UK final salary pension transfers for Expats in Asia

AIMS Pensions and Investments

AIMS, ensuring excellence

Welcome to AIMS

AIMS Pensions and Investments is a Thai based advice business which aims to guide clients through every stage of their financial lives. We are focused on making a difference for our clients.

Paul Wyatt
Managing Director

We set out to provide the highest levels of customer service working and growing through referrals from clients who are happy with our service.

Making sense of final salary pension transfers

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How AIMS can help

AIMS has expertise in all aspects of pension investment and planning. Because we analyse your pension assets alongside your future income needs, your financial ambitions and those of your family, we can provide solutions tailor-made to your unique needs.

Whatever your circumstances, we can help ensure that you make the most of your hard-earned pension savings

This can include:

- Locating and valuing all of your pension savings;
- Analysing if a pension transfer would be in your best interests based on the latest transfer value, your attitude to risk and your other retirement assets;
- Creating and managing modern income drawdown solutions that are individually tailored to your unique circumstances; and
- Consolidating your existing pension arrangements into one cost-effective portfolio that's invested to optimise returns within your risk tolerances

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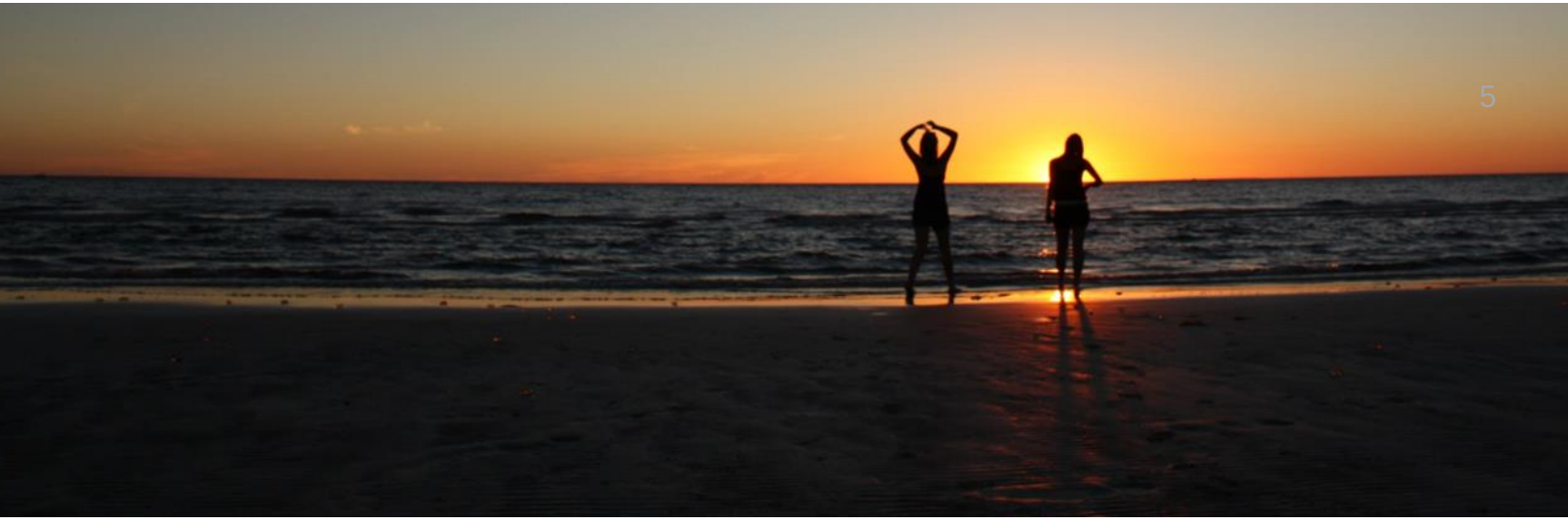


2017: The year of the pension transfer?

A combination of factors has led to record levels of pension transfers in the UK.

Chief among these is the fact that the transfer values being offered to those 6.75 million or so Britons lucky enough to have deferred final salary pensions have never been higher.

While the sudden hike in transfer values has, quite rightly, triggered the review of many final salary arrangements there are also other factors at work.

Among these is a renewed push by final salary schemes to remind their members that they can consider transfers (and so get them off their books for good) and the recent arrival of the so-called 'pension freedoms'.

