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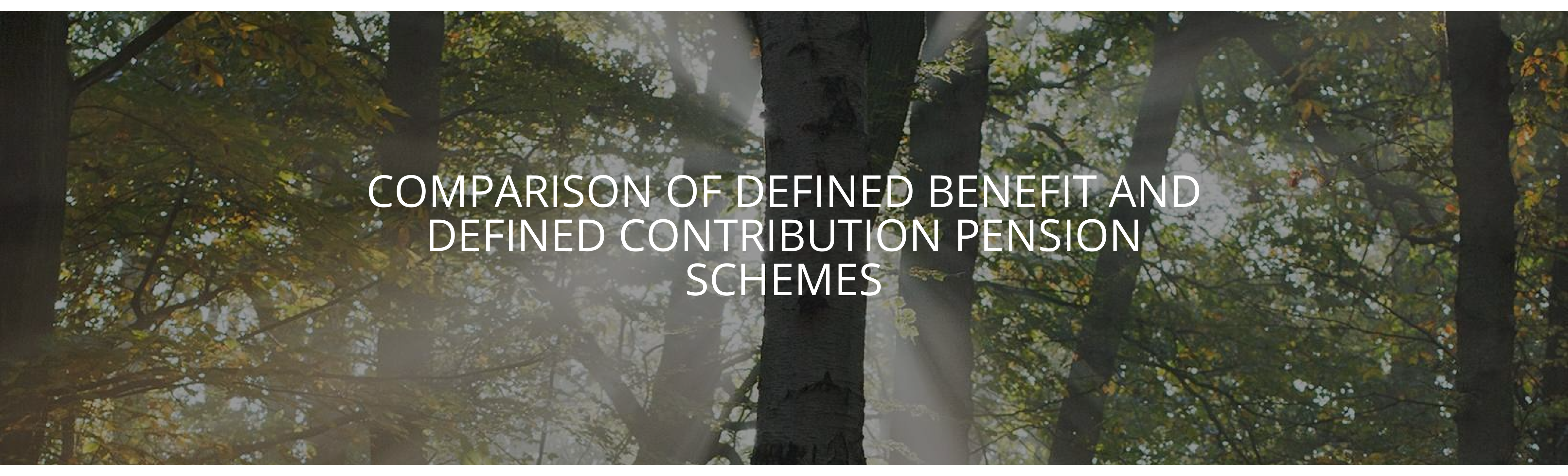

COMPARISON OF DEFINED BENEFIT AND DEFINED CONTRIBUTION PENSION SCHEMES

Defined benefit schemes

A defined benefit (DB) pension scheme is one type of workplace pension scheme, in which an employer promises a specific pension payment, lump sum (or a combination of both) on retirement. The scheme trustees make all the investment decisions so there is no investment risk to the individual members.

This type of pension scheme is also commonly known as a 'final salary' scheme.

The benefits payable are predetermined using a number of factors, typically including, your earnings, the length of time that you have been a member of the scheme, your age and a rate of accrual determined by the scheme. The pension scheme will define what is meant by 'earnings', this could be basic pay and may not include overtime, commission or other benefits.

Defined benefit schemes may be based on your final salary or an average over your career whilst you have been a member (career average).

Defined benefit schemes pay out a secure income for life which typically increases each year. You might have a defined benefit pension if you've worked for a large employer or in the public sector.

Your employer contributes to the scheme and is responsible for ensuring there's sufficient money within the scheme at the time you retire to pay your pension income. You may also be asked to contribute to the scheme. Any contributions you make are normally deducted from your salary before your income tax is calculated.

At retirement you will receive a pension income and potentially the option of a tax free lump sum. Many schemes will offer a reduced income if you wish to take a tax free lump sum payment, however some offer a tax free lump sum in addition to an income.

Where the total value of all of your pension benefits (the defined benefit pension and any other private pension plans that you may have) is £30,000 or less, you can take the whole of your defined benefit pension as a lump sum, currently 25% will be tax free and the remainder will be subject to tax at your marginal rate, this option is normally only available from age 55, this will be increasing to 57 from 2028.

If you die when you are in receipt of your pension, a reduced pension will continue to be paid to your spouse or civil partner for their lifetime.

Depending on your employment history, you may also have one or more deferred DB pension schemes. This is where you have been a member of a DB pension scheme but have left the company, or the scheme has closed, so you are no longer an active member and the benefits are 'deferred' until you retire or elect to transfer them.

