

**Police Pension Scheme 1987**  
**Police Pension Scheme (Northern Ireland) 1988**

**Commutation on Retirement**

Author: Trevor Llanwarne, Sandra Bell

Date: 20 April 2011

## Introduction

Regulation B7 of The Police Pensions Regulations 1987 (SI 1987/257) and of The Royal Ulster Constabulary Pensions Regulations 1988 (NI SR 1988/374) states that a member entitled to an ordinary, short service, ill health or deferred pension may commute a portion of their pension for a lump sum. Additionally, regulation M2 (in England and Wales) or M11 (in Scotland) of The Police Pensions Regulations 1987 and regulation N2 of The Royal Ulster Constabulary Pensions Regulations 1988 states that a pension credit member may commute a portion of their pension.

The lump sum is the actuarial equivalent of the commuted portion at the date of retirement, calculated from tables prepared by the Government Actuary.

The purpose of this note is to provide the tables for commutation of pension to lump sum in the Police Pension Scheme (PPS) in England and Wales, Scotland and Northern Ireland.

This guidance supersedes any previous guidance or advice issued by GAD in connection with police pension commutation and is effective with immediate effect.

If administrators have any questions about how to use this guidance they should in the first instance consult published information or raise queries on the Police Pensions Administrators' Forum at:

<http://pensions.police.homeoffice.gov.uk/>

If the Forum does not help, administrators may contact the relevant Police Pensions Team at the Home Office, the Scottish Public Pensions Agency or the Department of Justice (Northern Ireland), as applicable. The Home Office, the Scottish Public Pensions Agency or the Department of Justice will seek input from the scheme actuary if necessary.

## Caveats

This note should not be used for any purpose other than to determine the commutation factor that should be applied to the amount of pension commuted to provide a lump sum in the PPS. For example:

- This guidance does not apply to exchange of lump sum for additional annual pension in the New Police Pension Scheme.
- This guidance does not apply to the trivial commutation of pension under regulations B8 and E4(3) of The Police Pensions Regulations 1987 and regulation 38 of The Police Pensions Regulations 2006 (and under the corresponding Scottish and Northern Ireland regulations).
- This guidance does not cover the calculation of the capitalised value of benefits for the purpose of determining death gratuities under regulation E3 of The Police Pensions Regulations 1987 and regulation 45 of The Police Pensions Regulations 2006 (and under the corresponding Scottish and Northern Ireland regulations).

This note should be considered in its entirety, not as individual sections which if considered in isolation, may be misleading, and conclusions reached by a review of some sections on their own may be incorrect.

This note only covers the actuarial principles around the calculation and application of commutation factors. Any legal advice in this area should be sought from an appropriately qualified person or source.

## Administration

1. The amount of PPS pension that can be commuted is subject to the limits set out in the PPS regulations. In most cases a quarter of the pension can be commuted. With some exceptions, an ordinary pension in respect of at least 25 but less than 30 years of service can be commuted to give a maximum lump sum of no more than 2¼ times the full amount of the gross annual pension. Please refer to the relevant set of Police Pension Scheme regulations for full details of the commutation limits applicable to members.
2. Police Pension Scheme regulation B10 describes additional restrictions on the level of pension that can be commuted in certain circumstances.
3. Restrictions on pension commutation are also imposed by the pension taxation regime under Finance Act 2004. Administrators must ensure that the payment of a lump sum in lieu of pension is compliant with the tax rules as well as with the police pension regulations. The main taxation restriction is that for a lump sum to be authorised under the tax rules it must not exceed 25% of the total value of benefits vested.
4. There are some scenarios where the 25% HMRC limit could potentially be breached.
  - A member with a commutation factor above 20 commutes 25% of their pension. This can be avoided by commuting a lower proportion of pension.
  - Allocation in accordance with Police Pension Scheme regulation B9

Please refer to HMRC guidance if such cases arise.