Cry freedom

Until very recently, 'gold-plated' final salary pension scheme benefits were nearly always considered the best option compared to the alternatives. Not least because the risk (or cost) of providing an index-linked income for life rests firmly with your former employer.

But with the introduction of the new pension freedoms in April of 2015, the alternatives suddenly got a whole lot better.

2017: The year of the pension transfer?

Better pension options

Since April 2015, anyone over the age of 55 can access a money purchase pension whenever they like and take whatever level of income or cash lump sums they choose (subject to the tax rules).

Alongside the added flexibility and investment choice of transferring to the money purchase regime, the new pension freedoms also abolished the 55% 'death tax'. This allows pension wealth to pass more smoothly between generations than ever before.

This has suddenly made the personal pension regime one of the most tax-efficient ways in which to pass wealth down through your family, as pension assets have always been free of inheritance tax.

Taking control

Importantly, this change means that a final salary pension that will be lost when you die can instead be transformed into a major financial asset that can provide both income and tax-efficient lump sums in retirement and still be passed on to your loved ones, free of inheritance tax, when you die.

Naturally, the attractions of such freedoms have exerted a strong pull on those with final salary scheme pensions.

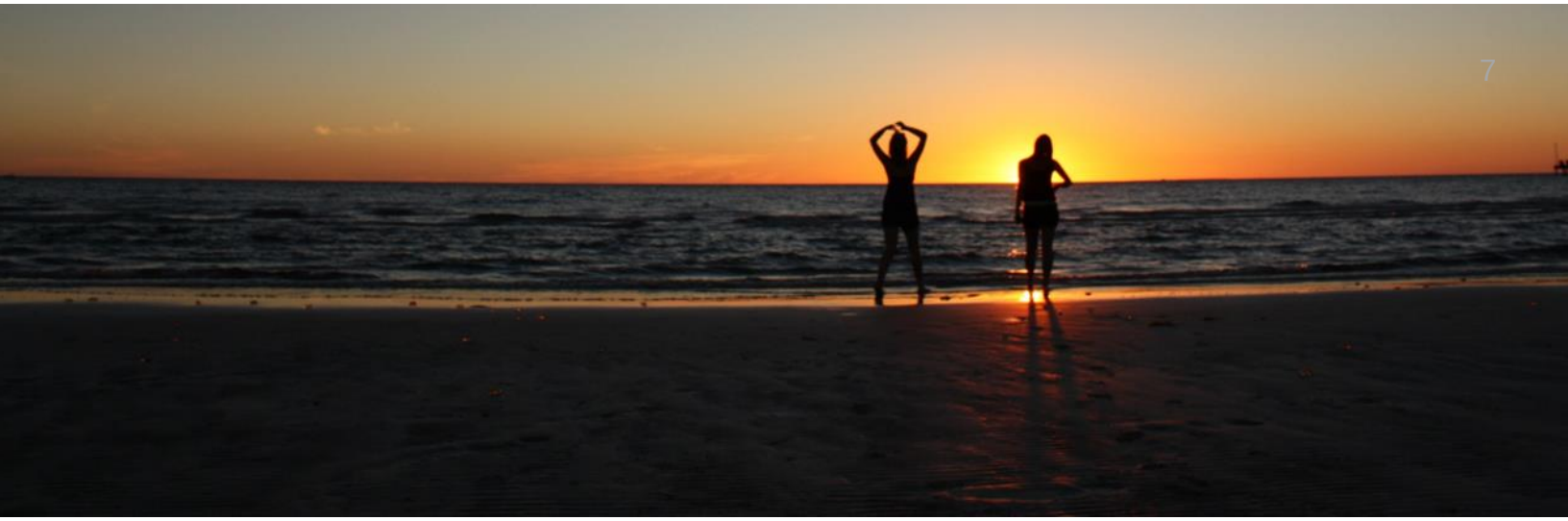
The fear factor

Meanwhile, many Britons are, understandably, anxious about the security of their hard-earned final salary pensions.

The recent scheme collapses at British Steel and British Home Store (BHS) once again highlighted how final salary pensions can become hostages to fortune, prompting a good many Britons to take a closer look at the security of their own pensions.

Ask a professional…

"Your pension arrangements are as individual as you are. Talk to an AIMS adviser about whether a pension transfer is right for you."