The value of a deferred pension in a DB pension scheme will continue to increase at least in line with inflation from the date of you leaving the scheme, up to the earlier of your retirement age when you take the scheme pension, or election to transfer out of the scheme.

Defined contribution schemes

A defined contribution scheme is a pension where you build up a pot of money which can be used to provide you with an income in retirement and can be in the form of:

- For individuals - Personal pension plan (PP), Stakeholder Plans, Self Invested Personal Pensions (SIPPS), Retirement Annuity Contracts
- Through your workplace – Group personal pensions (GPP), Group Stakeholder, Occupational Money Purchase Plans, Small Self-Administered Schemes (SSAS), Executive Pension Plans

You may have more than one of these.

You can get tax relief on personal pension contributions up to 100% of your annual earnings (or £3,600 if more).

Your total pension contributions from all sources, employer included, are subject to the annual allowance of £60,000 and if the annual allowance is exceeded you will be subject to a tax charge on the excess (which can in some cases be paid out of your pension fund). It may be possible for the excess to be covered by unused annual allowances from the last three tax years.

If you have a high income, you may have an annual allowance that is lower than £60,000 (down to as little as £10,000 potentially). And if you have already accessed some of your pension funds flexibly either through an Uncrystallised Funds Pension Lump Sum (UFPLS) or Flexi-Access Drawdown (FAD) and taken an income, you will be subject to the 'money purchase' annual allowance and your tax efficient total annual contributions from all sources will be limited to £10,000.

Defined contribution pension schemes invest the contributions, made by you and / or your employer in a range of different investments.

If you have a PP plan, you can choose your own contribution level and how your contributions are invested. You make your contribution net of 20% tax relief and your pension provider will automatically claim back 20% and add it to your pension pot. If you pay a higher rate of Income Tax, you will need to claim the additional tax yourself through your self-assessment return or tax code adjustment.

If you are a member of a GPP, the minimum contribution level will be determined by your employer but you are usually allowed to pay more than this if you wish and you should be offered a choice on how the contributions are invested. Your own contributions are deducted from your salary after tax has been taken off and your contributions are paid net of basic rate tax relief (currently 20%).

Another type of workplace defined contribution scheme is the occupational money purchase scheme. Each member of the scheme doesn't have their own individual policy and contributions may be deducted from salary before income tax is calculated.

Defined contribution pension schemes are also known as 'money purchase schemes'.

Your pension pot is built up using your own and your employer's contributions (if applicable) plus investment returns and tax relief.

The benefits available on retirement are dependent on:

- How much has been paid in on your behalf (by you and / or your employer)
- The length of time that monies have been invested and the fund's investment performance, and
- The level of charges deducted from the plan

You can access and use your pension pot in any way you wish from age 55, this is increasing to 57 from 2028. You can also keep saving into your pension and get tax relief until you reach the age of 75.

The options currently available when you access your plan are:

- Take your whole pension pot as a lump sum in one go. A quarter (25%) will be tax free within allowable limits and the rest will be subject to Income Tax and taxed in the usual way. Your tax free cash entitlement may be higher if you have applied for tax free cash protection or scheme specific protection applies. Bear in mind that a large taxable lump sum could tip you into a higher tax bracket for the tax year you take your lump sum.
- Take lump sums as and when you need them. A quarter of each lump sum will be tax free (within allowable limits) and the rest will be subject to Income Tax and taxed in the usual way. Bear in mind that a large taxable lump sum could tip you into a higher tax bracket for the tax year.
- Take a quarter of your pension pot as a tax-free lump sum (within allowable limits), then place the rest in a drawdown plan which allows the funds to remain invested and withdrawn as and when required (this might be to provide you with a regular taxable income or to make ad-hoc withdrawals). Bear in mind that a large taxable lump sum could tip you into a higher tax bracket for the tax year.
- Take a quarter of your pot as a tax-free lump sum (within allowable limits) and then convert some or all of the rest into a taxable guaranteed income for life (known as an annuity).

