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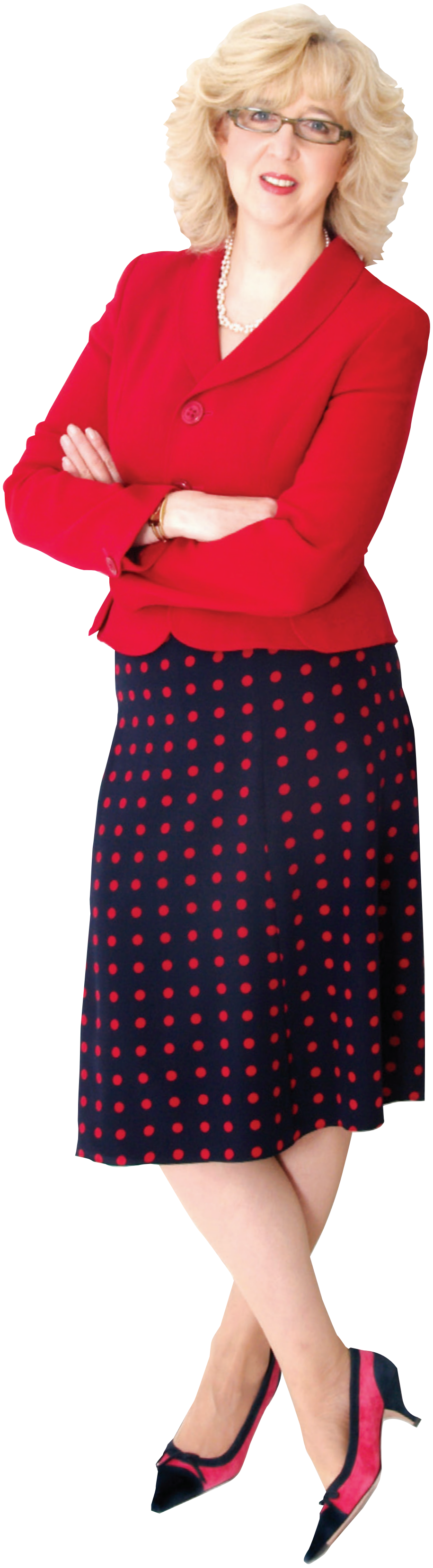

What is a pension?

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Well a pension means just 'putting a bit by for the future'. It's fundamentally only a savings scheme where you save up over your working life – until 65 (ish) and then when you stop work you get the money back by receiving an income from the pot of money you have saved – and that pot is your pension fund, and the income is the pension itself.

Sounds simple doesn't it – but it has become hugely over complicated because pensions are heavily regulated by the government with all the administrative bureaucracy that entails.

Pensions are regulated by the government for two reasons – or should I say they used to be regulated for two reasons:

Firstly,

- Pensions come with all sorts of tax benefits and tax reliefs, so the government want to safeguard their part of the money and make sure the pension is looked after properly and is there when you need it.

And secondly

- To stop you spending it too early!!! The government need you to hang onto this money otherwise they end up paying social benefits etc if – or when you're broke!

Now this second reason is the one that has changed recently – and one of the fundamental changes for 2015, because the government has now decided that you can spend it all if you wish – and more on that in a later report.

So with that basic definition of a pension made what different sorts of pension are there?

There are three basic types:

1. **Government or state pension** which is a pot of money you pay into through the tax and national insurance that are deducted from your earnings. If you have a paid job, these amounts are taken from your salary before you get it! If you are self employed you have to account for this, and pay over the money to the Inland Revenue (now called HMRC – Her Majesty's Revenue and Customs) yourself.

2. **Corporate pensions** are pensions provided by the company (or business or employer) you work for, and you may have to contribute to that (when the amounts saved are again deducted from your pay packet), or it may be a non-contributory pension (where you don't put in yourself but all the savings contributions are made by your employer), or it may be a joint scheme where you save some and the employer saves some – each scheme is different.

What do you get back from these corporate pensions? Well this depends on whether it's a final salary scheme or a money purchase scheme. If it's a final salary scheme you continue to be paid by the employer after you retire and the amount you get is related to what you earned in, normally, the final years of working there. So if you retire on a salary of £20k per year you may get two thirds of that for example. Again each scheme is different so make sure you check what you have.

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The final salary schemes are very rare nowadays and it's more likely that you have a money purchase scheme and that means you get back an amount based on what you (and your employer) have put in, plus whatever the pension fund managers' have managed to earn on that whilst you have been saving.

