

Taking a lump sum

A guide for DB members

One of the options you have at retirement is a tax-free cash lump sum and a reduced Scheme pension. Under this option, you give up some of your Scheme pension in exchange for a tax-free lump sum. Your monthly pension payments are then reduced accordingly.

How is the tax-free cash lump sum calculated?

HMRC has strict rules about the maximum tax-free cash you can receive; and broadly, this will equate to 25% of the overall value of your benefits. There may be further restrictions on the maximum you can take, but the Scheme administrator will tell you if this applies to you.

When you take a lump sum, you give up some of your annual Scheme pension and your monthly pension payments are reduced accordingly. We calculate the amount of annual Scheme pension you give up by dividing your lump sum value by the Scheme's commutation factor, which depends (amongst other things) on your age at the point of commutation. The commutation factor represents the amount of cash you would receive for each £1 of annual Scheme pension that you give up. For example, if the commutation factor is 10, for every £1 of annual Scheme pension you give up, you would receive a lump sum of £10.

How are the commutation factors calculated?

The Trustee sets the commutation factors on the advice of the Scheme Actuary, taking into account the expectations about investment returns on the Scheme's assets, levels of future pension increases and how long members will live. These expectations can change from time to time, and so the Trustee reviews the commutation factors regularly, which means they are subject to change at any time and could go either up or down in the future.

What happens if the commutation factors change?

Changes to the Scheme's commutation factors can have an impact on the maximum tax-free lump sum and remaining annual Scheme pension that are available to you when you retire.

If the commutation factors increase, the maximum lump sum you can take and your annual Scheme pension will be higher; but if they decrease, the maximum lump sum and your annual Scheme pension will be lower. However, you should also note that your lump sum and annual Scheme pension can also change if your date of retirement changes, because the commutation factors vary by age at retirement (because the younger you are at retirement, the longer your pension is expected to be paid for).

How often do the commutation factors change?

Commutation factors are reviewed regularly, at least once a year, or more often if needed, e.g. following big changes in the investment markets. However, the review does not necessarily mean that the commutation factors will change, and the Trustee does not have to inform members every time there is a review or a change in the factors.