### PPS commutation – retiring from active service

5. For an officer retiring on pension directly from police service (and for pension credit members) the lump sum payable can be determined as follows:

pension given up × factor from table 1

Equivalently, the pension given up can be determined as follows:

lump sum payable ÷ factor from table 1

6. The examples on page 5 and 6 illustrate this calculation, including an example showing how it may be possible to prevent breaching the 25% HMRC limit.

**PPS commutation – break between leaving service and pension commencing**

7. For an officer retiring with a break between leaving service and pension commencing the commutation lump sum should be calculated as in paragraph 5 above in the following cases:
- If the pension commences at or above age 55; or
  - If the pension commences on grounds of ill health before age 55 and attracts full pension increases.
8. In other cases, that is where the pension commences before age 55 and the member is not immediately entitled to full pension increases, an alternative calculation may be needed. This guidance will be extended at a later date to cover these cases. If any cases arise before this guidance is issued, please refer to the Police Pensions Teams at the Home Office, the Scottish Public Pensions Agency or the Department of Justice (as applicable) for further information.



Trevor Llanwarne  
Government Actuary  
20 April 2011



Sandra Bell  
Fellow of the Institute and Faculty of Actuaries  
20 April 2011

Police Pension Scheme: Commutation on Retirement

## Example Calculations

This section provides two examples of the calculations described in this note.

### Example 1 – PPS: retiring from active service

Date of birth: 22 December 1961

Date pension commences: 22 December 2011

Pensionable Service: 25 years (excluding doubling)

Total pension payable: £20,000 pa

Age on day pension commences: 50 years

Commutation Factor = 22.10 (from table 1)

The member retires at age 50 with 25 years' service, so the maximum lump sum he can commute according to the PPS regulations is two and a quarter times the full amount of the pension.

$$\begin{aligned}\text{Maximum lump sum} &= 2.25 \times 20,000 \\ &= £45,000\end{aligned}$$

$$\begin{aligned}\text{Pension after commutation for maximum lump sum} &= 20,000 - 45,000 / 22.10 \\ &= £17,964 \text{ pa}\end{aligned}$$

### Example 2 – PPS: avoiding breaching the 25% HMRC limit

To illustrate how members may be able to avoid breaching the 25% HMRC limit by commuting less pension than the maximum available under the PPS, this example makes use of the current tax regime in force at the time of writing, in its most common form. Administrators should check whether there have been any changes to the tax regime, or whether any additional complexities apply, before undertaking individual calculations. Individuals may wish to seek financial advice regarding pensions and taxation.

Date of birth: 15 August 1959

Date pension commences: 15 August 2011

Pensionable Service: 30 years (excluding doubling)

Total pension payable: £30,000 pa

Age on day pension commences: 52 years

Commutation Factor = 21.50 (from table 1)

The member retires from active service at age 52 with 30 years' service, so the maximum lump sum he can commute according to the PPS regulations is a quarter of the full amount of the pension.

$$\begin{aligned}\text{Maximum lump sum under scheme regulations} &= 30,000 \times \frac{1}{4} \times 21.50 \\ &= £161,250\end{aligned}$$

Police Pension Scheme: Commutation on Retirement

Pension after commutation for the maximum lump sum permitted under scheme regulations  
 $= 30,000 - 161,250 / 21.50$   
 $= £22,500 \text{ pa}$

Under the current tax regime, the maximum lump sum that can be taken without being liable for a tax charge is 25% of the combined assessed value of the post-commutation pension and lump sum. To assess the value of the post-commutation pension HMRC currently use a factor of 20. As such:

Under HMRC's assessment the value of these benefits is therefore:  
 $= 22,500 \times 20 + 161,250$   
 $= £611,250$

25% of this is:  $= 25\% \times 611,250$   
 $= £152,813$

Therefore if the member commuted the maximum under the scheme regulations (to give a lump sum of £161,250), they would be liable for a tax charge, as this exceeds the maximum tax-free lump sum permitted (£152,813).