Why transfer values are the highest they've ever been

The record low yield on UK government bonds has translated into a bonanza for final salary pension scheme members

If you didn't already know, we're currently witnessing the death throes of the traditional lifetime annuity.

Thanks to the combination of our ever-longer life spans and the record low yields on government bonds, UK annuity rates are now at their lowest levels of all time.

This is crucial as the same factors that drive annuity prices also drive the valuation of final salary benefits. This means that the cost to your old employer of providing you with a final salary pension for life has never been higher.

As a result, the cash equivalent transfer values (CETV) now being offered by final salary schemes as an alternative are also now at an all-time high.

On the rise…

Transfer values reached new peaks in 2016 when the already meagre yield on UK government bonds halved to below 1% (for the first time in history) following June's shock Brexit decision.

When the Bank of England responded in August by cutting interest rates to just 0.25% (pushing down government bond yields still further) transfer values rose once again, only to soften slightly in the last quarter of the year as government bonds yields staged a modest recovery.

Why transfer values are the highest they've ever been

Multiple reasons to transfer

Even so, at the start of 2017 we were still seeing clients with improvements of 25% or more in their transfer values over the previous year.

Historically, the industry 'multiple' tended to float at around 20 (meaning a £10,000pa pension would equate to a transfer value of around £200,000). However, multiples in the 30s, 40s and even 50s are now much more standard.

But there's little consistency between company schemes, even those in the same industry.

A good example was the difference in multiples being offered by BT's final salary scheme and that of Cable & Wireless at the start of 2017. While the former offered a muted multiple of 20, the latter was offering a multiple of above 50.

This means that anyone with a £10,000pa Cable & Wireless pension could cash it in for a transfer value well in excess of £500,000!

In good company

A high transfer value naturally reduces the investment risk that you take on when you transfer.

In 2016, a record number of final salary scheme members decided that the rewards clearly outweighed the risks and elected to transfer their final salary benefits to a personal pension or SIPP.

Among them were numerous high-profile pension savers including former pensions minister Baroness Altmann and the chief economic commentator for the *Financial Times*, Martin Wolf.

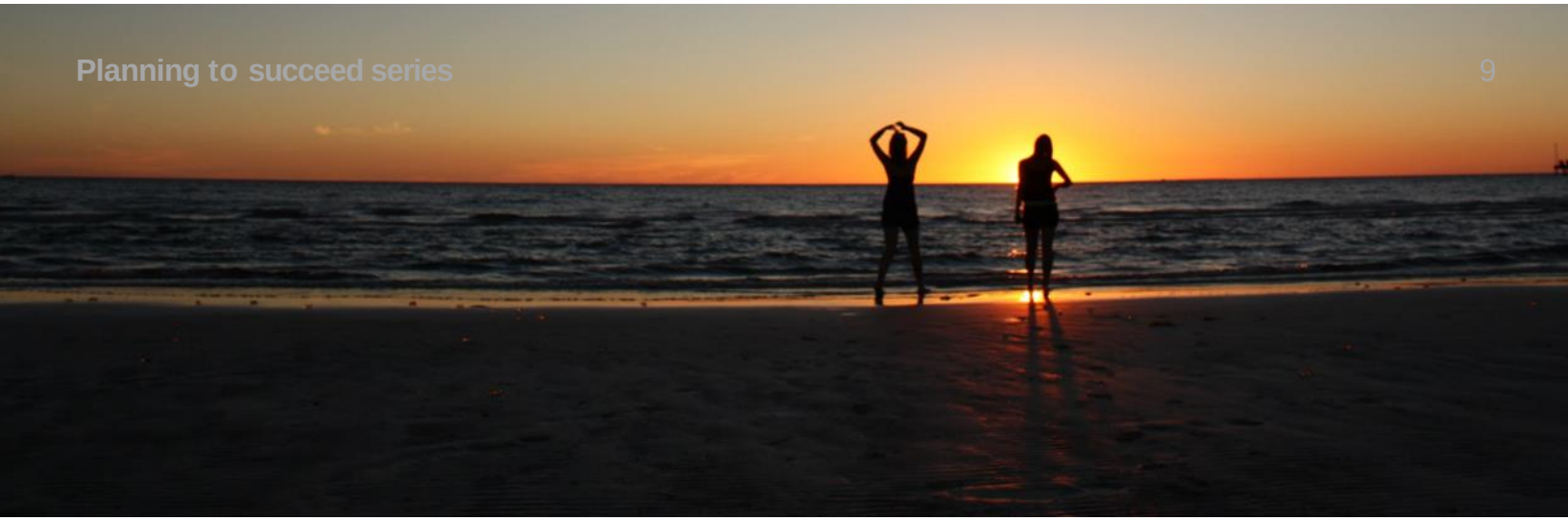
In late 2016, Baroness Altmann revealed to the *FT* that she had decided to cash in two of her (non-index linked) final salary pensions from the 1980s after the transfer values on both had at least doubled over the previous two years.

