

## **Annex B**

### **Example 1**

Consider a member registered for Primary Protection (PP) and Enhanced Protection (EP). The member is first treated under EP, and PP applies only once EP lapses. The member opts to take maximum commutation and has no other benefits in payment.

#### **Standard Lifetime Allowance**

2006-07: £1,500,000

2008-09: £1,650,000

At 5 April 2006, PPS details are as follows:

- Reckonable service : 27 years
- Final Pensionable Salary: £150,000
- Accrued PPS pension: £85,000 a year
- Capital value of benefit rights as at 5/4/06 = 20 x pension = £1,700,000

This is equal to the EP limit on the certificate issued by HMRC. He has also registered for Primary Protection and has a personal lifetime allowance of 113.33% of the standard LTA [ $113.33\% = 1.7m/1.5m$ ].

The member retires on 5 April 2009. During the 3 years to retirement, the officer retains his EP. At retirement, his PPS details are as follows:

- Reckonable service : 30 years
- Final Pensionable Salary: £180,000
- Pension before commutation: £120,000
- Applicable PPS commutation factor: 18.85

His earnings recalculation amount proves to be the best method of revaluing the EP limit. The EP limit is therefore £2,040,000 ( $= £1,700,000 \times (£180,000 / £150,000)$ )

The member's benefits can be split into two separate events, the first to which EP will apply, and the second to which PP could apply.

#### **FIRST BCE**

The maximum tax-free lump sum that the officer can crystallise under EP is:  
 $25\% \times \min(\text{standard LTA, HMRC value of benefits, EP limit})$   
 $= 25\% \times \text{standard LTA}$   
 $= £412,500$

This is obtained by commuting £21,883 ( $= £412,500 / 18.85$ ) of pension.

The maximum pension that can be crystallised without losing EP is:  
 $(\text{EP limit} - £412,500) / 20$   
 $= £81,375 \text{ a year}$

By taking this pension and lump sum at the first BCE the member uses up all his scope within EP and has crystallised benefits worth £2,040,000.

PPS pension rights (before commutation) crystallised at this BCE  
= £21,883 + £81,375  
= £103,258

## **SECOND BCE**

The member crystallises the remaining benefits on the same day as the benefits crystallised within the EP limit.

The member's personal LTA in this tax year is £1,870,000 (=113.33% x £1,650,000). He has already crystallised benefits worth more than this so has no remaining available lifetime allowance. All further benefits will therefore be subject to the Lifetime Allowance Charge (LTAC).

Uncrystallised PPS annual pension before commutation  
= £120,000 - £103,258  
= £16,742

Pension commuted so far is £21,883

Maximum commutation under PPS is £30,000 (= 25% of pre-commutation pension)

Further commutation lump sum that can be taken under PPS  
= (£30,000 - £21,883) x 18.85  
= £153,005

LTAC in respect of lump sum payable by scheme administrator  
= 55% x £153,005  
= £84,153

Commutation lump sum payable to member following LTAC  
= £153,005 - £84,153  
= £68,852

Remaining pension subject to LTAC  
= £16,742 - (£30,000 - £21,883)  
= £8,625

LTAC in respect of pension payable by scheme administrator  
= 25% x 20 x £8,625  
= £43,125

Reduction to pension following LTAC  
= 25% x £8,625  
= £2,156

Remaining pension following LTAC  
= £8,625 - £2,156  
= £6,469

## **SUMMARY**

The member's benefits at retirement are now therefore:

- annual scheme pension of £87,844 (= £81,375 + £6,469)

- lump sum of £481,352 (= £412,500 + £68,852)

The total LTAC payable is £127,278 (= £84,153 + £43,125 )

### **Example 2**

Consider the member in example 1 but now he does not opt for two BCEs, so EP lapses.

The member opts to commute 25% of his pension, which is the maximum permitted in PPS.

The member's pension before LTA charge is £90,000 (= 75% x £120,000)

The pension commuted is £30,000 (= 25% x £120,000) and so the member's lump sum before LTA charge is £565,500 (= £30,000 x 18.85)

Total HMRC value of these benefits is £2,365,500 (= £90,000 x 20 + £565,500).

The member's personal LTA in this tax year is £1,870,000 (= 113.33% x £1,650,000).

The maximum tax-free lump sum that the officer can crystallise under PP is:

$$\begin{aligned} &25\% \times \text{standard LTA} \\ &= £412,500 \end{aligned}$$

The maximum pension that can be crystallised within PP is:

$$\begin{aligned} &(\text{Personal LTA} - £412,500) / 20 \\ &= (£1,870,000 - £412,500) / 20 \\ &= £72,875 \text{ a year} \end{aligned}$$

All further benefits are subject to the Lifetime Allowance Charge (LTAC).

Lump sum subject to LTAC

$$\begin{aligned} &= £565,500 - £412,500 \\ &= £153,000 \end{aligned}$$

LTAC in respect of lump sum payable by scheme administrator

$$\begin{aligned} &= 55\% \times £153,000 \\ &= £84,150 \end{aligned}$$

Pension subject to LTAC

$$\begin{aligned} &= £90,000 - £72,875 \\ &= £17,125 \end{aligned}$$

LTAC in respect of pension payable by scheme administrator

$$\begin{aligned} &= 25\% \times 20 \times £17,125 \\ &= £85,625 \end{aligned}$$

Reduction to pension following LTAC

$$\begin{aligned} &= 25\% \times £17,125 \\ &= £4,281 \end{aligned}$$

## **SUMMARY**

The member's benefits at retirement are now therefore:

- annual scheme pension of £85,719 (= £90,000 - £4,281)
- lump sum of £481,350 (= £565,500 - £84,150)

The total LTAC payable is =  $55\% \times £153,000 + £85,625 = £169,775$

## **Comparison of examples**

The lump sum payable in both cases is the same (the difference of £2 in the quoted amount results from the rounding used in the examples). However, in the first example, by using EP through the split crystallisation events, the member receives £2,125 more pension and the LTAC is £42,497 lower.