Features	Defined benefit schemes	Defined contribution schemes
Contributions	Your employer contributes to the scheme and is responsible for ensuring there's enough money at the time you retire, to pay your promised pension income. You may have to contribute to the scheme too.	Defined contribution pensions build up a pension pot using your contributions and your employer's contributions (if applicable) plus investment returns and tax relief.
Investment Choice	The scheme trustees make all the investment choices.	With a personal pension plan or group personal pension plan you can usually choose from a range of funds to invest in. With an occupational money purchase scheme the trustees normally make the investment decisions.
Flexibility	It's not usually possible to reduce your contribution levels or suspend them. Contributions can usually be increased by using a separate plan (an additional voluntary contribution plan) or potentially by purchasing additional pension/years within the scheme.	It's often possible to increase and decrease contribution levels or stop them. You can also change your investment choices on a regular basis with a group or personal pension plan.
Security	Defined benefit schemes are protected by the Pension Protection Fund.	These schemes are usually covered by the Financial Services Compensation Scheme. The cover can vary depending on the structure of the plan and how the funds are invested.
Charges	There are no explicit charges or fees.	These will vary from scheme to scheme and often include an annual management charge and, particularly for older schemes, a bid / offer spread or policy fee.
What happens if you leave your employment?	You will become a deferred member of your pension scheme so you will be entitled to benefits on your retirement in line with your period of employment. You may transfer your accrued benefits to a new pension plan. Please note that if you were a member of a public service pension scheme, for example NHS or civil service, this may not be possible.	Your fund will remain invested until your retirement. You could transfer the accrued fund to another pension provider. With personal pension plans it's normally possible to continue your own contributions, within allowable limits until age 75.

Benefits	Defined benefit schemes	Defined contribution schemes
Pension commencement lump sum	Some schemes offer a tax free lump sum in addition to a pension income, whilst others offer a reduced pension in return for the tax free lump sum. The maximum lump sum is based on a combination of HM Revenue and Customs' rules and those of the particular scheme.	25% of the total pension fund can be taken as a tax free lump sum within your Lump Sum Allowance (£268,275 if you have no protection). This can normally either be taken in one go or in stages.
Income	Your pension income is based on: the number of years you have been in the scheme, your age, the scheme's accrual rate and either your final or career average salary. The scheme will pay the pension directly to you whilst you are living and it may increase annually, for example in line with Retail Price Index / Consumer Price Index, but it will not reduce.	You can choose how you take your pension income, you can withdraw the entire fund in one go or take income withdrawals at your chosen level. This level of income can increase, decrease or stop as required, however when the total fund is exhausted, you will be unable to take any further income. Or you can take a guaranteed income for life i.e. purchase a pension annuity.
Tax	Your income will be paid to you net of tax at your marginal rate via the PAYE system.	Your income will be paid to you net of tax at your marginal rate via the PAYE system. Ad-hoc withdrawals may have emergency tax deducted but any overpayment can be reclaimed.
Retirement age	You can usually take your pension from age 55, this will increase to 57 from 2028. However, if the scheme's normal retirement date is higher, you may incur an early retirement penalty should you retire earlier than this age.	You can usually take your pension from age 55, however this is increasing to 57 from 2028.

Death benefits	Defined benefit schemes	Defined contribution schemes
Lump sum	Depending on the rules of the scheme and whether you were still a contributing member of the scheme at the time of your death, should you die before taking your pension, your dependants may receive a tax free lump sum (on death before age 75) and / or a taxable pension income. If you have already left the employer (for example are a deferred member), your dependents may only receive a return of your contributions. However, you should check the scheme rules as a lump sum and / or a reduced spouse's pension may also be available.	Should you die before drawing on your pension pot or if you have placed funds in a drawdown plan, your selected beneficiary(ies) can elect to take a lump sum. This will be tax free should you die before age 75 and the lump sum isn't more than your available Lump Sum and Death Benefit Allowance (with any excess being subject to income tax) and the full lump sum is taxed at the recipient's marginal rate should you die after 75. If you have purchased an annuity, depending which options you selected at the time of purchase, there may be an ongoing income or a lump sum available in respect of any pension guarantee period or capital protection that you chose to include (payable tax free if death occurs before 75).
Survivor's pension	If you are married or have a civil partner, a pension will normally be payable for the duration of the spouse / civil partner's life. In some cases, a pension may be paid to dependent children for a specified period of time. Each pension scheme's rules and booklet will specify the criteria it will use. Any pensions paid are taxed at the recipients' marginal rates. These pensions cannot be passed on or left to another beneficiary of your choice.	If you purchase an annuity, for there to be a survivor's pension payable on your death, this must have been selected at the time of purchase. If you have a drawdown fund, any remaining benefits can be passed to a beneficiary(ies) of your choice. They can elect to take an income (drawdown income or annuity) or a lump sum and this will be tax free should you die before age 75 (in the case of a lump sum, if it isn't more than your available Lump Sum and Death Benefit Allowance (with any excess being subject to income tax)) or taxed at the recipient's marginal rate should you die after 75. On the recipient's death, they can pass any remaining drawdown funds to their beneficiaries (with the rate of tax determined by their own age at death).

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