Making the most of pension transfers: 2016 saw both Baroness Altmann (former pensions minister) and Martin Wolf (chief economic commentator for the *FT*) transfer their final salary pensions

Meanwhile, Martin Wolf, writing for the paper, expressed his view that, "At current ultra-low interest rates, the transfer value of a defined benefit pension has become significantly overvalued. It seems sensible to take advantage of that fact."

He admitted that it could be the wrong decision but that, in his circumstances, he "would have to live to be close to a hundred and the pre-tax real returns on investments would have to be zero – or less – over decades.

"If the latter were to be true," he said, "capitalism would truly be dead."



The benefits of a pension transfer

There are a number of good reasons why a pension transfer might make good sense for you

1 Taking advantage of today's record transfer values

Thanks to the fact that government bond (gilt) yields are at record lows following the financial crash and the more recent Brexit, the transfer values now being offered by final salary schemes have reached record highs. In many cases, transfer values are more than 200% higher than they were a few years ago.

While there's probably no such thing as an 'average' transfer value, most final salary pension scheme members will have seen the likely value of their pension transfer more or less double over the two years to the end of 2016.

Although the decision to relinquish a guaranteed income for life shouldn't be made lightly, with transfer values now at such high levels, great numbers of final salary scheme members are deciding that the price is right for them to 'sell up'. This explains the current 'boom' in pension transfers.

2 The ability to pass on your pension wealth – not see it lost when you die

Remember that under a final salary scheme, the value of all your pension savings will be lost when you (and possibly your spouse) die.

The benefits of a pension transfer

By contrast, a pension transfer 'monetises' your final salary benefits by translating them into a notional cash value.

When you transfer this to a personal pension arrangement your pension savings become an asset that can usually be passed onto your loved ones and their descendants free of income tax (if you die before age 75) AND free of any inheritance tax.

3 Consolidating your existing pension arrangements into one streamlined portfolio

There are a number of advantages to consolidating all of your different pension arrangements into one low-cost wrapper. Not least are the opportunities to reduce charges and greatly improve investment choice.

Creating one large portfolio also increases the chances of generating a higher level of income than if your pension was divided across several smaller pots.

Perhaps most importantly, consolidating your pensions puts all of your retirement savings where you can see them.

4 The chance to seriously reduce your tax bills when you retire

Many members of the UK's 6,000 or so final salary schemes have accrued benefits that are well in excess of the current lifetime allowance (LTA) of £1 million. Those in this position who are drawing an income of more than £50,000 pa will find themselves subject to LTA charges of 55% tax on any lump sums and 25% on any income in excess of the LTA, plus income tax (40%/45%), deducted at source.

However, a transfer to a money purchase arrangement allows such LTA tax charges to be deferred to age 75.

There won't be any additional tax to pay so long as the value of the benefits taken remains below the LTA limits up to age 75. Only when the value taken exceeds the LTA limit will a tax charge be made.

Given that the pension pot has grown in a tax-efficient environment for the intervening years, this can seriously reduce the total value that's eventually lost to tax.

The benefits of a pension transfer

Similarly, a transfer from a final salary arrangement will deliver far greater flexibility when it comes to drawing tax-free lump sums and income.

And, by managing your income to remain below specific income tax bands, you can reduce your tax bills.

5 The opportunity to benefit from stock market growth in the decades after you retire

With a final salary pension, once you've selected your retirement date and received your tax-free lump sum, the pension income you subsequently receive will (at best) only ever grow in line with inflation.

And, naturally, you'll have no opportunity to either vary the income you receive or to take any additional lump sums.

6 The flexibility of the pension freedoms and access from age 55

Moving to a personal pension arrangement delivers far greater income flexibility in retirement, along with numerous options for drawing down lump sums, all of which is useful for coping with life's ups and downs.

