



# Is your pension stuck in the mud?

Some older pensions that are closed to new business charge hefty fees if you try and leave. *Which? Money* investigates the murky world of closed-book pensions

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**WHAT YOU'LL LEARN** ■ Whether you should stay in your closed-book pension scheme  
■ The types of fees charged  
■ Other issues with closed schemes

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**C**ancelling a contract never seems to be as easy as it should be. From mobile phones to gym memberships, there are often exit penalties to pay, and you're unlikely to be able to escape without being given the hard sell to stay.

Getting out of a pension scheme is no different – especially if you're in a scheme that is closed to new business. Some schemes will charge you thousands of pounds to take your money elsewhere – leaving you with the unenviable choice of putting up with the poor returns and poor customer service that older providers often offer, or accepting disproportionately high fees.

Some schemes that are shut to new business, known as 'closed-book' pensions, are charging those leaving the scheme before their retirement date as much as 15% of their pension value.

There are almost five million closed-book pension schemes in the UK, and 16% of *Which?* members have money in one of them. When we carried out an online survey of 1,032 *Which?* members

and surveyed the 16 largest closed-fund providers, we found some shocking practices. One member, with a pension pot of £60,000, was charged £6,698 to leave his scheme.

## Why exit a closed-book pension scheme?

The main reason people want to leave a closed-book pension scheme is poor performance, but they are often trapped by high exit charges. Closed-book pension schemes are generally invested in with-profits funds – a type of investment that holds back payouts in good years to pay a steady return in years where the stock markets have fallen. They often guarantee to increase the fund by a minimum amount each year, and some (but not all) will even pay you a guaranteed income when you retire, agreed when you take out the policy (see p34 for more).

With-profits funds have performed poorly in recent years. According to independent financial advisers AWD Chase de Vere, some with-profits pensions have dropped in value by more than a quarter in the past five years. Scottish Widows paid out almost 30% less this year than it did in 2008, while Prudential's pension fund value dropped by 25%.

Performance of with-profits funds has been poor because while stock markets performed well in the late 1990s, insurers didn't stash away enough for the bad times to follow. So, while early >

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investors in with-profits funds did well, recent payouts have been falling dramatically.

Some closed-book pensions have struggled to recover from the falls in the stock market. When a pension scheme closes, it reduces its investments in riskier shares and increases its weighting in safe assets, such as gilts. This reduces the chance of the fund losing more money, allowing it to pay all the guarantees it has made.

But the move out of shares, which offer a better chance of growth, means a fund's ability to perform well is seriously diminished. For example, Royal & Sun Alliance reduced the proportion it invests in shares from 41% to 10% when it closed its pension fund – significantly reducing the possibility of higher returns.

### Lack of transparency

We found very little information available on closed-book pension schemes – even from the regulator. While the Financial Services Authority (FSA) was able to tell us the total number of closed policies in the UK, it couldn't reveal how many were workplace schemes and how many were personal schemes. And it was unable to say how many pension schemes currently had

exit penalties. Which? believes the regulator should have a clearer idea of the number of consumers in closed-book pensions.

Of the 16 providers surveyed, two declined to respond and five said it would take too much time. One even told us it would take 'months'. And those who responded didn't always provide all the information requested. We think that this shows a worrying lack of transparency surrounding closed-book pensions.

### Market value reductions and high charges

A market value reduction (MVR), is a percentage deduction which can be applied when you have been invested in a with-profits fund, and exit a scheme. Providers say they are in place to ensure each fund investor gets their fair share (see p34 for more).

But one Which? member, who is part of an Equitable Life scheme, told us that her MVR was 5% – while her minimum guaranteed rate of interest (the minimum amount that her money is guaranteed to grow by each year) was 3.5%. This means that if she stayed in the scheme for less than six years, her exit penalty would be higher than the benefits achieved – so it's worth looking out for the tipping point between MVR and guaranteed value.

Which? Money has also found that closed schemes can charge members as much as 11% for leaving. As with MVRs, providers justify these high charges by saying they're in place to protect people who remain in the scheme. One Abbey Life scheme we looked at charged an exit fee of £6,698 on a pension pot of £60,000, which seems completely disproportionate. Sun Life

### Time delays

While ordinary pension companies take an average of 8.7 days to transfer a pension to a new provider, according to the Department for Work and Pensions, closed providers can take up to a month. Which? Money found that just requesting – not even obtaining – basic information can take more than two



weeks, according to the independent financial advisers we spoke to. Delays can have a serious impact. Annuity quotes come with a guarantee period (usually 14 days) after which the quote is invalid. In today's climate of falling annuity rates, a delay of this length can wipe thousands off your pot.

Financial of Canada also charged one customer more than £2,000 to transfer a pot of £57,000. Thankfully, most modern pension schemes don't levy any sort of exit fee – stakeholder pensions aren't allowed to, and most other schemes opened since 2001 don't either. But all except one of the closed-book providers who responded to our survey told us they charge exit fees.

Closed schemes can charge high annual-management charges (AMCs) – more than 4% in some policies we examined. None of the providers surveyed were willing to reveal their AMCs.

### Slashed bonuses

Bonuses are cited as one of the positive features of older with-profits funds – for example, one Scottish Provident scheme pays a minimum of 4% a year. One Which? member told us that the bonuses from his policy are worth £25,952, and would take his pot at retirement from £72,024 to £97,966 – a valuable element.

But some providers stopped paying bonuses almost a decade ago. And many schemes have been winding down annual bonuses and offering larger bonuses on maturity – called terminal bonuses – which people who exit the scheme may not be able to access.

