



# A Guide to the Treatment of Pensions on Divorce

The Report of the Pension Advisory Group

July 2019

## Executive Summary



© Hilary Woodward (on behalf of The Pension Advisory Group) 2019

This work is licensed under the Creative Commons Attribution-ShareAlike 4.0 International License. To view a copy of this license, visit <http://creativecommons.org/licenses/by-sa/4.0/> or send a letter to Creative Commons, PO Box 1866, Mountain View, CA 94042, USA.

The Report of the Pension Advisory Group is available at

DOI: 10.3927/108542233

URL: <https://www.nuffieldfoundation.org/pensions-divorce-interdisciplinary-working-group>

Any enquiries regarding this publication should be sent to:

Hilary Woodward <[woodwardhd@cardiff.ac.uk](mailto:woodwardhd@cardiff.ac.uk)>

Full Report ISBN 978-0-9576682-5-6

# A Guide to the Treatment of Pensions on Divorce

The Report of the  
Pension Advisory Group

July 2019

## Executive Summary

This is the Executive Summary of the  
Pension Advisory Group Report



# Executive Summary

## Part 1: Introduction and overview

1. The Pension Advisory Group (PAG) is a multi-disciplinary group of professionals specialising in the field of financial remedies and pensions on divorce. The group was formed in June 2017 under the joint chairmanship of Mr Justice Francis and His Honour Judge Edward Hess with the aim of **improving understanding** of the complex area of law relating to pensions on divorce **and enabling more consistent and fairer outcomes**. This good practice guide results from two years of deliberations and widespread consultation by the PAG and seeks to explain the most critical legal, actuarial and practical issues facing practitioners, the judiciary and couples who are divorcing in the area of pensions on divorce in England & Wales.
2. The guide aims to: help legal practitioners, financial experts, and judges dealing with pensions on divorce to understand issues relating to pensions in divorce cases that they may not have been aware of; provide more detailed information to those who would like to dig deeper and signpost readers on to more detailed, authoritative sources elsewhere; help parties, legal practitioners and judges to decide when 'pensions on divorce expert' (called a PODE in this report) input might be necessary to ensure that legal professionals and the clients involved are as well informed as they can be to make fair and appropriate decisions about the pension component of the overall financial settlement on divorce; draw attention to potential pitfalls that may be encountered in these cases; and provide a good practice guide for legal practitioners and experts involved in these cases. We advise on who can or should act as a PODE, what skills need to be certified, and the content of PODE reports. We also provide a comprehensive glossary of terms that parties and professionals are likely to encounter.
3. **Key recommendations** discussed in the body of this report and appendices **include**: best practice in comprehensively **gathering information** on all client's pensions, including state pensions, and benefits such as death benefits, guarantees, and other potentially complicating features; **how to approach valuations** for divorce purposes in 'needs' based and 'sharing' based cases, including timing and source of pension entitlements, apportionment of pensions, cases involving equalisation of income and equalisation of capital approaches; and cases involving **offsetting**. We discuss cases where there are **large age differences** between divorcing parties with 'income gap' issues. We comprehensively discuss complications in valuations and treatment of pensions on divorce where **Defined Benefit pension schemes** are involved and provide guidance as to when it is likely that expert advice and **expert valuations** will be needed. Lawyers, judges and parties need to be aware of **tax issues** and potential interactions with **means tested benefits**. We also cover complications arising with **post-order implementation** and **underfunding** and insolvency issues.

## Part 2: Essential Action Points

4. In summary, the essential stages of a typical case include: gathering information on all of each client's pensions, using Form P for non-State entitlements and completing online requests of the DWP using BR19 and BR20 for State entitlements; comprehensively considering a range of potentially complicating issues (26 such issues are listed); validating the reasonableness of any potential valuations obtained given what is known about employment histories and pension memberships; and serving copies of applications on pension trustees where required. Parties need to evaluate whether a PODE should be instructed, considering these investigations.

A PODE is normally instructed by both parties as a Single Joint Expert (SJE). PODEs need to be able to certify that they have the necessary range of skills; and parties need to ensure compliance with regulations in the instruction of experts. A **template recommended letter of instruction** is provided.