It can also help to significantly reduce the tax that you might otherwise pay if you received a set level of income from your final salary pension.

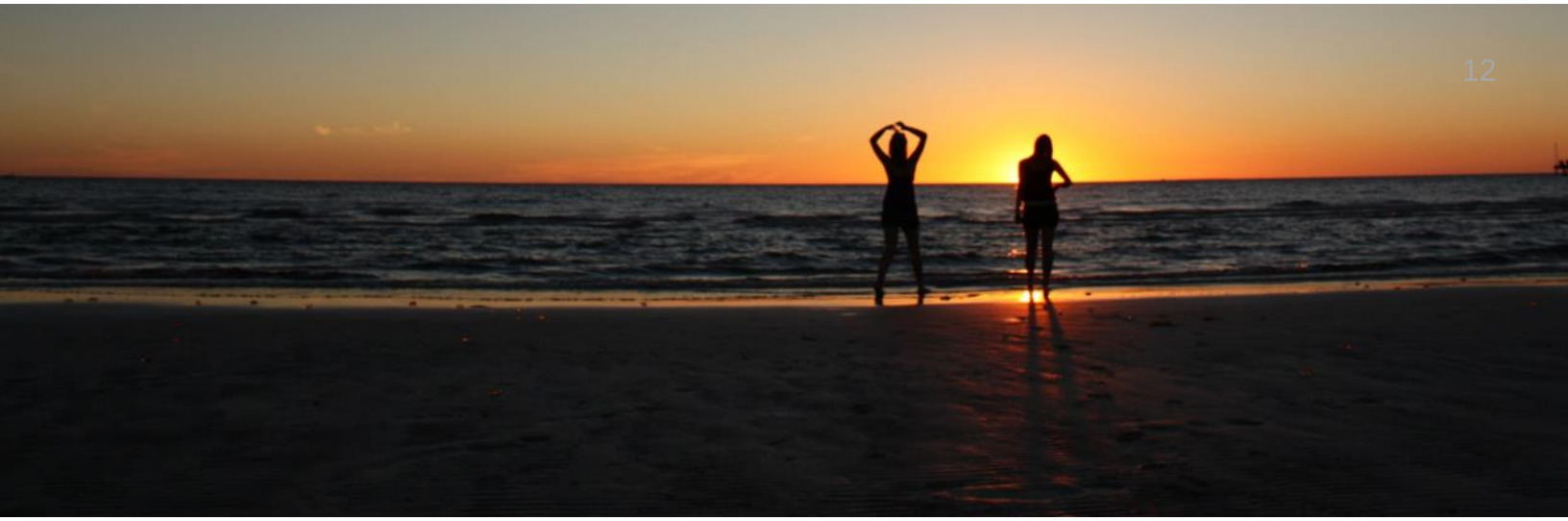
7 Doubts as to your longevity

As the income paid by a final salary pension is priced on average life expectancy, those expecting a shorter innings will be paying too much for the income they're likely to receive!

Consequently, transfers have a particular appeal to those in poor health.

In other words, because a transfer converts your pension benefits into a cash value based upon normal life expectancy, all else being equal, an ill-health transfer should be worth more to your family than your previous scheme benefits.

This means that arriving at an informed decision about whether a transfer makes sense for you requires you to take a view on your own life expectancy.



The benefits of a pension transfer

8 Doubts as to the health of your previous employers

Don't forget that the great majority of defined benefit pensions are significantly underfunded.

