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Dear Colleague

POLICE PENSIONS CIRCULAR No 2009/1
THE POLICE PENSIONS REGULATIONS 1987
THE POLICE PENSIONS (SCOTLAND) REGULATIONS 2007

This circular should be brought to the immediate attention of force personnel officers, Human Resource Managers and the Pension Managers and administrators of the PPS and NPPS.

Further Changes To PPS And NPPS As A Result Of 'A Day'.

- A. Introduction**
- B. Calculation of Lifetime Allowance Charges**
- C. Splitting Benefit Crystallisation Events**

A. Introduction

1. This Circular provides updates on a number of developments relating to police pensions in the light of 'A-Day' changes in 2006. Police authorities are required to note the information provided below, and take action where necessary.
2. Contact names, numbers and email addresses are provided at the end of the Circular if further clarification or other support is required.

B. Calculation of Lifetime Allowance Charges

3. This guidance provides clarification on the methods to be used when calculating the lifetime allowance charges that may be due on an officer's pension benefits.
4. Where an officer's total pension savings exceed the HM Revenue & Customs (HMRC) lifetime allowance (LTA) an additional tax charge falls due. It can be paid by the officer at the time that the pension commences or it can be paid by the scheme administrator. If paid by the scheme administrator the officer's ongoing police pension scheme benefits (and lump sum benefit if it also exceeds the LTA) must be reduced so as to recoup the tax charge.
5. Regulations 85 and 86 of the Police Pensions Regulations (Scotland) 2007 describe this. A similar rule will also be inserted into the Police Pensions Regulations 1987, with backdated effect from 6 April 2006.
6. The guidance and calculation method below apply to both the 1987 Police Pension Scheme (PPS) and to the 2006 New Police Pension Scheme (NPPS).

Meeting the tax charge

7. In order to calculate the incidence of the charge, it is necessary to determine how much of the lump sum and the annual pension are above and below the LTA. This depends on whether or not Primary Protection applies.
8. This guidance does not apply to a Benefit Crystallisation Event (BCE) where Enhanced Protection applies, because if Enhanced Protection applies then no LTA charge is payable. However, this guidance might apply to officers who originally registered for Enhanced Protection but where that status no longer applies. This could be because they have chosen to split their BCEs so that Enhanced Protection applies to only the first BCE. In that case this guidance would apply to any subsequent BCEs, where the applicable LTA will be zero.
9. For officers not covered by Primary Protection the amount of the lump sum above the limit is whatever remains once one-quarter of the available LTA has been subtracted from the total lump sum entitlement. If the lump sum entitlement is smaller than one-quarter of the LTA, then none of the lump sum is liable for a tax charge. The amount of the pension above the limit is the post-commutation pension minus one-twentieth of the residual LTA after the tax-free lump sum has been deducted. In cases where the lump sum attracts a tax charge the residual LTA will be 75% of the prevailing LTA. In other cases the residual LTA will be the prevailing LTA less the lump sum paid. See examples 1 and 2 in Annex B.
10. For officers covered by Primary Protection the amount of the lump sum above the limit is whatever remains once any tax free lump sum has been subtracted from the total lump sum entitlement. The level of lump sum that can be taken tax free should be calculated in accordance with HMRC guidance as it applies to members with Primary Protection, taking account of any rights to a lump sum of more than £375,000 on 5 April 2006. The amount of the pension above the limit is the post-commutation pension minus one-twentieth of the residual LTA after the tax-free lump sum has been deducted.
11. The tax charge in respect of ongoing pension is 25% of the excess of the HMRC valuation of ongoing pension benefits over the available lifetime allowance. HMRC uses a set factor of 20 to determine the overall valuation of post-commutation pension benefits. In addition, any lump sum over the limit is charged at 55%. (These two charging rates are equivalent if allowance is made for income tax at a rate of 40% on the pension element.)

12. The charge is paid by the scheme administrator to HMRC and can be financed in the following ways:

- by the officer paying the amount of the LTA charge to the police authority for onwards transmission to HMRC; or
- by reduction of the officer's pension lump sum by the amount of the LTA charge; or
- by a reduction to the officer's ongoing pension

13. A combination of the financing mechanisms could be used to meet the charge. However, the option of reducing the ongoing pension to meet the charge is available only in respect of the portion of the LTA charge that relates to ongoing pension. The portion of the LTA charge that relates to lump sum benefits must be paid out of the lump sum itself (or, equivalently, by a cash payment from the officer to the police authority). The reduction in lump sum/ongoing pension is the default arrangement. If an officer does not wish to incur this reduction, and wishes instead to pay the LTA charge straight away via the police authority, he/she must submit a request in writing to the police authority and must pay the police authority the full amount in question prior to the relevant benefit crystallisation event.

