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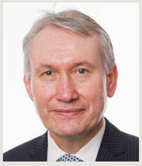
New pension flexibilities: the first few months

Three months on from the start of the new pension freedoms and, despite all the fanfare and media attention, it appears many workers still have **limited knowledge of the pension reforms**.

That's not to say there has not been much interest; the ABI say pension providers received over a million calls about the new freedoms in the first month.

People don't seem to be buying sports cars



PSIT opinion by:
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Initial reports from insurers and master trusts suggest that after an initial surge of enquiries, the feared **mass encashment of defined contribution (DC) pots hasn't happened**. If anything, policyholders and members are taking a more measured approached as the **tax consequences sink in**. Could this be as a result of the free guidance available from the government's Pension Wise service?

Concerns that allowing DC members to withdraw funds from their pension at any time over 55 would promote irresponsible spending thus far appear unproven. However, the Treasury's tax take from people cashing in pensions is now expected to be significantly higher than the government's original forecast. Remember, though, this **'windfall' for the Chancellor** simply brings forward tax revenues and consumer spending that would otherwise have been paid out over the years and decades to come.

Another factor hampering access to the new pension freedoms is the stance of some insurers and schemes not to offer members the new flexibilities. This has been condemned in the media but, in defence, the pensions industry was given little time to prepare and flexible access and drawdown pose an administrative complication and additional costs that need to be properly implemented. That said, members do have the right to transfer to an alternative arrangement that offers the flexibilities, although there may be a cost on transfer. As the market develops, I'm sure **choice and costs will improve.**

What about DB members?

Similarly, the much anticipated rush of defined benefit (DB) members seeking to convert their pension entitlement into a DC pot in order to access the new freedoms has also not yet materialised. Most commentators are united in the opinion that such a move would be against a member's best interest in view of the increased risks and loss of guarantees.

Whilst we agree it would not be right for everybody, there may be situations where **reshaping benefits** by using the new flexibilities **may be beneficial**.

Given the different tax treatment on death in a DC arrangement, in certain situations there may be a **compelling case to transfer.**

Of course, the importance of taking advice from an independent, Financial Conduct Authority (FCA) regulated professional is key. For transfer values in excess of £30,000, **trustees are expected to police that advice has been taken** prior to a transfer. Interestingly, however, they do not need to check the advice suggested a transfer to be positive before making a payment.

Considerations for trustees

DC schemes are not obliged to offer the new pension freedoms and, as noted earlier, many are choosing not to do so. We are finding the decision is largely made on the grounds of administration costs. This is perfectly justifiable and does not present a problem when members are entitled to transfer to an arrangement that can deliver the flexibility they seek.

Two interesting questions arise in DB schemes:

- **should you automatically quote and offer a transfer value at retirement?**
- **if you do, could this be viewed as encouragement to transfer?**

The jury is very much out on this. On balance, we feel the transfer option should not be hidden from members as, in some cases, it may be a perfectly justifiable decision.

A further dilemma DB trustees should consider:

- **If your scheme is underfunded, how might a flurry of transfer requests impact on the security for the remaining members?**

As is ever the case with DB schemes, some fine balancing acts will be needed.

In conclusion...

It remains early days with members, policyholders and the industry feeling their way. There is currently **no evidence that members are making poor decisions**, although the regulators are keeping a watching brief on developments.

The concern about ill-considered transfers paid from DB to DC arrangements to access the freedoms are mitigated, at least for those with transfers over £30,000, by the requirement to check the member has received regulated financial advice. This has effectively put a brake on many transfers. We hear many **financial advisers are reluctant to provide advice** because of a concern that advice not to transfer will be ignored. Past experience makes them naturally wary of the potential ramifications from members and regulators in the future. To some extent this probably also reduces concerns about transfers to pensions liberation 'schemes', at least for members with larger pension pots.

It remains to be seen whether the government are keen to progress their suggested plans for encashment of annuities, which would seem consistent with the new freedoms. One thing we can be sure of, with the recently launched consultation on pensions tax relief, **we haven't seen the end of changes to the pension system just yet!**

What do you think?

Share your thoughts with us, email **mark.homer@psitl.com**