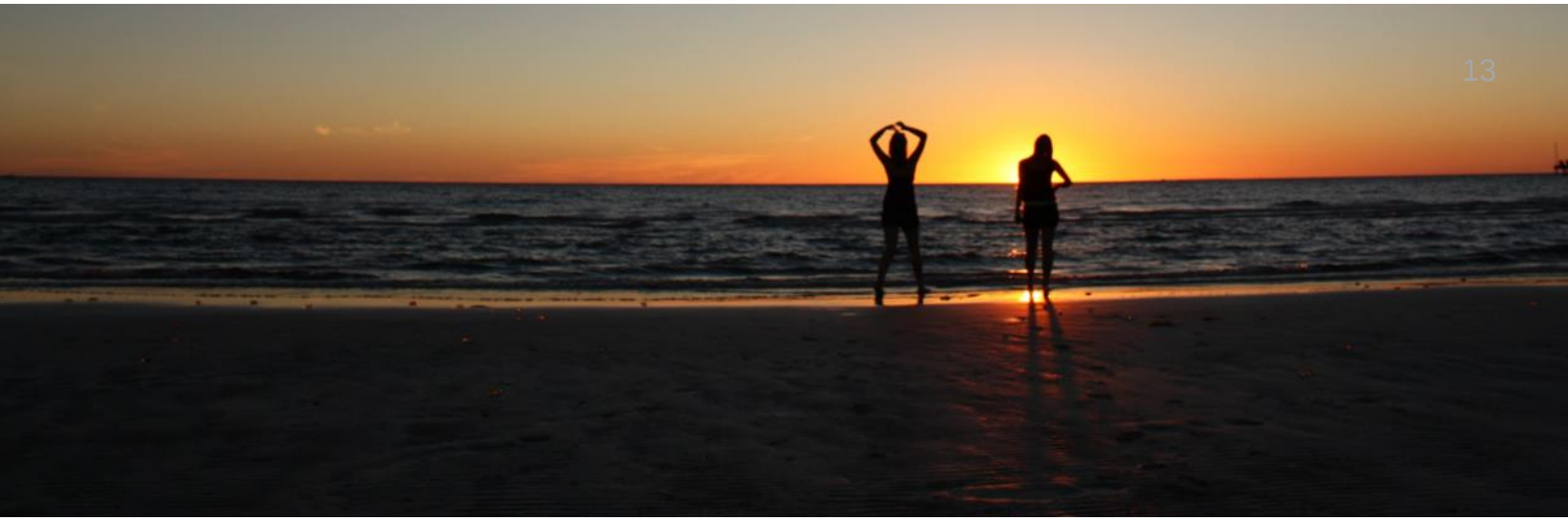
The precarious position of the UK's 6,000 or so private sector final salary schemes was illustrated in August of 2016 when the Bank of England's 0.25% rate cut added an estimated £100 billion to their existing £610 billion of deficits over the course of a single month.

If your former employer fails, you could find your pension is in the hands of the Pensions Protection Fund. From 1 April 2017, someone aged 65 will receive 90% of their benefits capped at £38,505.61 (ie £34,655.05) per year, while future increases will also be reduced.

This could represent a major loss of benefits for those who enjoyed relatively high earnings during their working life.

Ask a professional…

"You can request a transfer value yourself. But beware. Valuations are only guaranteed for three months, so the clock suddenly starts ticking. A pension transfer is one of the most important and complex financial decisions you'll ever make, so don't try to make it in a rush."



How the new 'pension freedoms' changed the game

Under the new rules that were introduced in April 2015, everyone over the age of 55 with a personal pension can access it as they wish – regardless of their total pension wealth

This means that most investors aged 55 or over now have complete freedom to take whatever level of income or cash lump sums they choose (subject to the tax rules).

Savers who transfer to personal pensions now have the freedom to:

- Take their whole fund as cash with 25% paid tax free and the remainder taxed as income;
- Take smaller lump sums whenever they please, with 25% tax free and the remainder taxed as income;
- Take up to 25% tax free and use the remainder to generate a regular taxable income, through drawdown or an annuity, either immediately or later down the line.

How the new ‘pension freedoms’ changed the game

Other important changes

One of the most far-reaching changes introduced by the pension freedoms was the abolition of the 55% ‘death tax’ on pension assets that are passed to your beneficiaries.