14. The LTA charge should be reported on the Accounting for Tax form APSS 302, whilst the tax itself is due at the same time that the form is due to be submitted to HMRC, i.e. 45 days after the quarter of the year in which the benefits are paid. HMRC does not need to issue an assessment to tax for this purpose. For more information see HMRC RPSM11300055 (<http://www.hmrc.gov.uk/manuals/rpsmmanual/rpsm11300055.htm>).

Reduction to officer's pension

15. The reduction to the officer's annual pension should be calculated as the applicable amount of the LTA charge, divided by 20. This is a factor determined by the scheme, but it happens to be the same as the factor used to value pensions for HMRC purposes.

16. The reduction to the officer's pension is permanent: it continues for as long as the pension continues to be paid, i.e. for the life of the officer.

Reduction to survivor's pension

17. A corresponding reduction is also made to any pension payable to a dependant after the officer's death. The reduction to the annual pension is calculated as follows:

1/8th of the lower of:

- (i) **MP – MPLTA**
- (ii) **the higher of:**
 - **2 x DP □ MPLTA**
 - **zero**

MP = member's post-commutation pension entitlement before any LTA reduction is applied

MPLTA = member's pension that falls within the member's LTA. This is 1/20th of the member's LTA in excess of any tax-free lump sum.

DP = dependant's pension entitlement before LTA reduction is applied

In most cases this will result in the reduction to a surviving dependant's pension being half the reduction to the officer's pension. In some cases, where the surviving spouse's pension is less than half of the officer's pension (eg widowers and civil partners), the reduction to dependant's pension will be lower, possibly nil.

C. Splitting Benefit Crystallisation Events

Introduction

18. On 6 April 2006, ('A-day') the system by which pensions are taxed changed substantially. This included the introduction of a new Lifetime Allowance (LTA) as an amount within which an individual's total pension benefits will not be subject to an additional tax charge, the lifetime allowance charge (LTAC).
19. It is, however, possible for officers to protect their pension rights from the LTAC up to a certain point, if they consider that their pension will exceed the LTA over the course of their career.
20. This guidance outlines a new arrangement whereby officers with high levels of pension savings are able to split their benefit crystallisation events to make best use of the protection rights and ensure that they do not have to pay more taxation than is necessary. This guidance is for immediate implementation.
21. Under this guidance *all* officers, not solely those who have high levels of pension savings, are able to choose to split their benefit crystallisation events, regardless of whether their benefits exceed the LTA or not.

Lifetime Allowance

22. The Lifetime Allowance is the amount within which an individual's total pension benefits will not be subject to an additional tax charge. The Lifetime Allowance has been set for future tax years as follows:
 - 2008/09 - £1.65m
 - 2009/10 - £1.75m
 - 2010/11 – 2015/16 - £1.8m
23. For both the Police Pension Scheme (PPS) and the New Police Pension Scheme (NPPS), the value of retirement benefits coming into payment, as assessed for LTA purposes, is calculated as 20 times the annual pension plus any lump sum.
24. The LTA covers benefits in all pension schemes. At the "**benefit crystallisation event**" (BCE), that is the point when benefits come into payment, officers must inform the police authority of any other benefits already in payment, providing the amount of LTA that has already been used by benefits that crystallised on or after 6 April 2006 and the level of benefits in payment at 5 April 2006 for benefits that crystallised before that date. The administrators can then determine the amount of LTA that remains. However, to prevent unnecessary delays to the process, officers should notify police authorities of the amount of LTA that has already been used when advising of their intention to split their BCEs under the PPS or the NPPS.

25. Unless the member has protection, any amount above the LTA will be subject to the LTAC. For benefits above the LTA paid as pension, the LTAC is 25% (and income tax is payable on the remaining pension). On lump sums, the LTAC is 55% (with no further tax payable).

