PENSIONS AND DIVORCE

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Courts will generally take the **value of pension rights** into account when deciding on the overall distribution of financial assets on divorce (in England, Wales and Northern Ireland).

However, pension rights **cannot easily be transferred** between individuals, and so there are a number of **alternative options** for taking them into account, each of which has their drawbacks, as detailed in this note.

Please note that these comments apply to English law and are intended to be an overview of the main options only. Professional legal advice should be sought.

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There are three main choices when it comes to deciding how to account for pensions assets in a divorce: offset, attachment order, and pension sharing. Each has advantages and disadvantages, and it is important to be fully aware of the potential pitfalls when agreeing to a particular method.

OFFSET

This is perhaps the simplest arrangement, where the pension assets are left as they are, and the distribution of other assets is adjusted accordingly. In considering whether this route is suitable, the individual should consider the method of valuation used for the pension scheme assets (i.e. whether this is favourable or not). In addition, the administration, complexity and time (and therefore cost) involved in pensions earmarking or sharing is likely to be considerable, which makes offset a popular and potentially cheaper route.

ATTACHMENT ORDER

ALSO KNOWN AS PENSIONS EARMARKING OR DEFERRED MAINTENANCE

This requires an Attachment Order, which decrees the proportion of the pension scheme member's retirement pension/lump sum to be 'earmarked' for the former spouse. A pension already in payment cannot be earmarked.

This can entail a number of problems, which mean that this method is not frequently used:

- There is no clean break.
- The former spouse remains dependent upon the retirement age and pension investment decisions of the member, including any decisions made on the method of taking benefits under the new pensions freedom rules.
- The member remains liable for income tax on the total pension paid, and the earmarked pension is paid to the former spouse net of tax, which may clearly be inefficient if they do not otherwise use their personal allowance, for example.
- Entitlement to earmarked benefits may be lost if the former spouse remarries.
- Entitlement to earmarked benefits may be lost if the member dies, unless the ex-spouse is compelled to be named as a beneficiary. This could mean that no benefits are received by the former spouse whatsoever.
- The amount earmarked is worked out as a percentage of the Cash Equivalent Transfer Value (CETV), which may understate the true pension value (for example, it may not include discretionary increases, salary increases, scheme surpluses for final salary schemes, or any guaranteed annuity rates for money purchase schemes).
- The total benefit, including benefit to be paid onto the ex-spouse, is assessable against the member's Lifetime Allowance.

However, earmarking can also apply to the retirement lump sum, which is not the case with the alternative, Pensions Sharing.

PENSION SHARING

OR SPLITTING

The Pensions Sharing Order was introduced to try to introduce a clean break, and took effect for proceedings starting on or after 1 December 2000. This works by creating a pensions credit for the former spouse, with a corresponding debit on the member's account. For a money purchase scheme, the debit is simply a reduction in the fund value. The situation is more complex for a final salary scheme, where the debit is a proportion of the benefits that would be payable on leaving service (based on the Cash Equivalent Transfer Value), revalued under statutory rules to the date of retirement, and then deducted from the final benefits payable.

Pension sharing overcomes many of the problems with earmarking, in that the credit can be moved to the spouse's own arrangement (except for SERPS/S2P pensions, where it becomes a shared additional pension), and the spouse then has control over investment decisions and when to take the benefits.

Pension sharing orders are able to be made in respect of:

- Occupational pension schemes, AVCs and FSAVCs.
- Personal pensions and RAPs.
- Services pension schemes.
- FURBS.
- Pensions in payment.
- SERPS and S2P.

The following schemes cannot be shared:

- State graduated pension scheme benefits and equivalent benefits.
- Widow/ers' and dependants' pensions in payment.
- Lump sum benefits on death in service.
- Basic State pension.

However, there are a few drawbacks:

- This arrangement may mean that both parties incur higher fees than with earmarking.
- The pension share is worked out as a percentage of the Cash Equivalent Transfer Value (CETV), which may understate the true pension value, as detailed above.
- The former spouse may be required by the trustees to transfer the pensions credit.