This communication is for financial advisers only. It mustn't be distributed to or relied on by customers or any other persons.

DB and DC schemes – what's the difference in protection cover?

Are pension savings protected?

An important consideration when someone begins to build up significant pension savings is how secure their savings are. What happens if an employer or the pension provider holding the benefits or funds finds themselves in financial difficulties?

If your clients are members of more than one pension scheme or contract, and are considering consolidating their pension pots or taking benefits, then it it becomes even more important to understand the level of protection available for their savings.

Generally, there are two main types of pension savings that someone can build up in the UK - **defined benefit (DB)** and **defined contribution (DC)**.

The information in this guide will help you explain to your clients how their savings are protected.

aegon

Defined benefit schemes

What happens if an employer encounters financial difficulties?

In a DB scheme, each member is promised a set level of benefit based on:

- Their salary
- Their length of service
- Their retirement age
- The scheme accrual rates

If an employer goes out of business, the Pension Protection Fund (PPF) offers some protection, although the amount of protection offered will depend on a person's circumstances. There may also be a cap on the amount of benefit provided.

PPF compensation

The PPF pays compensation to members of eligible DB schemes when there's a qualifying insolvency event in relation to the employer and there aren't enough assets in the pension scheme to cover PPF levels of compensation.

Before a scheme can be accepted into the PPF, it will enter an assessment period, which typically lasts an average of two years.

The level of benefits payable by the PPF depends on whether someone has passed their normal pension age on the date their employer became insolvent.

Generally, an employee will receive a pension equal to 100% of their scheme pension on the insolvency date if:

- They've passed their normal pension age when their employer becomes insolvent
- They've retired through ill health
- They're receiving a survivor's pension

If an employee hasn't reached their scheme's normal pension age when their employer becomes insolvent, they'll receive 90% of their scheme pension on the insolvency date. Any compensation amount paid will be increased in line with PPF rules rather than the former scheme rules.

Who is the PPF?

The PPF is a public corporation of the Department for Work and Pensions and you can find more information on them at **ppf.co.uk** – the PPF was set up on 6 April 2005 to protect members where an employer with a DB scheme becomes insolvent on or after this date and the pension scheme can't afford to pay those benefits promised to members on wind up. They're funded through collection of a compulsory levy from eligible DB pension schemes, by accepting assets from schemes that transfer to the PPF and by recovering funds from insolvent employers.

Defined contribution schemes

With DC schemes, the pension funds are generally held by a pension provider and each person has their own policy or product with the pension provider that holds their pension savings.

What happens if a pension provider encounters financial difficulties?

If a UK pension provider gets into financial difficulties, there should be protection in place through the Financial Services Compensation Scheme (FSCS). This protection should cover all pension policies and products held in the provider's pension schemes, although it's worth noting that the FSCS provides different levels of compensation according to the type of financial product involved.

Who is the FSCS?

The FSCS is an independent body set up under the Financial Services and Markets Act 2000 and is funded by levies received from the authorised firms that it covers. You can find more information about them at **fscs.org.uk**.

The FSCS may provide compensation for customers who've lost money as a result of a company or individual authorised by the Financial Conduct Authority (FCA) or Prudential Regulation Authority (PRA) going out of business.

FSCS compensation

For pensions, the compensation paid depends on:

- The type of pension product held
- The investments contained within it
- If any benefits have been taken or not

In general, pension products and annuities are treated as long-term insurance contracts, so if a pension provider is in default, compensation will be calculated as 100% of the value of the whole claim with no upper limit. In practice, it won't always be as straightforward as that. For example, self-invested personal pensions (SIPPs) can hold many different types of assets. Whether the FSCS can be called upon will depend on the investments held and who is in default (the SIPP provider or the investment provider of an asset held in a SIPP policy or product). More information on compensation limits for pensions can be found on the **FSCS website**.

What happens if an employer encounters financial difficulties?

If a person is a member of their employer's DC scheme, their pension savings won't be lost if the employer goes out of business. This is because pension funds in a DC scheme are generally held by a pension provider and each employee will have their own policy or product in the employer's scheme.

All funds held in individual policies or products will be secure if the scheme's employer stops trading. As part of the process of a company going out of business, a firm is appointed to deal with the company's affairs. The firm will check that all due employer and employee pension contributions have been paid and will seek to receive or recover any that are outstanding.

Aegon Retirement Choices SIPP, Aegon Platform SIPP and One Retirement

Any financial review and personal recommendation to transfer benefits from DB to DC will include your assessment of the suitability of the receiving scheme, the investment choices, benefits, and options that are available.

The **Aegon Retirement Choices (ARC) SIPP**, **Aegon SIPP** and **One Retirement** offer the full income and death benefit flexibilities that were introduced for DC schemes in April 2015. They give your clients more control over their pension savings and also a wide investment choice that can be tailored to meet their individual risk appetites.

You should be comfortable with the investment choices that you make for your client as they may lose features, protections, guarantees or other benefits when they transfer.

Please also remember that a transfer to the ARC SIPP, Aegon SIPP or One Retirement is moving to an investment-based product where the client's capital is at risk and the final value of their pension pot may be less than has been paid in.

For more information on DB to DC transfers, have a look at our DB support material, which aims to help with the suitability assessment and important areas to consider before deciding if a transfer is suitable.

aegon.co.uk/consolidation-toolkit

If you have any questions please speak to your usual Aegon contact.