetime Allowance
Institute and Faculty of Actuaries	IFoA	Professional body which regulates actuaries who subscribe to its code of conduct.
Internal Transfer		A PSO implemented by the pension claimant being awarded rights as a Pension Credit Member within the existing pension scheme. (see also External Transfer)
Level Annuity		An annuity (policy) under which the income will never increase (and hence will be eroded by inflation over time).
Lifetime Allowance	LTA	Introduced in April 2006 it is the total capital value (as calculated in accordance with regulations) of benefits which an individual can accrue in all UK regulated pension schemes during their lifetime without incurring

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		additional tax charges. The limit was originally £1.5m, which rose over a period of years to £1.8m and has since been reduced in stages to £1m (2017/18). Various protection regimes exist for those who are able to benefit from a previous, higher Lifetime Allowance (Fixed Protection 2012, 2014 and 2016 as well as Individual Protection 2014 and 2016), or, where appropriate, the often more generous limits that applied under earlier legislation before April 2006 (Primary Protection and Enhanced Protection).
Lifetime annuity		An annuity (policy) that will pay an income, normally guaranteed, for the duration of the life of the annuitant(s).
Limited Price Indexation	LPI	A legal requirement to increase pensions in payment under a DB scheme by a minimum amount each year. The minimum is in line with the Consumer Price Index (CPI) or, if lower, 5% (for benefits accrued between April 1997 and April 2005) and 2.5% for benefits accrued after April 2005.
Money Purchase scheme		See Defined Contribution scheme.
Money Purchase Annual Allowance	MPAA	The reduced tax relievable contributions which may be made to any DC scheme after certain Crystallisation events have taken place in one of those schemes. From 6 April 2017 the figure was reduced to £4,000 per annum.
New State Pension		State pension entitlements for those reaching State Pension Age on or after 6 April 2016. Previously referred to as 'the single tier state pension'.
Normal Retirement Age	NRA	The age defined in the pension scheme rules which is normally the earliest age at which DB pension rights can be taken without reduction for early retirement.
Occupational Pension Scheme		Pension scheme related to a particular employment and established under a trust

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		arrangement for the benefit of the scheme members (employees).
Offsetting		The process by which the right to receive a present or future pension benefit is exchanged for present capital within divorce or dissolution proceedings.
Old State Pension		State pension entitlements for those reaching State Pension Age on or before 5 April 2016.
Pension Attachment Order	PAO	Court order (formerly called Earmarking) that redirects all or part of a person's pension benefits to a former spouse or spouse separated by an order of the court.
Pension Claimant		The divorcing spouse seeking pension rights by way of court intervention. The terms 'non-member spouse' or 'transferee' are also used for this party in some contexts.
Pension Commencement Lump Sum	PCLS	A lump sum drawn from a pension scheme (up to 25% of the CE in many cases but can occasionally be greater) which may be drawn down tax free.
Pension Commutation		This relates to DB schemes only and refers to the option usually (but not necessarily) available to the member to exchange (commute) part of their future pension income for a tax free lump sum (PCLS) at retirement.
Pension Compensation Attachment Order	PCAO	The equivalent of a PAO made in relation to a scheme within the PPF.
Pension Compensation Sharing Order	PCSO	The equivalent of a PSO made in relation to a scheme within the PPF.
Pension Credit		The amount of benefit rights that the pension claimant becomes entitled to in the destination pension scheme following a PSO.
Pension Credit Member		A pension claimant who has Pension Credit rights under the Destination Pension Scheme. Sometimes referred to as 'shadow member' of the scheme, particularly when the Pension Credit arose through an Internal Transfer.

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
Pension Debit		The amount of benefit rights given up by a scheme member when a PSO has been made against the scheme.
Pension Freedoms		Flexibility in the way that DC scheme benefits can be taken which mostly derive from the Taxation of Pensions Act 2014.
Pension Holder		The divorcing spouse who holds the pension being considered for court intervention by way of PSO, PAO, Off-setting or otherwise. The terms ‘member spouse’ or ‘scheme member’ or ‘the party with pension rights’ or ‘transferor’ are also used for this party in some contexts.
Pension Protection Fund	PPF	The statutory scheme for administering an Occupational Pension Schemes that is unable to meet its future liabilities where the sponsoring employer has become insolvent.
Pension Provider		The trustees, insurance company, SIPP provider or other institution providing and/or managing the pension fund. The term ‘person responsible for a pension arrangement’ is used in some contexts and defined in s.46(2) of WRPA 1999.
Pension Scheme		A generic term for one of a range of occupational pension rights, personal pension rights, policies, contracts, annuities or state pension rights.
Pension Sharing		Introduced by WRPA 1999 to enable a percentage of the pension rights of one party to be transferred to a pension scheme of their spouse upon divorce by order of the court. Effective for divorce petitions issued on or after 1 December 2000.
Pension Sharing Order	PSO	Court order stating the percentage of the CE of an individual’s pension scheme benefit rights to be transferred from their pension scheme to a Destination Pension Scheme for the benefit of their former spouse.
Pensions on Divorce Expert	PODE	Actuaries or other financial experts who specialise in this field.