5. Clients will need to be advised about a range of **complicating features**. These include risks relating to types of pension, retirement ages, benefits lost on pension sharing, charges, moving target syndrome, clawbacks, and income gaps. Destination funds for pensions shared need to be considered and IFA advice may need to be sought for the client. Pension annexes and Form D81 must be correctly completed, and it is good practice to set out the pre- and post- pension share financial positions and justification for any offset in or with the D81. Pension administrator approval must be sought prior to submission of paperwork for Pension Attachment Orders and it is good practice to do so for Pension Sharing Orders. Parties need to determine who is going to pay for any pension share. Specific thought needs to be given to the timing of Decree Absolute. Prompt implementation must be ensured, and outcomes reported to any PODE if an order is made following a hearing.
6. Parties need clearly to have understood the **implications of pension freedoms**; complications that arise with **final salary schemes**, unfunded Defined Benefit schemes, closed schemes and AVCs; and the value for divorce purposes of **public sector pensions**.

### Part 3: The first stage: computation of pension assets and methods of division

7. Parties need to evaluate whether the Cash Equivalent (CE) represents appropriate value for divorce purposes, whether other complicating features arise, and whether a PODE needs to be instructed. Methods of settlement include a Pension Attachment Order (PAO – now rare), a Pension Sharing Order (PSO), and offsetting (a division of assets and incomes where parties retain some or all of their pensions in lieu of some other distribution). For PSOs and offsetting cases, the most common approaches are 'equalisation of income' and 'equalisation of capital'. In contested cases division is a matter of judicial discretion in the s25 exercise with guiding principles from case law; however, there is little specific case law on pensions for guidance. **Ignoring the pensions or agreeing to ignore the pensions is not an option.**
8. Whichever approach is taken, the **limitations of CE figures** need to be clearly understood, and where these are a poor reflection of value for the purposes of divorce it is likely that expert valuation and advice will be needed. This applies as a general rule to Defined Benefit (DB) schemes, and to some Defined Contribution (DC) schemes. CEs of DC and DB schemes are not usually comparable, nor are CEs from different DB schemes. Significant complications can also arise with SIPP (Self-Invested Pension Plans) and SSASs (Small Self-Administered Schemes).
9. The **role of the PODE** is to provide valuations and expert opinion that will assist the parties and the court in the discretionary exercise, not to determine which approach or apportionment is appropriate in the case.

## Part 4: Treatment of pensions in 'needs-based and 'sharing' (non-needs) cases contrasted

10. **The vast majority of divorces are needs-based cases** where broadly speaking the assets do not exceed the parties' needs, rather than being governed by the 'sharing' principle, where broadly speaking assets do exceed needs. Note though that the discretionary approach means that these are two strands of the overall search for fairness and are not necessarily always mutually exclusive. In needs-based cases the timing and source of pension assets is not generally a relevant consideration as the court can have resort to any assets, whenever acquired, to ensure the parties' needs are met. In sharing cases the issue of timing, source and apportionment remains live. In needs cases issues of potential for income streams, tax consequences, loss of value on pension sharing, and the detailed consequences of orders may be more important, and often require expert pension evidence.

## Part 5: Pensions: deferred income or capital?

11. Whether a pension should be viewed as deferred income or capital depends on the case, rather than the type of pension. There is no difference in approach between Defined Contribution and Defined Benefit pensions for this purpose. Generally speaking, if it is likely that parties will withdraw **tax free lump sums**, these are seen as **capital**; the **balance of the fund** is viewed as **deferred income**; **pensions in payment** are viewed as an **income** stream. 'Pension freedoms' may affect this analysis, and the ability to withdraw a whole pension subject to tax rules may become pertinent in a particular case.

## Part 6: Dealing with pensions fairly on divorce

12. The overall aim in divorce financial remedy cases is to achieve **fairness between the parties**. This applies to pensions as much as to other assets and income. But **pensions are difficult to value and difficult to divide**, and the assistance of a PODE may be needed whether the case is contested or not. It will often be fair to aim to provide the parties with similar incomes in retirement, but equality may not be the fair result depending on needs, contributions, health, ages, the length of the marriage, or, in non-needs cases, the non-matrimonial nature of the asset.
13. There are **cases where it may be appropriate to share pensions according to their CE and without the assistance of a PODE**. These might include where all pensions are Defined Contribution with no guarantees and the parties are of a similar age; both parties are under 40 and neither is in the uniformed services nor has a significant Defined Benefit scheme; where the governing principle is sharing not needs and pensions are modest in the context of other assets; where combined pension assets by CE are below £100,000; or where the only pension is a non-uniformed service public sector scheme offering internal transfer only and the remedy is pension sharing (rather than offsetting), there are no special complicating features, and there is no significant age difference between the parties.
14. However even with these examples **there may be complicating features that may necessitate PODE input**. These include where guidance is needed as to the level of income likely to be generated by a pension share; where there is a uniformed-service public sector scheme; where the pension assets are likely to exceed the Lifetime Allowance after or as a consequence of a Pension Sharing Order; where there are implicit guarantees for example

Retirement Annuity Contracts or Section 32 Buy-Out policies; where there are older occupational pension schemes with high tax-free allowances; where there is a significant disparity in State Pension entitlement (e.g. £20+ a week); where there is a choice of schemes to be transferred; where combined Defined Benefit pension CEs exceed £100,000; where there are public sector pensions and the parties are considering offsetting, there are complicating features, there is a significant age difference between the parties, or a uniformed service pension is involved; or where one of the parties has a serious medical condition.