### Should I stay or should I go?

If you have an older with-profits or closed-book pension scheme, should you stay or transfer out? We summarise the options, but you should seek financial advice based on your circumstances

#### Stay

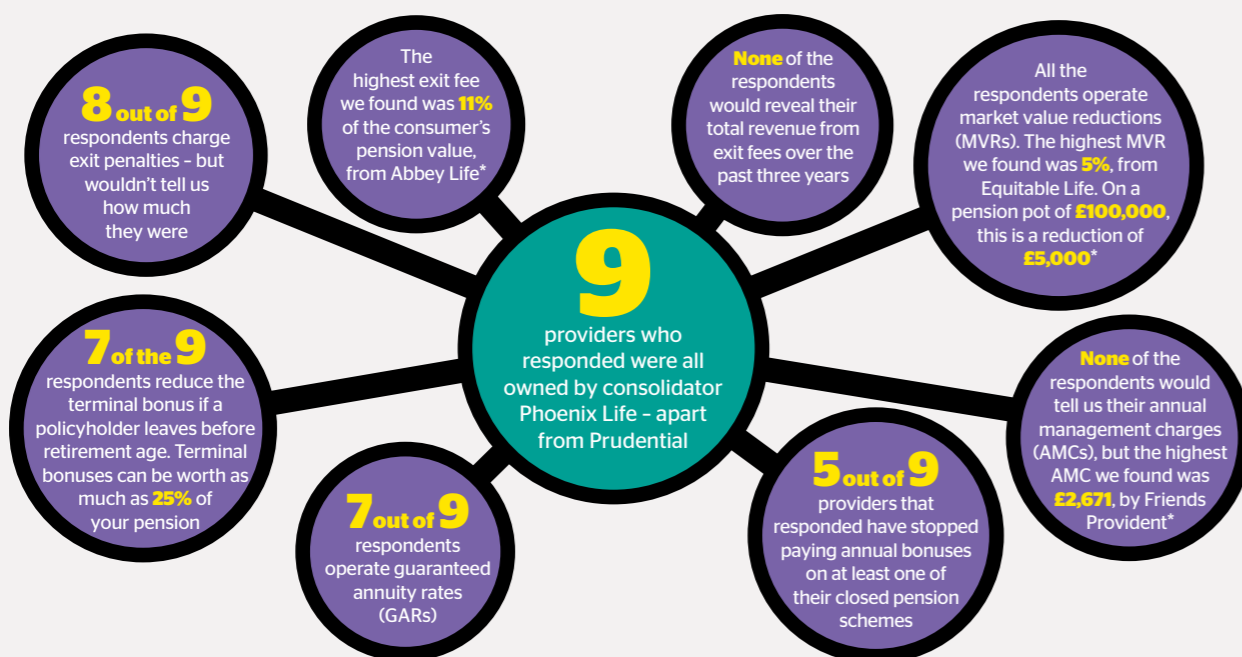
- Does your policy have a guaranteed annuity rate (GAR; see p34 for more)? If it's worth more than 5.5% (the current rate for a 65-year-old man), you might want to consider remaining in the scheme.
- Does your scheme offer annual or terminal bonuses? They can boost your pension pot, so might be worth staying for.
- Will the scheme charge an exit fee if you leave? Exit fees can be as much as 15% of your pension-pot value, which could be hugely detrimental.
- Will a market value reduction (MVR) be applied if you leave before your retirement date? You could be in for a nasty shock if so – Which? Money saw some MVRs that would reduce your pension pot by 5%, although the amount varies from scheme to scheme. MVRs are sometimes waived at retirement though, so you may be able to get out penalty-free.

#### Go

- Has the asset allocation of your scheme changed since you joined? Many schemes move investors into less risky asset classes, such as bonds, which means your returns will be lower.
- Are you invested in capital units? If so, you might be paying a whopping 4.5% annual charge on top of the standard 1% AMC. This could reduce your pot by hundreds of pounds a year.
- Do you feel in safe hands? Many Which? members said changes to provider names led to confusion about exactly who is looking after their pension pot.
- How many years do you have until your retirement date? If you're nearing retirement, you have probably built up more bonuses that are worth hanging on to. If you're further away from retiring, the weakness of the companies running the funds may mean lower returns – so you might be better off elsewhere.

## Opening the book on closed-book pensions

The results of our survey on charges, MVRs, bonuses and guaranteed annuity rates (GARs), sent to the 16 largest closed-book providers



\* Based on member feedback  
**Responded:** Pearl Assurance Plc; Prudential Assurance Company Ltd; London Life; Britannic Assurance Plc; Swiss Life; NPI Limited; Royal & Sun Alliance; Scottish Provident; Scottish Mutual.  
**Didn't respond:** Scottish Equitable; The Equitable Life Assurance Society; Clerical Medical Investment Group Ltd; Royal London Mutual Assurance Society Ltd; Aviva; Diageo Pension Scheme; Standard Life.

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### Which? works for you

We need a regulator who is prepared to get to grips with the issues surrounding closed-book pensions

When we asked the FSA why it was unable to take action on the high charges on closed-book pensions, it told us that all charges are fully disclosed in the policy documents – so policyholders should have been in a position to enter a scheme with their 'eyes open'. But despite this disclosure, these schemes operate in such a complicated way that it's hard to see how policyholders can make sense of how they work. Financial advice is scarce as many advisers are reluctant to make recommendations on closed schemes because of the amount of money and risk at stake. Which? Money would welcome more transparency for policyholders. The problems surrounding closed pension schemes are exacerbated by the fact the regulator doesn't seem to know everything it needs to. Which? thinks the regulator should raise awareness of the terms of the policies and exit penalties – and force providers to make this information public. This would be a step towards helping consumers decide whether they should stay or leave a closed scheme. The box, above, also looks at what you should consider before exiting.