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Common pension terms and terms used in this report	**Abbreviation Used in this paper**	**Meaning/Comment**
Personal Pension Scheme		A type of Individual Pension plan which includes SIPPs.
Primary Protection		See Lifetime Allowance
Protected Payment		Where a person's pre 6 April 2016 Additional State Pension entitlement takes their total State Pension entitlement to a figure higher than the single tier base figure as at 6 April 2016 the difference will be designated as a 'protected payment' and this may be subject to a PSO.
Protection (Primary, Enhanced, Fixed and Individual)		There are a variety of forms of protection against the Lifetime Allowance Charge which have been available to allow those who would have been adversely by changes to the LTA rules since they were introduced in 2006 to protect themselves against the charge, either in whole or in part. See Lifetime Allowance.
Purchased Life Annuity	PLA	A non-pension annuity purchased from already taxed personal funds. The income from a PLA is taxed more favourably than that from an annuity purchased with pension savings because the latter will have previously benefited from tax reliefs.
Retail Price Index	RPI	The measure of inflation commonly used by most DB pension schemes prior to 2011 where pensions were fully or partially protected against inflation. Still used by some schemes.
Retirement Annuity Contract or Section 226 policy	RAC (s.226)	Insurance based annuity contract, a type of Individual Pension Plan introduced by Finance Act 1956 Part III for the self-employed and those in non-pensionable employment, subsequently governed by Income and Corporation Taxes Act 1970, section 226 and replaced by Personal Pension Plans in July 1988.
Self Invested Personal Pension	SIPP	A Personal Pension Plan where the pension holder can make their own investment decisions using the full range of investments approved by HMRC.

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
Shadow / Primary membership Shadow membership		A person who is a member of a pension scheme by virtue of a pension credit is referred to as a shadow member, in contrast to the original member, who is referred to as a primary member. See Pension Credit member
Shadow PODE		A shadow PODE is a Pension on Divorce Expert instructed by one party to advise that party on questions to ask the SJE PODE.
Single Joint Expert PODE	SJE PODE	A PODE instructed on a Single Joint Expert basis.
Small pots lump sum		Ability to draw small sums (up to £10,000 in no more than 3 pensions) from pension schemes rather than purchase an annuity. The limit of 3 schemes does not apply to unrelated Occupational Pension schemes.
Small Self-Administered Pension Scheme	SSAS	A form of Occupational Pension Scheme typically set up for key employees or directors of a company with a maximum 11 members typically.
Stakeholder Pension Scheme		A type of Individual Pension Plan that satisfies certain government criteria for a cap on charges, no exit penalties and low minimum contributions. Introduced in April 2001 as a result of the WRPA 1999.
State Earnings Related Pension Scheme	SERPS	Additional State Pension accrued by employees who were not Contracted-out between April 1978 and April 2002.
State Pension Age	SPA	The age at which an individual is entitled to receive their State Pension. The SPA may be subject to ongoing changes.
State Second Pension Scheme	S2P	Additional State Pension accrued by employees who were not Contracted-out between April 2002 and April 2016.
Substitution or Basic State Pension substitution		Where, on divorce, the spouse with the worst National Insurance contribution record substitutes this for the better National Insurance contribution record of the other

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Common pension terms and terms used in this report	Abbreviation Used in this paper	Meaning/Comment
		spouse to increase their Basic State Pension. This is no longer available for claimant ex-spouses who reach State Pension Age after 5.4.2016. For claimant ex-spouses who reached State Pension Age prior to 6.4.2016, it is only the NI contribution record of the other spouse up to 5.4.2016 that can be substituted.
Tapered Annual Allowance		The progressive loss of the Annual Allowance for those whose adjusted income (income + pension contributions) exceeds £150,000. The Annual Allowance is reduced to £10,000 p.a. when earnings exceed £210,000.
The Pensions Advisory Service	TPAS	Guidance service relating to pensions and workplace pensions.
The Pensions Ombudsman	TPO	An independent organisation with legal powers to resolve complaints about pension scheme administration that cannot be resolved by other means. A decision of the Pensions Ombudsman is final, legally binding and enforceable in court. From 1 April 2018 the dispute resolution team at TPAS is to be transferred to TPO providing an end to end dispute resolution service.
Uncrystallised funds pension lump sump	UFPLS	Lump sums paid from uncrystallised funds. Can be used to cash out a DC scheme pot in part or in full without entering drawdown.
Utility discount		A notional adjustment sometimes applied in the pension on divorce offsetting process to reflect the perceived advantages of holding cash now rather than pension benefits later.
Welfare Reform and Pensions Act 1999	WRPA 1999	Act of Parliament introducing Pension Sharing and Stakeholder Pension Schemes

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Appendix 5: List of PAG members and acknowlegements

Mr Justice Francis, Co-Chair of PAG and Chair of Valuation Working Group

HHJ Edward Hess, Co-Chair of PAG and Chair of Expert Working Group

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