15. Where pensions need to be expertly valued, valuations may be undertaken according to potential income value, whether the outcome is determined by sharing or needs principles. It is usual for reports to contain an equalisation of income analysis, which will pick up the quirks of the pension and is usually consistent between experts. There may be cases where the parties or court requests a capital valuation, notably in offsetting cases. There is more scope for variation between experts in these cases. In either case, it is important for **all pensions in the same case** to be valued on a **consistent basis**.
16. In some cases, an equal division is not appropriate for example in a short marriage with no children. Where the parties have worked throughout the marriage and each have their own pensions, no adjustment may be needed. On the other hand, an unequal adjustment might be appropriate in favour of a primary carer whose earning and pension accumulation capacity has been significantly impacted by looking after children.
17. A number of issues arise when considering the correct calculation approach whether for equalisation of incomes or equalisation of

capital. The difficult issue is usually to consider how the pension asset can realistically meet financial needs in the future.

## Part 7: The dominant practice: Pension Offsetting

18. **Offsetting** is the process by which the **right to receive a present or future pension is traded for present capital**. Offsetting may be desired by parties and in some circumstances may be the only feasible option. The result, however, needs to be considered and fair, and it is important that people engaged in the process know the value that they might be losing, retaining, or acquiring. It is possible to use a mixture of offsetting and pension sharing to resolve a case fairly. So far, **negligence claims** against family lawyers in cases involving pensions **overwhelmingly relate to ill-considered offsetting agreements**.
19. As noted already, the CE is often not considered an appropriate value for offsetting purposes in divorce cases, for example for DC funds with guarantees, or for public or private sector DB funds. Parties, advisers and judges also need to understand the interactions with the tax and benefit systems in considering how to value pensions for offsetting agreements. Expert valuations for the purposes of offsetting have historically shown great variation between experts using different methods. We suggest ways of narrowing these differences.
20. Where a PSO is evaluated as either bad value for money or destructive of value such that offsetting should be considered, or offsetting is being considered for some other reason, thought needs to be given to whether the pension value for offset purposes is the value of pension that could have been surrendered, or the loss of value of pension that could have been acquired. These lead to different valuations. The usual approach is to evaluate the value to the pension holder; valuing the loss



of pension that could have been acquired is especially complex. PODEs may be required to present the figures for competing approaches where the circumstances of the case suggest this.

21. There are three **options for considering the value of pensions for offsetting purposes**: the CE (often not appropriate); a figure based on calculations for equality of income or capital; a figure based on the value of the pension holder's retained present or future benefits in the absence of a pension share. The third option is likely to be the fairest in most cases. There are a few ways of approaching this valuation: (a) the Defined Contribution Fund Equivalent (DCFE); (b) the realisable value; (c) the fund account value or cashflow modelling (making assumptions about risk); (d) an actuarial value; (e) a value based on amortising the fund down to a zero balance at median life expectancy. Options (a), (b) and (d) are likely to be the most appropriate in most cases. PODEs need to state the range of acceptable opinions.
22. **Adjustments to values based on the likely tax** that the pension holder would pay **might be between 15% and 30%** depending on circumstances.
23. So-called **adjustments for 'utility' will often not be appropriate**; where justified in a particular case, a range of 0% - 25% might be considered. This is a matter for the parties to decide, or for judicial discretion in contested cases, and not for PODEs to decide.
24. Good practice requires that the pre- and post-implementation income, capital and pension positions of the parties be stated on or with **Form D81**, together with the nature of any expert advice taken in assessing pension value and an explanation of how the offset was arrived at. The judge will need to be satisfied that the settlement arrived at is fair.

