Pensions on Divorce and the parameters of need

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Pensions on Divorce and the parameters of need

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- My brief is to discuss:

  "What are the boundaries on need in pensions, <u>particularly</u> in short to medium length and childless marriages or where the parties are comparatively young?"

- Easy to answer question?!?
- More difficult to answer with longer marriages and where people have detrimentally altered their financial position as a result of joint decisions in the marriage. A.k.a relationship generated need.

The short and childless marriages

- PAG:

  Part 6, page 25, second indent "It will often be fair to aim to provide the parties with similar incomes in retirement, but equality may not be the fair result depending on needs, contributions, health, ages, the length of the marriage, or, in non-needs cases, the non-matrimonial nature of the asset."

  Part 6, page 25, seventh indent "In some cases, an equal division is not appropriate; for example, in a short marriage with no children. Where the parties have worked throughout the marriage and each have their own pensions, no adjustment may be needed…."

- PAG2 due to launch shortly.

Needs or sharing?

- *WC v HC* [2022] EWFC 22 at [21] per Peel J

  "Where the result suggested by the needs principle is an award greater than the result suggested by the sharing principle, the former shall prevail.

  In vast majority of cases the enquiry will begin and end with the parties' needs. It is only in those where there is a surplus of assets over needs that the sharing principle is engaged."

- *Juffali v Juffali* [2016] EWHC 1684 (Fam) [66] – [79] – good statement on needs (albeit in very big money case)

The elasticity of need

- *FF v KF* [2017] EWHC 1093 (Fam) [18]

"18. So far as the "needs" principle is concerned there is an almost unbounded discretion. The main rule is that, save in a situation of real hardship, the "needs" must be causally related to the marriage. Like equity in the old days, the result seems to depend on the length of the judge's foot. It is worth recalling that Heather Mills-McCartney was awarded over £25m to meet her "needs" (McCartney v McCartney [2008] EWHC 401 (Fam)). Mrs Juffali was awarded £62m to meet her "needs" (Juffali v Juffali [2016] EWHC 1684 (Fam)). In the very recent case of AAZ v BBZ [2016] EWHC 3234 (Fam) the court assessed the applicant-wife's "needs" in the remarkable sum of £224m. Plainly "needs" does not mean needs. It is a term of art. Obviously, no-one actually needs £25m, or £62m, or £224m for accommodation and sustenance. The main drivers in the discretionary exercise are the scale of the payer's wealth, the length of the marriage, the applicant's age and health, and the standard of living, although the latter factor cannot be allowed to dominate the exercise."

The short and childless marriages

- Short marriage (Dictionary of Financial Remedies 2022 at p.37)

    "In practice a marriage of three years or less can properly be characterised as a 'short marriage' … "

- No exact rule, up to 5 years perhaps?
- Not huge amount of case law on short marriages and nothing really on pensions in this context.
- Short (childless) marriage = more parsimonious capital relief?
    - Needs looked at more conservatively?
    - "Get back on feet fund?"
    - But what if sharing results in higher award?

The short and childless marriages

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- *Miller* per Lady Hale [153] "…still some scope for one party to acquire and retain separate property which is not automatically to be shared equally between them."

- *Charman* – Unilateral assets "confined"

- *Sharp v Sharp* [2017] 2 FLR 1095 – [95] and [107] Short marriage, still space for unilateral asset. (Mostyn J extra-judicially "absolute shocker.")

- *XW v XH (Financial Remedies: Business Assets)* [2020] 1 FLR 1051 [142] "…I find it hard to envisage how, <u>in other than short, childless marriages</u> fairness would be achieved if the existence of 'business assets' was the basis of justifying an other than equal division." (and see [145])

- *E v L* [2021] EWFC 60 (Fam) – Mostyn J - No special approach for short childless marriage. Acquest shared equally. Debate about childlessness inappropriate and "was to make a window into people's souls."

Asset classes compared

- *Miller* [22] – Matrimonial home has central place in the marriage "So it should normally be treated as matrimonial property for this purpose. As already noted, in principle the entitlement of each party to a share of the matrimonial property is the same however long or short the marriage made have been."

- *GS v L* [2013] 1 FLR 300, King J (£4M assets) "So far as the pension is concerned, it can and should, in my judgment, properly be excluded from the division of the assets, a position effectively, although not absolutely, conceded by the wife. The pension cannot be drawn down for many years and was accrued entirely before the marriage; the fund cannot be used to provide for the wife's needs in either the short or medium term. Given the benefit of the capital with which she will leave the marriage and a working life of 25 years ahead of her, fairness in my judgment requires that the husband should retain his pension fund absolutely."

