

## **JCC Circular 75 of 2008**

Ref: JG/LS

28 May 2008

Dear Colleague

### **CHANGE IN COMMUTATION AND EXCHANGE FACTORS - Information**

The purpose of this Circular is to provide JCC with information in relation to the change of commutation and exchange factors and to address some of the questions that are likely to be raised by members.

If, as may well be the case, further questions are raised, then an updated version of this Circular will be issued in due course.

It is anticipated that most questions will relate to the commuted lump sum payable under the Police Pensions Regulations 1987.

### **COMMUTED LUMP SUM UNDER POLICE PENSIONS REGULATIONS 1987**

#### **1. What is commutation?**

Commutation is where part of the entitlement to a pension for life is exchanged for a lump sum payable on retirement. This requires a calculation of the current value of the entitlement given up. The calculation is done using actuarial advice. The advice is set out in tables containing "factors". The level of the factors depends on age and life expectancy.

#### **2. What is the legal basis for commutation?**

Regulation B7 Police Pensions Regulations 1987 ("PPR 1987") allows an officer to commute part of their pension for a lump sum. That regulation sets out the maximum levels of commutation and the time limits.

Where an officer chooses to commute, the police authority reduces the pension by the amount given up and must pay the officer "a lump sum of such amount as is the actuarial equivalent of the surrendered portion of the pension at the date of his retirement, calculated from tables prepared by the Government Actuary."

The tables are not found in the PPR, but in separate guidance produced by Government Actuary's Department ("GAD").

#### **3. Why are the factors being changed?**

In short, mainly because life expectancy has increased. This means that officers are giving up more when they commute part of their pension.

#### **4. What changes are being made to the factors?**

There are three main changes:

- the factors are increased
- the same factors are applied to men and women
- the factors vary with months of age rather than age next birthday

#### **5. Can a member who commutes pension for lump sum under PPR 1987 be worse off as a result of the change?**

No. At all ages the new factors are higher than the previous ones. This means that the lump sum will be higher.

#### **6. Why are the same factors being applied to men and women?**

We are advised by our actuaries that while life expectancy does differ the gap has been narrowing in recent times and that a gender neutral approach is consistent with current trends in other schemes.

#### **7. What difference will the month by month factors make?**

Using annual factors, there could be potentially significant differences in the lump sum calculation depending on how the date of retirement related to birthday. There are now many more steps, and less dramatic differences in amounts.

#### **8. When do the new factors apply?**

The new factors apply immediately and are backdated to 1 October 2007.

#### **9. How does the backdating operate?**

The new factors will apply to any officer:

- who retired with an immediate pension on or after 1 October 2007; or
- whose deferred pension came into payment on or after 1 October 2007

This means that additional payments will be due to some retired officers. Details of the arrangements are set out in the Home Office Circular, but some of the main issues are dealt with in the questions that follow.

#### **10. How will backdating affect an officer who commuted 25% of their pension?**

The officer should be paid the additional amount, together with interest if appropriate (see question 12 below). The officer will have the option of receiving additional

annual pension instead of the additional lump sum. Any officer wanting additional pension should notify the police authority within one month of receiving the relevant letter. The Home Office Circular indicates that police authorities have the discretion to allow late notifications in exceptional circumstances.

**11. How will backdating affect an officer who was subject to the 2 ¼ times annual pension limit of their pension?**

The key point here is that the 2 ¼ limit still applies. If the officer commuted to the limit, then s/he will receive additional pension, which will be backdated together with interest if appropriate (see question 12 below).

In any case where the 2 ¼ limit applied but the officer did not commute up to the limit a lump sum will be paid up to the limit. The officer will have the option of receiving additional annual pension instead of the additional lump sum.

**12. When will interest be paid?**

The Home Office Circular indicates that interest will be paid in any case where lump sum or additional pension is not paid within three months of the date to which the entitlement is backdated.

**13. What does this mean for officers who have not yet retired?**

If they choose to commute they will either get higher lump sums than those currently payable, or have to give up less pension for the same lump sum as currently payable.

There should also be less need to retire very near to a birthday to maximise lump sum.

**14. What effect will this have on the RJW pensions calculator?**

It will be inaccurate for any officer retiring with a lump sum.

David Marsden at RJW is working on a revised version which will be issued as soon as possible.

**15. Do the changes affect any other part of the Police Pension Scheme?**

The new factors also apply to pension credit members' awards. They do not apply to the commutation of trivial awards. Other provisions of the PPR which relate to actuarial guidance are not affected.

**EXCHANGE OF LUMP SUM IN THE NEW POLICE PENSION SCHEME (NPPS)**

**16. What is the exchange of lump sum?**

NPPS has a different design to PPS. NPPS provides for an annual pension and lump sum as the standard benefit, rather than a pension part of which can be commuted.

NPPS does however allow members to exchange the lump sum for additional pension – in effect reverse commutation. This requires the valuation of a current lump sum as an additional pension for life, which requires actuarial factors.

### **17. What is the legal basis for the exchange of lump sum?**

Regulation 37 Police Pensions Regulations 2006 allows an officer to exchange all or part of their lump sum for additional pension payments. That regulation sets out the maximum levels of commutation and the time limits.

Where an officer chooses to exchange, the police authority withholds the lump sum in whole or part as appropriate pays to “additional annual pension payments of such amount as represents the actuarial equivalent of the surrendered lump sum... calculated from tables prepared by the Scheme actuary”

As above the tables are not found in the PPR, but in separate guidance produced by Government Actuary’s Department (“GAD”).

### **18. What is the impact of the changes?**

The changes will worsen the position, ie, surrender of the same amount will now “buy” less additional pension. This is because longer life expectancy means that the pension is likely to be paid for longer.

### **19. When will these changes take effect?**

They will apply to any officer who retires with an immediate pension on or after 1 July 2008 or whose deferred pension comes into payment on or after that date.

### **20. Is there any backdating?**

No.

## **MISCELLANEOUS**

### **21. Where can further information be found?**

The Government Actuary’s Department has produced guidance on Commutation and Exchange of Lump Sum which can be found at

<http://www.police.homeoffice.gov.uk/publications/human-resources/new-pension-docs/commutation-GAD-guidance>

In the forthcoming Home Office Circular, the text of this Circular can be found at

<http://www.police.homeoffice.gov.uk/publications/human-resources/new-pension-docs/circular-commutation-factors>

The Home Office has also produced a Q&A document on the new commutation factors which can be found at

<http://www.police.homeoffice.gov.uk/publications/human-resources/new-pension-docs/commutation-factors-qa>

**22. What should JBBs do if they have any further queries?**

Please contact the General Secretary.

Yours sincerely

Joe Grant  
General Secretary