Methods of Protection

26. The LTA will not affect most police officers. However, some high-earning officers may exceed the LTA – for more detail see Annex E of Police Circular 3/2006 (*Police Pensions: 'A-Day' And Changes to Police*

<http://sppa.gov.uk/police/documents/PoliceCircular2006-3.pdf>

27. Her Majesty's Revenue and Customs (HMRC) has provided two methods of protection for individuals who had already built up high levels of pension savings by 5 April 2006.

28. **Primary Protection:** An officer with pension rights with a value of more than £1.5m at 5 April 2006 is entitled to permanently augment the standard LTA. The officer will have a personal LTA that exceeds the standard LTA by the same proportion as that by which his pension rights valued at 5 April 2006 exceeded £1.5m. Any amount over the individual's personal LTA is not protected from tax.

29. **Enhanced Protection (EP):** Application for this protection is open to all officers, regardless of whether they exceeded the LTA prior to 5 April 2006. It provides protection for rights built up before 6 April 2006 from the LTA charge (up to an appropriate limit), even if they exceeded the LTA at 5 April 2006, when these rights come into payment. In addition, the **annual allowance charge** does not apply in relation to the individual for any completed tax year during which enhanced protection is retained. Enhanced protection is lost if **relevant benefit accrual** occurs, i.e. when the value of the benefits crystallised exceeds the **appropriate limit**.

30. The appropriate EP limit is calculated as the greater of the value of pension rights on 5 April 2006 adjusted in the following three ways:

- a. Increased by 5% compound per annum since 5 April 2006; or
- b. Increased in line with the Retail Prices Index since 5 April 2006; or
- c. Recalculated using final pensionable pay at the BCE, i.e. allowing for the increase in pension value resulting from an increase in salary, **not** from further accrual of service, since 5 April 2006. This is known as the earnings recalculation amount. (Although it is of general application this is particularly important for officers with 30 years' service by 5 April 2006, who expect that their salary will rise between 6 April 2006 and retirement, whose police pension rights can be fully protected from LTA charges. The officer must keep paying the 11% contribution towards the pension scheme in order to maintain the link between their pension and their current salary.)

31. If the EP appropriate limit is exceeded at the BCE, then relevant benefit accrual has occurred and enhanced protection is lost. Benefits will be subject to the standard LTA, or personal LTA if the officer has primary protection. If the EP limit is the earnings recalculation limit and the officer has accrued additional years of service after 5 April 2006, then in most cases, the value of benefits at retirement will exceed the EP limit and enhanced protection will be lost if all benefits are crystallised in a single event.

32. Enhanced protection can be lost by relevant benefit accrual only at the point when benefits actually come into payment. Enhanced protection can also be lost in other circumstances, for example if an individual, or employer, makes contributions to a money purchase arrangement

(such as a stakeholder pension or Additional Voluntary Contribution fund) after 5 April 2006. It is the individual officer's responsibility to notify HMRC if enhanced protection is lost.

33. The individual also loses protection from the annual allowance from the start of the tax year in which enhanced protection is lost.
34. Police authorities are reminded that the decision to apply for either primary or enhanced protection depends on the personal circumstances of each officer. Neither the SPPA nor police authorities are able to advise officers in this matter. Officers may wish to seek independent financial advice if they are unsure whether to register for protection.
35. Police authorities are also reminded that if an officer wishes to register for either of these protection schemes, the individual must inform HMRC, using the appropriate form, APSS 200, on or before **5 April 2009**. The form can be found on the HMRC website at:
www.hmrc.gov.uk/pensionschemes/protection.htm.
36. Further explanation of these protection measures may be found in HMRC's Registered Pension Schemes Manual, available at:
<http://www.hmrc.gov.uk/manuals/rpsmmanual/index.htm>.