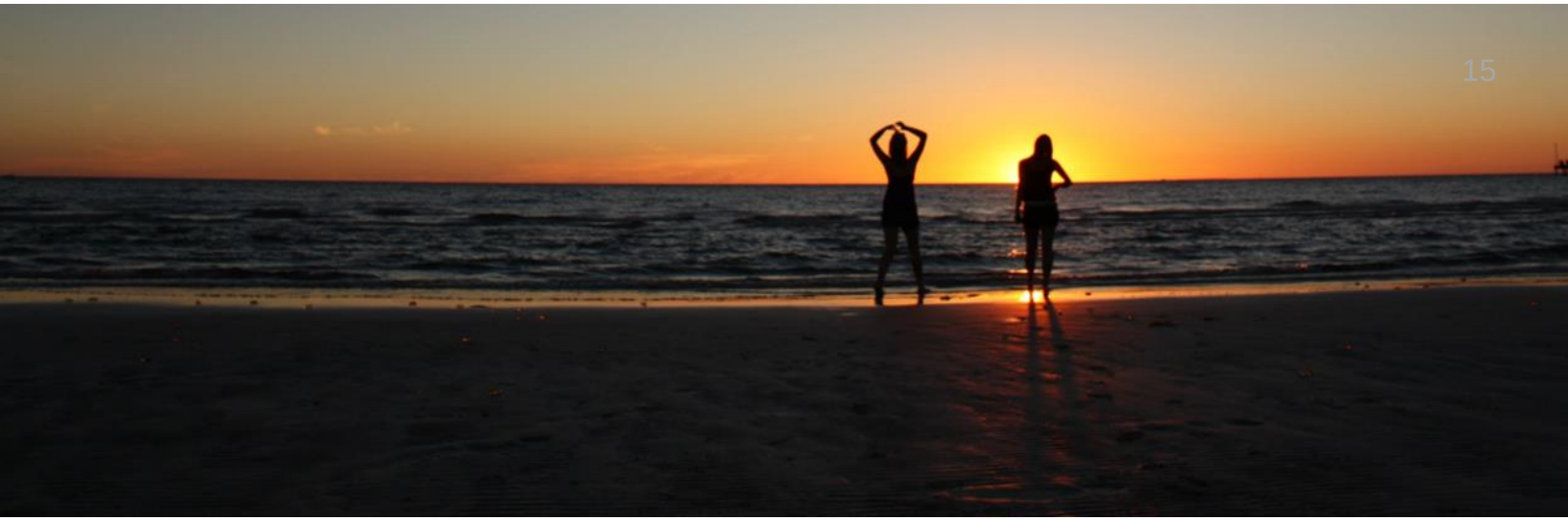
As pensions have always been free of inheritance tax liability (because they’re held in trust outside of your estate) the removal of these charges means that personal pensions are now one of the most tax-efficient ways in which to pass wealth from one generation to the next.

Don’t be caught out

Elsewhere, the pension freedom rules also introduced a new £10,000 per annum contribution allowance for those who’d already drawn taxable benefits from their pension.

The new measure, called the money purchase annual allowance (MPAA), was intended to prevent the risk of ‘pension recycling’ – namely the reinvestment of pension money in order to claim a second helping of tax relief.

Importantly, from the start of the 2017 tax year, the MPAA was due to be reduced to just £4,000 pa (gross). However, the onset of a snap general election has left the issue in limbo until a new government takes power.



Final salary transfers: what are the risks?

Although a transfer enables you to take advantage of the new pension freedoms and to create and manage your own pension 'pot' that can be passed to your beneficiaries, it's important to appreciate what you'll be giving up in return

If you choose to carry out a transfer of your final salary pension benefits, you'll lose:

1 Any guarantee as to the level of income you receive in retirement

A transfer passes the investment risk that accompanies the provision of a lifetime income from your former employer to you (and you can't transfer back again should you change your mind).

Outside of a final salary pension, the only way to effectively guarantee an income for yourself in retirement is by buying an annuity. However, with annuity rates now at all-time lows, an annuity will only deliver a fraction of the income that you would receive if you remained in your former scheme.

A transfer means taking on investment risk as you'll need to invest your pension pot in a range of different 'risk assets' such as equities and bonds.

That said, the level of today's transfer values means that only very modest levels of investment performance might be required in order for your new portfolio to deliver at least the same level of income as you would have received in your old pension.

But remember, there are no guarantees whenever investment performance is required.

Final salary transfers: what are the risks?

2 Any guarantee that you won't run out of money in retirement

Ultimately, there are no guarantees that your new pension portfolio will generate a higher level of income than the one your previous scheme was offering.

Hand in hand with this is the risk that if you fail to manage your withdrawals correctly, you could exhaust your pension pot before you reach the end of your retirement. There's no such risk with a final salary arrangement.

That's why you'll need to find an adviser who can produce a 'cashflow model' which will illustrate just how well your new pension pot will need to perform in order to at least match the level of income you would have received from your final salary pension.

Ask a professional…

"Once we receive an up-to-date transfer value we produce a detailed analysis which shows how well your new pension pot will need to perform to at least match the income from your former arrangement.

