

From: David Friend [<mailto:David.Friend@civica.co.uk>]
Sent: 27 June 2014 16:02
To: Terry Edwards
Subject: GAD guidance

Terry,

I promised during our telephone conversation from earlier this week that I would send an email which summarises the problem with GAD guidance "Limit on Additional Cash Commutation".

- Paragraph 2.11 on page 4 contains a link to [RPSM09104490](#);
- This RPSM page has a flowchart which contains formula that are not appropriate for the LGPS as they do not include a variable for a defined lump sum (as is required for any LGPS member who was active before 1 April 2008);
- The flowchart on RPSM09104490 does not tally with formula, in paragraph 2.9, on how to calculate the value of crystallised benefits where the member has in-house AVCs;
- The formula in paragraph 2.9 means the crystallised value for any in-house AVC (which is converted to an annuity) is now calculated differently from the example given in Example A3 of the GAD guidance 'Lifetime allowance and Additional Cash Commutation'. [This original GAD guidance is dated 18 June 2008 and is available from the Previous Guidance section of the Timeline Regulations Post 2008 GAD guidance page.] Why have GAD changed their interpretation?

My earlier email gives more detail and also shows an example of how the formula quoted on RPSM09104490 calculates an incorrect maximum tax-free cash lump sum given paragraph 2.9.

Regards,

Dave

David Friend | Pensions Calculation Developer | Civica UK Limited
Tel: 01132010832
e-mail: David.Friend@civica.co.uk | <http://www.civica.co.uk>

From: David Friend [<mailto:David.Friend@civica.co.uk>]
Sent: 30 May 2014 18:49
To: Terry Edwards
Cc: Tim Hazlewood
Subject: GAD Guidance - Limit on Additional Cash Commutation

Terry,

At the software suppliers meeting I pointed out that there was a link to RPSM09104490 which contained formulae which were not suitable for some members of the LGPS as there is variable for a defined lump sum.

Subsequent to the meeting, I discovered that the formula on RPSM09104490 will only work if any AVCs (which are used to purchase an annuity) are included at the fund value rather

than the crystallised value of the annuity pension. Paragraph 2.9 of the GAD guidance states that the crystallised value of benefits includes 20 times the GAD annuity pension. The attached spreadsheet contains one worked example which shows that one of the formula from RPS09104490 is not compatible with the statement in paragraph 2.9.

The figures in column E (in the black font) as far as row 29 demonstrate that formula A does not work. The figures in the blue font are based on my alternative generic formula. As you can see my formula works because the calculated maximum tax-free cash lump sum is $\frac{1}{4}$ of the value of crystallised benefits.

The middle formula on the right hand side is what you obtain when you plug a commutation rate of 12 and a relevant valuation factor of 20 into the generic formula. This formula appeared in the very first GAD guidance on how to calculate the maximum tax-free cash lump sum. The middle formula can be used if the member can take all of his pre April 2014 AVCs as cash. The last formula on the right hand side is the formula which can be used to calculate the maximum tax-free cash lump sum where the member has post March 2014 AVCs or orphan AVCs. This formula is also derived from the generic formula but with no pension element and no defined lump sum element. I have used the same letters as HMRC used on RPSM09104490 with the addition of a letter for the defined lump sum.

The delay in my response is partly due to an inability to think of an example which will meet the criteria for the other formula. In hindsight, I should have concentrated on providing examples for the other formula. I will forward examples of the other formula from the right hand side of the formula in due course.

There are some other points to bear in mind. The three formulae assume that a member will take as much cash from pre April 2014 AVCs as possible in the first instance. In other words, members will either convert part of the pre April 2014 AVCs to an annuity pension or commute part of their main scheme pension to a lump sum. That is, they will not do both. In the vast majority of cases I think this assumption will hold true. I did think there might be some rare instances where a member who is close to his LTA might take some of his AVCs as an annuity (especially where the annuity factor is less than 5) and commute part of his LGPS pension at 12:1. This is because both actions will reduce the overall value of crystallised benefits based on paragraph 2.9 of the Additional Cash Commutation.

I think paragraph 2.9 has implications for members who have primary protection, enhanced protection etc. or members who do not have any protection from the LTA and whose benefits exceed the LTA at the BCE date. I am more than happy to discuss any of the above further.

Cheers,

Dave

David Friend | Pensions Calculation Developer | Civica UK Limited
Tel: 01132010832
e-mail: David.Friend@civica.co.uk | <http://www.civica.co.uk>