## Part 8: The impact of pension freedoms

25. Since 2015, **pension freedoms have enabled people to access their pension funds**, subject to tax, from age 55, and this increased freedom also applies to recipients of PSOs. Pension freedom flexibility might also be realised by a spouse younger than 55 sharing a pension with a spouse older than 55 to create liquidity. However, there are many issues to be aware of. Flexi-access drawdown has become an option, but, while flexible, requires the holder to accept investment return risk, interest rate risk, sequencing risk, mortality drag, longevity risk, and the inability to provide secure spousal pensions. Uncrystallised funds pension lump sums might be an option for relatively small funds, or where cashing in the whole or a series of lump sums with limited flexibility is appropriate. Advisers need to be aware of the **Money Purchase Annual Allowance** so as not to inadvertently prejudice the parties if further contributions are to be made. This is a mechanism to prevent people cashing in their pension and reinvesting in a pension to gain tax advantages. The MPAA is triggered by taking any income under flexi-access drawdown, taking an uncrystallised funds pension lump sum, or taking income from capped drawdown in excess of the cap and triggering flexi-access drawdown.

## Part 9: Taxation of pension benefits on divorce

26. This complex subject is beyond the scope of this report. However, practitioners are here alerted to the potential to trigger the Money Purchase Annual Allowance which could significantly impact on the ability to rebuild a pension pot and issues with the **Lifetime Allowance**. The Lifetime Allowance is designed to restrict the maximum amount that people can accrue in pensions but people with prior accrued pensions might have protected their privileged status through allowed mechanisms. There are many issues to be aware of with the Lifetime Allowance, including that a pension share might lead to loss of protected status and tax charges; but on the other hand, a PSO might enable the parties to utilise two sets of Lifetime Allowances instead of one. The value of pension benefits for testing against the Lifetime Allowance is *not always the same* as the CE value.

## Part 10: Age differential and 'income gap' syndrome

27. An **'income gap'** results when there is an **age differential** such that after a pension share, **one person is in receipt of their pension and the other is not**, possibly for many years; or where one spouse being in a short-service pension scheme such as the police or military, or for reasons of ill-health, can access their pension early whereas the other can not. The pension holder's income will be reduced during those years by the pension share with no immediate benefit for the pension claimant, while the pension claimant (and any dependent children) may need financial support during those years. Further, if the pension claimant begins to draw the pension early under pension freedom rules, they may not have sufficient income later in life. If the claimant spouse becomes a 'shadow member' in the same DB scheme as the pension holder, the benefits to each may
- not be the same; if the spouse was required to take a pension credit to another scheme from a DB scheme, then the new scheme is likely to be substantially less certain in providing a future income stream. Lifetime Allowance protection may be needed for the claimant spouse.
28. There are six ways that some of these **problems might be mitigated**, some of which require a high level of co-operation between the parties: a return to work by one or both parties; reverse pension sharing to create liquidity (though with tax consequences); maximising pension benefits by supplemental payments (including to State Pensions); deferring divorce; adjourning the application for a PSO (with concomitant risks); a deferred PSO (arguably technically possible but not necessarily advisable).

## Part 11: State pensions on divorce

29. **State Pensions are valuable assets in divorce and must not be ignored.** Both parties need to obtain full State Pension information. Components may include Old State Pension, Basic State Pension, Additional State Pension (which can be shared by a PSO and could be valued in excess of £100k), Graduated Retirement Benefit, New State Pension, and protected payments under transitional arrangements. Protected payments can also be shared under a PSO.
30. In lower and some middle income cases, interaction of a PSO with means tested benefits in retirement may be an issue, and if potentially material, specialist advice may be required.

## Part 12: Some issues arising in valuing pensions for the purposes of divorce

31. Whether pensions should be apportioned for the period of the relationship is a matter for judicial discretion in contested cases; as a general rule **in 'needs cases' apportionment is rarely appropriate**. There are three potential methods – the deferred pension method, the CE method, and the straight-line method. Sufficient data is not always available for the first two; in some cases the straight-line method is the only practical approach.
32. Where there is a clearly diagnosed medical condition with a substantial probability of impaired life expectancy, this should be reflected in the calculations; more minor or less obvious conditions where there is the possibility of change (smoking, drinking, weight) should not normally be reflected in the calculations. PODEs should clearly state assumptions about health and the effect of any assumptions on calculations.
33. Which pensions to share first may make a material difference to outcomes, and this is often not straightforward. **Where there is a choice of pensions, expert advice is likely to be needed**.
34. Lifetime Allowance issues are likely to affect more cases in future given reductions in allowances.