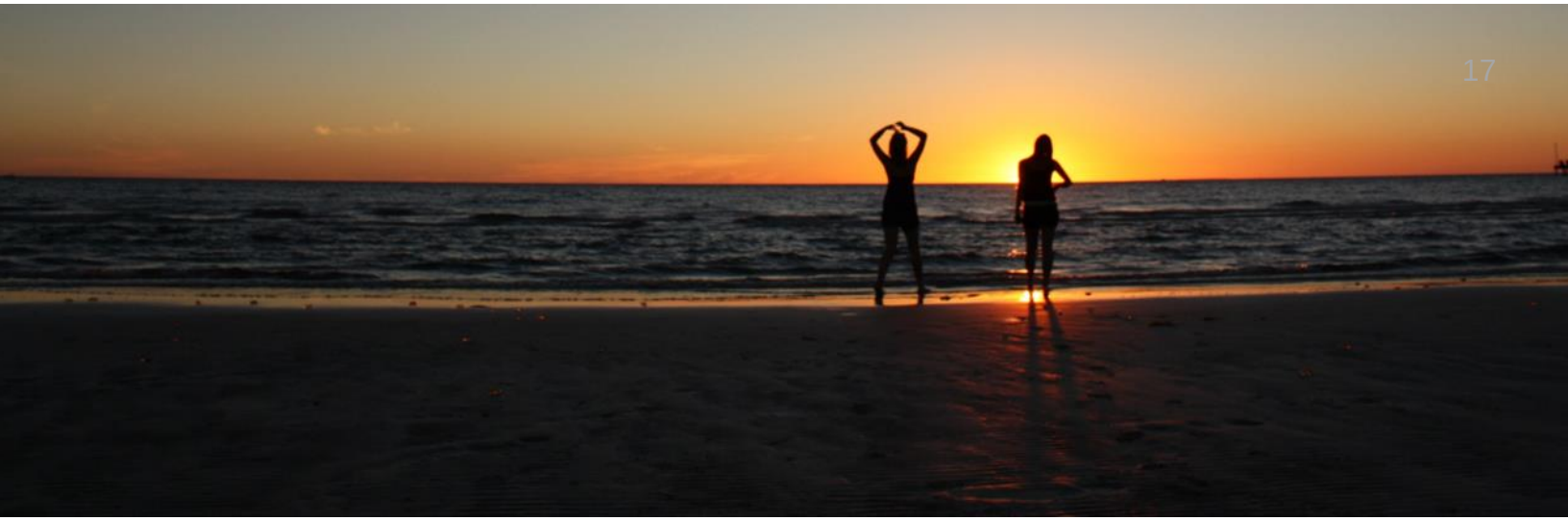
"This is central to making an informed decision about whether a transfer is right for you."

3 Any guaranteed widow's pension

Typically final salary schemes will offer a reduced (50%) widow's pension to your spouse once you die.

But this is actually an extremely expensive way to provide an income for your partner as it's taxable. By contrast, a widow's drawdown or annuity pension is now tax free (if you die before age 75).

Remember, under a final salary scheme, the value of all your pension savings will be lost once you and your spouse have died.



The need for professional advice

At AIMS Pensions and Investments, we often deal with clients who have numerous existing pension plans including both money purchase and final salary arrangements

By building up a detailed picture of each client's unique financial ambitions and analysing each pension contract individually, we can advise our clients on which pensions might be worth transferring and which ones should stay where they are.

But pension transfers are a complex and nuanced process. This explains why it's now a legal requirement to seek professional financial advice (which carries a fee) on any pension transfers from a final salary pension scheme worth over £30,000.

Remember, both your existing scheme and your new pension provider will require evidence that you've received this advice before they'll authorise a transfer.

The first step to finding out whether the combination of record transfer values and the new pension freedoms mean that a pension transfer is right for you is to talk to a qualified pension adviser.

Ask a professional…

"At AIMS Pensions and Investments, we analyse every aspect of your finances to make sure that a move will improve your circumstances; we'll never recommend on a transfer unless we're confident that it's in your best interests."

If you're one of the many expat Britons in Asia with a deferred final salary pension, the best way to find out whether your old scheme is offering a good deal on a potential transfer is to contact us today

The information contained in this guide does not constitute advice and AIMS Pensions and Investments accepts no liability for any use you may choose to make of it. We always recommend that readers seek professional advice before taking any major financial decision.

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