

### Commutation

The LGPS regulations allow the commutation of 'small pension pots' under various pieces of overriding legislation\*. The new Freedom and Choice in Pensions legislation provides further flexibility in respect of commuting small pensions, the most notable being that some members of the Scheme can commute small pension pots from age 55 (previously age 60).

The LGPS regulations set out that the Fund may make the following payments:

1. A commutation payment (where the value of LGPS-only small pension pots must not exceed a lump sum payment of £10,000)
2. A trivial commutation lump sum (where the total actuarial value of all LGPS and non LGPS small pension pots does not exceed £30,000)
3. A trivial commutation lump sum death benefit (where the value of all LGPS death benefits does not exceed a lump sum payment of £30,000)

*\*The LGPS regulations set out that the above terms are defined, in the case of (2) and (3), within the Finance Act 2004 and, in the case of (1), within the Registered Pension Schemes (Authorised Payments) Regulations 2009.*

The principle of commutation relates to converting a 'small' pension entitlement into a one-off cash lump sum payment to be made by the Fund, effectively discharging any further liability.

### Current Policy and Practice

The Fund's current policy is to commute small pensions where they meet the relevant criteria. However, in practice commutation has been both age limited and inflexible and consequently current practice, as opposed to the actual policy, has been to include reference to commutation within the normal retirement process but not to offer commutation in isolation. The information required to satisfy the trivial commutation lump sum criteria shown at 2. above is particularly difficult to obtain and assess.

### Potential Change

In the light of the intention to increase flexibility provided by the new freedom and choice in pensions legislation, it would appear to be appropriate now to reinforce the Fund policy to commute small pensions where the relevant criteria are met. It should be noted that it would not be possible to 'impose' commutation as specific information must be obtained from the scheme member in order to commute.

In reinforcing commutation as the Fund's standard offer where the relevant criteria are met, there is no doubt that this would result in a reduction in administrative effort in terms of processing a commutation as opposed to processing an actual retirement, and including the additional ongoing effort

involved in maintaining pensioner payroll records. In addition it is clear that discharging any future liability would also be beneficial to the Fund. Day to day processing of commutation payments as business as usual should not result in any significant cashflow issues.

However, current practice has resulted in a significant number (around 10,000) of pensioners and deferred pensioners with very small pension entitlements that could potentially be commuted. The Fund Actuary has been asked to consider the potential impact on both the Fund's cashflow and liabilities, of carrying out an exercise to commute these pensions. Clearly the cost of undertaking such an exercise would need to be weighed against the benefits of potentially discharging the ongoing liability in full but nonetheless the affected pensioners and deferred pensioners could be offered the option to commute in line with future practice.

It is also possible to commute pensions payable to a Child dependent. Children's pensions can be paid up to age 23 so long as the child is in higher education. Assumptions would need to be made in calculating a commuted children's pension as to how long they will be in higher education, but again it would be beneficial to the Fund to commute where possible.

### **Recommendation**

That a policy be adopted where:

- Commutation is the Fund's standard offer when a member retires or leaves the Scheme, where the pension value satisfies the £10k commutation criteria described at 1. above
- All other retirement/leaver cases are offered the option to commute where possible i.e. where they satisfy the criteria described at 2. and 3. above.
- Child dependant pensions will be commuted where possible.
- Where a child is aged 16 or over and still in full time education, the commutation will be based on an assumption that the pension would be paid until the age of 23.
- In respect of certain protected members, it may be possible to pay an ill-health commutation, and the policy would continue to be that this provision be applied where possible.

In addition, following consideration of advice from the Fund Actuary, a one-off exercise will be undertaken with a view to commuting current pension and deferred pensions where they satisfy the criteria described at 1. above.