Splitting the Benefit Crystallisation Event

37. It is not possible for an officer to waive their entitlement to the part of the pension that would cause the EP limit to be exceeded. The Department for Work and Pensions has stated that this would be an illegal practice. It is also intended to discontinue the option for officers to allocate part of their pension to increase the level of benefits payable to a dependant upon their death. This does not mean that existing allocations will be revoked; members will simply now not have the ability to make new allocations. However, the removal of this ability to allocate can only be implemented once the relevant amendments to the regulations have been made – police authorities are advised not to change their approach to allocation until further notice of the required regulation amendment.
38. We are implementing with immediate effect an arrangement to allow officers to use enhanced protection to its maximum effect so as to limit the tax payable. Members of both the PPS and the NPPS will now be permitted to receive their pension benefits upon retirement in stages, a practice known as splitting the benefit crystallisation event.
39. This will be of particular benefit to an officer who has built up further 60ths since 5 April 2006 and would exceed his or her EP limit if all the pension benefits were crystallised in a single event. At the first stage, benefits up to the EP limit would be brought into payment, thus not breaching enhanced protection. The officer would then receive his or her remaining benefits in the second stage (and any further stages). The second stage would result in relevant benefit accrual and trigger the loss of enhanced protection. Benefits taken at this stage (and any further stages) would then be subject to the standard LTA (or personal LTA if primary protection applies). Crucially however, the portion of benefits between the standard LTA and the EP limit would not be subject to the LTAC because, at the benefit crystallisation event in the first stage, enhanced protection is still valid. Each police authority pensions administrator is responsible for conducting the relevant benefit accrual test, and will calculate the tax accordingly.
40. Officers must notify their police authority in writing within 4 months prior to their retirement, and no later than their last day of service, with their request to split their BCE. Police authorities may exercise discretion to allow officers to give notification of their request earlier than 4 months before their last day of service. The officer must also specify at this time the amount that he or

she wishes to receive as pension and the amount to be commuted for a lump sum at each separate stage. The total LTAC payable and the remaining pension and lump sum will depend on whether pension is commuted at the first or subsequent BCEs (or the split between the two if commutation occurs at both events).

41. There are no limitations on the sequence of BCEs, apart from the fact that the Pension Commencement Lump Sum BCE must always occur immediately before the BCE of the associated pension. Police authorities should be aware that according to HMRC guidance, the payment of a retirement lump sum and the payment of a retirement pension should be seen as **separate** BCEs.
42. Benefits received at the second stage (and any further stages) can occur on the same day as the initial BCE, although the police authority may exercise discretion in allowing later payments as and when requested. Police authorities are reminded that pensions administrators must have in place suitable mechanisms so that, for audit purposes, each BCE can be distinguished from one another. HMRC have advised that there is no set method that pensions administrators must adhere to. Police authorities are therefore recommended to develop local procedures to ensure compliance with HMRC rules. In addition, each officer's decision to split their BCEs should be set out in a written agreement with the police authority. Police authorities should seek legal advice on such an agreement to ensure it is enforceable.
43. There may be cases where individuals have previously registered for both primary **and** enhanced protection, and retain dormant primary protection whilst their enhanced protection is still valid. If enhanced protection is lost or surrendered, the individual is still entitled to rely on his/her primary protection and the associated personal lifetime allowance. The individual must notify HMRC, who will issue the individual's primary protection certificate as proof of protection. There is nothing to prevent administrators from paying further BCEs on the officer's word that he/she has primary protection before receiving this certificate (i.e. on the same day as the other BCEs and the loss of EP), but administrators would risk being liable for a scheme sanction charge if HMRC later confirmed that the officer in fact did **not** have primary protection, and that there was an overdue tax charge payable. We would **strongly advise** that any further BCEs should **not** take place until the pensions administrator has received the certificate. In these circumstances, police authorities must ensure that members are aware that all BCEs may not occur on the same day.
44. If enhanced protection is lost, and the police authority pays the lifetime allowance charge on the officer's behalf, the pensions administrator must account for and pay it under the next quarterly Accounting for Tax return. Payment of the tax due should be made at the same time as the Accounting for Tax return is submitted. Further information may be found at HMRC's Registered Pension Schemes Manual, available at <http://www.hmrc.gov.uk/manuals/rpsmanual/index.htm>.
45. Forces may exercise their discretion when considering how many extra crystallisation events an officer may request. Forces must bear in mind the administrative time and costs that would be incurred if an officer requests more than 2 payment stages, and should consider each case accordingly.
46. Officers must be aware that the police authority bears no liability for any loss of income as a result of staging payment of the pension. Police authorities are not empowered to give individual officers financial advice; therefore officers are strongly recommended to seek independent financial advice before making a decision.

Officers who do not exceed the LTA

47. In order to ensure that there is equality across the forces, officers whose pensions do not exceed the LTA will nevertheless be able to request to receive their pensions in separate stages. However, the advantages of doing so are not clear, therefore officers are strongly advised to seek independent financial advice before making such a decision, as police authorities are not permitted to give individual guidance.

For further enquiries on any of the issues covered in this Circular, please contact:

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Yours sincerely

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View [ANNEX A.doc](#) attachments here:
[ANNEX B.doc](#)