## Part 13: Pensions where an application has been made to vary the original order

35. The breadth of judicial discretion is such that it is difficult to advise clients with any certainty of the outcome of variation applications. For petitions issued after 1 December 2000, for example, a clean break could be achieved by substituting a pension share for a periodical payments order. As a general rule, **a PSO cannot be made against the same pension from the same marriage**, but can be made against another pension from the same marriage. However, upon a capitalisation application a PSO might arguably be made against the same pension from the same marriage which has previously been subject to a PSO. It is possible to discharge a PAO and substitute a PSO on a variation application. **Pensions must not be viewed in isolation** on variation applications but must be considered alongside all other factors that the court is required to consider.

## Part 14: Pensions and international issues

36. The location of a pension may be important in deciding the most appropriate jurisdiction for proceedings.
37. Anti-alienation laws in the UK preventing transfers out of a pension do not exist in all jurisdictions, and the law and possibilities in each relevant jurisdiction will need to be investigated. It is **not possible** to make a PAO or PSO against **a foreign pension**. Various complex strategies may be required to effect any division. With collaboration between the parties, it may be possible to transfer a foreign pension to England to effect a PSO.

38. English pension providers **neither recognise nor implement** PSOs made in **foreign courts**. Orders can only be made in English courts if jurisdiction exists to make these. At the time of writing this report, it is possible to found jurisdiction if conditions are met under s15(1A) of the Matrimonial and Family Proceedings Act 1984 and the EU Maintenance Regulation, Article 7. The future of this jurisdictional pathway is uncertain with the UK's withdrawal from the EU.

## Appendices

39. This report contains **22 Appendices** where issues are expanded and technical details explored. These include a **comprehensive glossary**, appendices concerned with procedures and practice, issues with implementation, complexities of certain types of pension and where insolvency is an issue, data and content of PODE reports, assumptions behind PODE reports and seeking a consistent basis of valuation, the range of agreed acceptable methods for calculations, apportionment of final salary schemes, and issues relating to fees and costs. We also set out a possible future approach to pension valuation based on *Ogden*- style tables, and then detail a range of issues beyond our remit for the attention of responsible bodies. We hope that our remarks and recommendations will be helpful in reforming the law and practice in this area. [Appendix W](#) contains our detailed acknowledgements to the numerous people and bodies who have contributed to this report, and [Appendix X](#) a range of other useful resources.

## Conclusion

40. This report has been written with the aim of improving knowledge, understanding, and good practice in the area of pensions on divorce. The PAG has deliberated at length and consulted widely to provide a consensus view across the disciplines involved in this field as to best practice in valuing and treating pensions on divorce. **We hope to make outcomes more predictable and consistent** for divorcing couples, their advisers, and judges across England and Wales who deal with these issues daily.

# Acknowledgements

The Pension Advisory Group was set up in mutual recognition of the urgent need for interdisciplinary discussion between lawyers, actuaries and financial advisers to achieve better common understanding and consistency in cases involving pensions on divorce.

This resulting report reflects collaboration between a great many people who have given their time willingly and without charge over two years to the Pension Advisory Group, aiming to improve inter-professional working, provide a consensus on the law and improve practice, and, most importantly, improve outcomes for individuals involved in the resolution of pensions issues on divorce. Contributors include the members of the Pension Advisory Group, consultees, focus group and survey participants, and the many people who have fed into this report more informally at events, workshops and conferences. Too numerous to include here, we have listed contributors at Appendix W, with huge gratitude for their commitment to this project.

We are very grateful to the President of the Family Division and the Family Justice Council for their support of this project.

We thank the Nuffield Foundation for their financial support, primarily in covering the time of two of our academic members on this project and financing other general project expenses. The Nuffield Foundation is an independent charitable trust with a mission to advance social well-being. It funds research that informs social policy, primarily in Education, Welfare, and Justice. It also funds student programmes that provide opportunities for young people to develop skills in quantitative and qualitative methods. The Nuffield Foundation is the founder and co-funder of the Nuffield Council on Bioethics and the Ada Lovelace Institute. The Foundation has contributed towards the funding of this project, but the views expressed are those of the authors and not necessarily the Foundation. Visit [www.nuffieldfoundation.org](http://www.nuffieldfoundation.org).



We are also grateful to the Nuffield Foundation for hosting the project website at: <http://www.nuffieldfoundation.org/pensions-divorce-interdisciplinary-working-group>.

We gratefully thank Brewin Dolphin PLC, wealth managers, for their support in hosting focus groups and events, David Chaplin and Helen Lacey at Bath Publishing Ltd for their kind assistance with proof-reading the report, and the University of Manchester for funding the publication of the report.

We would also like to thank the Cardiff School of Law and Politics, together with the University of Manchester and Cambridge University, under whose auspices this project has been conducted.