Approach to pensions in needs case

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- *W v H (Divorce financial remedies)* [2020] EWFC B10
    - No one size fits all.
    - Para 60(i) broad approach where parties young.
    - Capital value may not be fair result as parties closer to retirement.
    - Often fair to equalise incomes.
- FJC Needs paper (2018) (Annex 3) Emphasis on income approach in needs cases
- *Waggott v Waggott* [2018] EWCA Civ 727. Deploy (+ amortise?) free capital to meet needs

Approach in needs case – Apportionment?

- PAG 4.3 "It is important to appreciate that in needs based cases, just as with non-pension assets, the timing and source of the pension saving is not necessarily relevant – that is to say, a pension-holder cannot necessarily ring-fence pension assets if, and to the extent that, those assets were accrued prior to the marriage or following the parties' separation. It is clear from authority that in a needs case, the court can have resort to any assets, whenever acquired, in order to ensure that the parties' needs are appropriately met."

- CF: Sharing cases where apportionment is appropriate see e.g. Non-matrimonial pensions: the forgotten discussion. Joe Rainer. Family Law Journal [2020] 95.

- Key question: Where does one draw the line between needs and sharing?

How to turn DC funds into a pension income

The two main approaches that can be adopted are:

Annuity purchase	Income drawdown
• Explicit product purchased from insurer • Provides a guaranteed income for life at point of retirement • Can specify increases, spouse's provision etc • Removes risk of long life expectancy but uses up capital regardless of how long annuity is in payment	• No explicit product purchased • Individual keeps monies invested in some form and draws down on it each year • No protection against investment risk or "longevity risk" (i.e. living longer than expected • Scope to leave funds to children etc if these still exist at point of death

Other methods exist and divorcing parties **must** be encouraged to seek the advice of an IFA or similar!

How to turn DC funds into a pension income

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- We shall consider retirement at age 60 and 67 for an individual / couple now approaching age 60 i.e. immediate retirement and then deferring retirement for seven years
- Assumptions made below provided by Mathieson Consulting Limited (MCL)
  - Funds will return 2.00% pa over CPI inflation in the period until retirement occurs at age 67
  - Funds will return 1.00% pa over CPI inflation after retirement (income drawdown only)
  - Incomes in retirement to be linked to CPI inflation
  - Annuity purchase using MCL annuity calculator, broadly in line with insurer pricing
  - Life expectancy using ONS18 tables in *At A Glance*, scaled up by 10%
  - Thus assume that a 60 y/o lives for **29 years** and a 67 y/o lives for **22 years**
  - "Single lives" only considered i.e. no attempt made to model what is payable after death of one party

How to turn DC funds into a pension income

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- Mathieson Consulting derive the following terms upon which we can convert DC funds at retirement into an income stream

- Figures below based on £100k DC pot at age 60

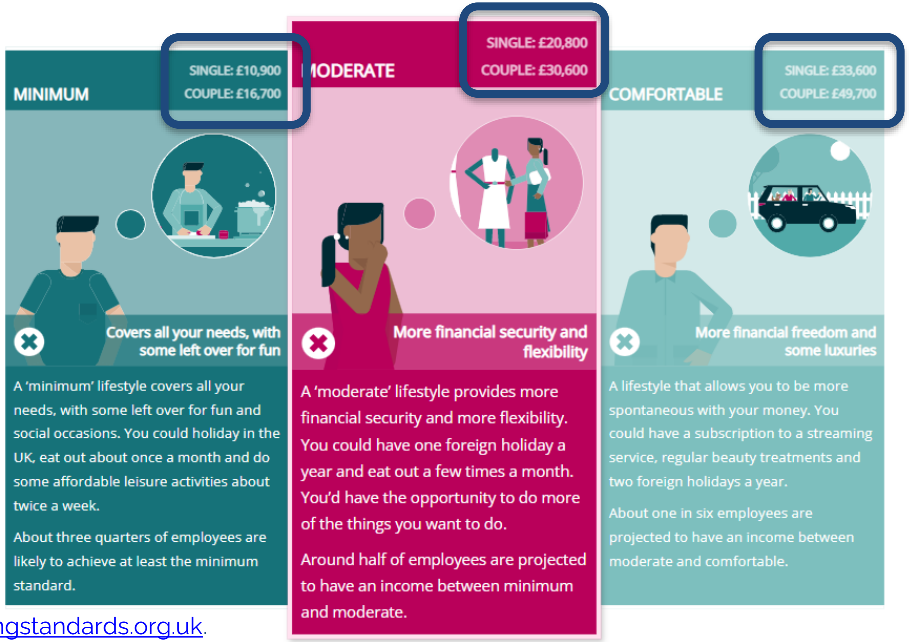
Retirement age	Age 60	Age 67
Annuity purchase	£3,050 pa	£4,580 pa
Income drawdown	£4,010 pa	£5,880 pa

- Thus if you had £100k at age 60, you could…
  - Retire immediately with a guaranteed annuity income of **£3,050 pa**, or
  - Defer retirement until age 67, then to receive an annuity income of **£4,580 pa** (in today's money); or
  - Follow a drawdown approach instead at either age 60 or 67

- These income amounts are GROSS before income tax

What level of income might be needed in retirement?