To calculate the pension that should be given up such that the member obtains the maximum lump sum which falls under the 25% HMRC limit, you should set the HMRC limit equal to the PPS lump sum; for this example that is:

The HMRC limit of:  $25\% \times [(30,000 - \text{pension commuted}) \times 20 + \text{pension commuted} \times 21.50]$   
 must be equal to  
 the lump sum from PPS  $= 21.50 \times \text{pension commuted}$

We need to find the amount of pension commuted that makes these two amounts equal. This can be found from:

Pension commuted  $= (20 \times \text{pension before commutation}) / (3 \times \text{commutation factor} + 20)$

Pension commuted  $= [20 \times 30,000] / [3 \times 21.50 + 20]$   
 $= 600,000 / 84.5$   
 $= £7,100.59 \text{ pa}$

To check; this would give a *tax-free* lump sum from the PPS of:  
 $= 7,100.59 \times 21.50$   
 $= £152,663$

The pension after commutation for maximum *tax-free* lump sum  
 $= 30,000 - 7,100.59$   
 $= £22,899.41 \text{ pa}$

The maximum tax-free lump sum permitted by HMRC would be:  
 $= 25\% \times [22,899.41 \times 20 + 152,663]$   
 $= £152,663$

The lump sum from the PPS does not exceed the HMRC limit.

Police Pension Scheme: Commutation on Retirement

**Table 1: PPS factors for commutation of pension to lump sum  
Males and Females**

Years	Age in years and completed months on day pension commences											
	0	1	2	3	4	5	6	7	8	9	10	11
<b>Below 48</b>	23.50											
<b>48</b>	23.50	23.50	23.50	23.50	23.50	23.50	22.40	22.38	22.37	22.35	22.33	22.32
<b>49</b>	22.30	22.28	22.27	22.25	22.23	22.22	22.20	22.18	22.17	22.15	22.13	22.12
<b>50</b>	22.10	22.08	22.05	22.03	22.00	21.98	21.95	21.93	21.90	21.88	21.85	21.83
<b>51</b>	21.80	21.78	21.75	21.73	21.70	21.68	21.65	21.63	21.60	21.58	21.55	21.53
<b>52</b>	21.50	21.48	21.45	21.43	21.40	21.38	21.35	21.33	21.30	21.28	21.25	21.23
<b>53</b>	21.20	21.18	21.15	21.13	21.10	21.08	21.05	21.03	21.00	20.98	20.95	20.93
<b>54</b>	20.90	20.87	20.83	20.80	20.77	20.73	20.70	20.67	20.63	20.60	20.57	20.53
<b>55</b>	20.50	20.48	20.45	20.43	20.40	20.38	20.35	20.33	20.30	20.28	20.25	20.23
<b>56</b>	20.20	20.17	20.13	20.10	20.07	20.03	20.00	19.97	19.93	19.90	19.87	19.83
<b>57</b>	19.80	19.77	19.73	19.70	19.67	19.63	19.60	19.57	19.53	19.50	19.47	19.43
<b>58</b>	19.40	19.37	19.33	19.30	19.27	19.23	19.20	19.17	19.13	19.10	19.07	19.03
<b>59</b>	19.00	18.97	18.93	18.90	18.87	18.83	18.80	18.77	18.73	18.70	18.67	18.63
<b>60</b>	18.60	18.57	18.53	18.50	18.47	18.43	18.40	18.37	18.33	18.30	18.27	18.23
<b>61</b>	18.20	18.16	18.12	18.08	18.03	17.99	17.95	17.91	17.87	17.83	17.78	17.74
<b>62</b>	17.70	17.67	17.63	17.60	17.57	17.53	17.50	17.47	17.43	17.40	17.37	17.33
<b>63</b>	17.30	17.26	17.22	17.18	17.13	17.09	17.05	17.01	16.97	16.93	16.88	16.84
<b>64</b>	16.80	16.77	16.73	16.70	16.67	16.63	16.60	16.57	16.53	16.50	16.47	16.43
<b>65</b>	16.40											