And the third category of pensions is the…

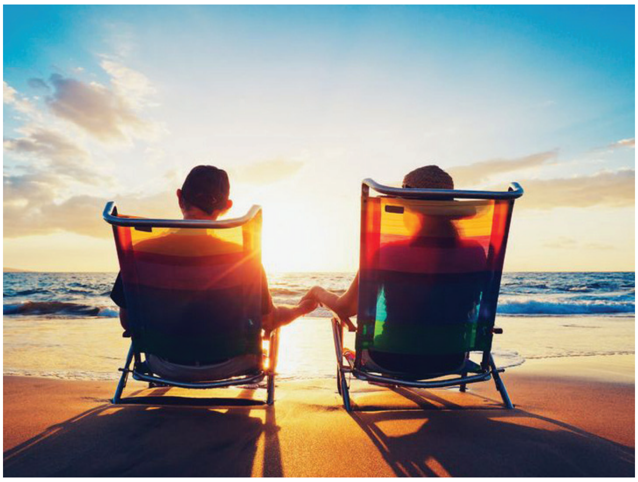
Personal pension where you basically look after your own pension savings and you have flexibility in where that goes and who invests it for you.

It isn't possible for you to have completely free rein with your own money here and you have to have it safeguarded as a pensions fund separately but you can decide where it gets invested.

The main personal pension now is a SIPP – a Self Invested Personal Pension, although there are others.

<u>Before we move on let's just consider If you're stuck with the Pensions you have and is there any flexibility to change?</u>

Obviously we have no choices with the state pension – that's for the government to decide and allocate to us – but with a corporate pension we may not have to stick with it.



However you might **want** to stick with a corporate pension if you are lucky enough to have a final salary scheme. Other than that you can generally transfer a company or employer pension into a SIPP, or another scheme and you won't lose the benefits even if you leave the job.

What you do here is to ask your current employer – or pension provider – if the pension is transferable, what the transfer value might be and how to transfer – and they should send you all the details.

You then transfer the pension's savings pot to a pension fund provider of your choice – and that may mean that YOU can have control of it!

And also remember that each of these pensions is independent of each other so you can have 1, 2 or all 3 of them – they aren't mutually exclusive

<u>Now all that sounds relatively simple – so how come the pensions provision in the UK and elsewhere is in such a mess?</u>

There are several contributing, and generally interlinked parts to that:

Firstly I have to say that most people don't really get the idea of pensions and long term savings. As at the end of 2013, approximately 1 in every 5 people retiring will be living below the poverty line: in an average retirement of 19 years, the normal person starts to run out of living money after 7 years and they then either make significant cuts in their living expenses or they have to go back to work: and that means that we now have over 1 million people over the age of 65 still working. Despite all those terrible warnings – many people still put their head in the sand and assume it won't happen to them – well I'm afraid to say unless you do something about this - it will!

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The second part of the problem with pensions is inadequate funding – and that's inadequate funding on a personal level in personal and corporate pensions but it's also inadequate funding into the state pension system whereby we have fewer people contributing into the system via their tax and national insurance contributions and more and more people drawing out from it. There are now 11 million pensioners, with more than 80% of the workforce living long enough to claim a pension. It is expected that there will be 12.5 million pensioners by the year 2025 when there will be only 3.5 working people for every pensioner compared to approximately 4.5 now...

...and we also have the issue of an ageing population because...

Thirdly people are living longer – so that means they need a bigger pension pot to start with so that it lasts them for as long as they need it. We already have over 12,320 people over the age of 100 and that figure is expected to grow.

And these combined changes means that there's less money to go round and we're trying to spread it too thinly.

Just on a family by family basis – if we have granny and granddad living to 100 and the children longer in full time education It can lead to one or two employed people in the middle – say mum and dad - trying to support three generations of living expenses. That's tough.

Increasingly we're all relying on each other in the family for more money – in some cases two complete generations within one family can both be retired - and we're hoping that granny is going to leave us something substantial in her will – but sadly granny has had to spend all her money topping up her pensions so that she could live and support herself, because again, frankly, she was rather hoping that you would support her.

It's a very difficult and inescapable vicious circle.

It's a situation that has resulted in over 3 million people declaring that they are relying on the lottery to fund their retirement – now that is a pipe dream – but very sad.

Unfortunately the pensions system is fundamentally flawed – and the system just wasn't set up right in the first place some 100 years ago.

Knowledge of how the state pensions system was established goes some way to helping us understand the problem we're in.

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