- The "Retirement Living Standards" are published by the Pensions and Lifetime Savings Association (trade body for pension schemes)
- Details of incomes needed (in 2021–22 terms) as opposite:
- Income figures include State pension i.e. "minimum" income largely covered by State pension
- It follows that a couple needs less than 2× what a single person needs in retirement
- Incomes are NET after income tax



Source: Retirement Living Standards website, https://www.retirementlivingstandards.org.uk.

How much might this income cost?

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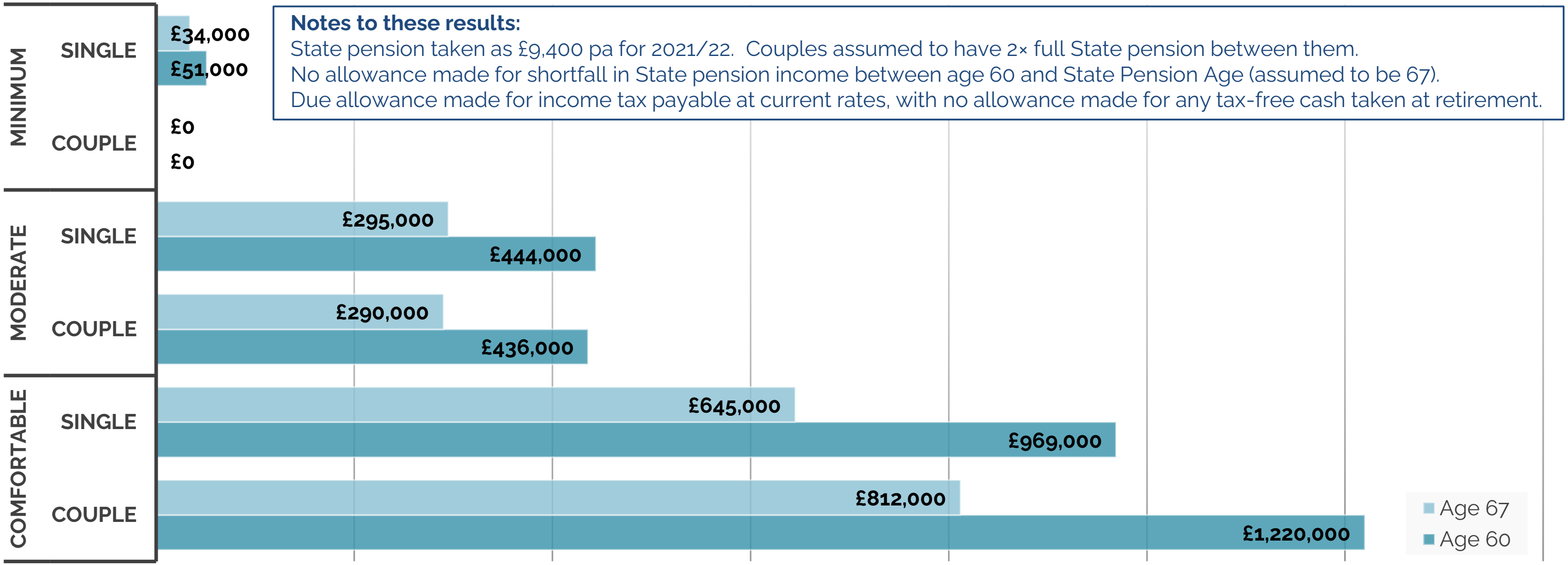
Based on **annuity purchase**, MCL determine that the following DC funds would be needed at age 60 to provide income in additional to State pension:

Notes to these results:
State pension taken as £9,400 pa for 2021/22. Couples assumed to have 2× full State pension between them.
No allowance made for shortfall in State pension income between age 60 and State Pension Age (assumed to be 67).
Due allowance made for income tax payable at current rates, with no allowance made for any tax-free cash taken at retirement.



How much might this income cost?

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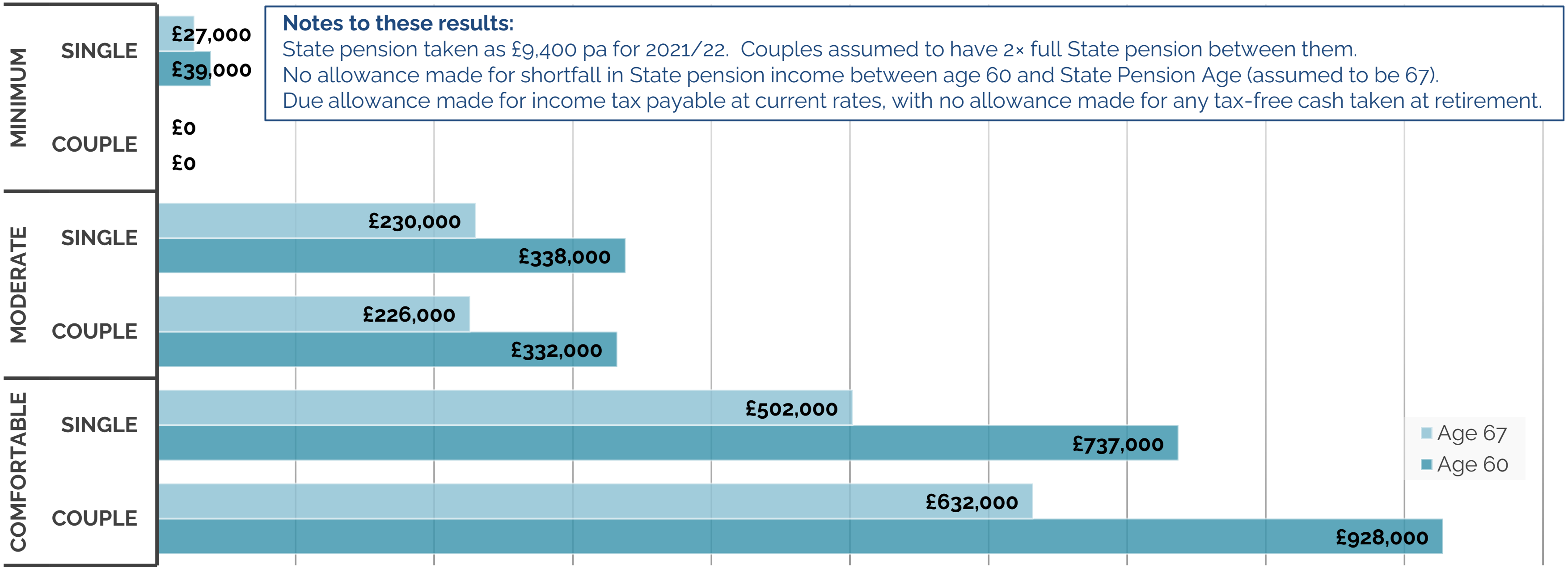
Based on **income drawdown**, MCL determine that the following DC funds would be needed at age 60 to provide income in additional to State pension:



What levels of income might the LTA provide?

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- The **Lifetime Allowance (LTA)** is the maximum amount of tax-advantaged DC funds that an individual can accumulate over his/her years of employment
- It is set by HMRC at **£1,073,100** and is frozen at this level until at least 2026/27
- *But how far might this level of DC fund now go in providing an income?*
- We shall consider:
  - Annuity purchase *versus* income drawdown
  - Immediate retirement at age 60 *versus* deferring retirement until age 67
  - Having the full LTA (£1,073k), half LTA (£536k) and quarter LTA (£268k) as a DC fund now
- Assumptions provided by MCL as before

What levels of income might the LTA provide?

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Based on **annuity purchase** (incomes shown are GROSS and no allowance made for State pension provision):

Notes to these results:
No allowance made for any tax-free cash taken at retirement. No allowance made for any LTA tax charge arising where fund remains invested until age 67.

What levels of income might the LTA provide?

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Based on **income drawdown** (incomes shown are GROSS and no allowance made for State pension provision):

Notes to these results:
No allowance made for any tax-free cash taken at retirement. No allowance made for any LTA tax charge arising where fund remains invested until age 67.

Key points to take away

- Annuity purchase is seen as “expensive”: low interest rates and increasing life expectancy lead insurers to price such products prudently
- Income drawdown is shown here as providing a higher *per annum* income BUT this comes with greater risk to the individual
- Subject to what “*Waggot* style provision” is available, most people after a medium to long marriage will need whatever pension they can get.
- Often inappropriate to be running apportionment arguments in non-big money cases.
- Figures from MLC hopefully give some indicative feel for what certain levels of pension capital can provide by way of income.

Notice and contacts

These slides are no substitute for professional advice and should not be relied upon as such.

Rhys Taylor would like to thank and acknowledge the invaluable assistance that Mathieson Consulting has made to the preparation of these slides.
Any mistakes, however, remain the fault of Rhys Taylor.

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