

## **Briefing on Outcome of the Public Sector Pension Schemes Consultation**

Below is briefing and FAQ's relating to the Response published by DOF in relation to the Public Sector Pension Schemes Consultation.

### **Background:**

In 2015 reformed pension schemes were introduced across all the main public service workforces. The reforms included a policy of transitional protection that meant members closest to their Normal Pension Age (NPA) stayed in their legacy schemes.

The Court of Appeal in England and Wales later found this transitional protection to be discriminatory against younger members in the judicial and firefighters' pension schemes. The Westminster Government accepted that the judgment also had implications for the other public service pension schemes, as they all contained similar transitional arrangements and this would require a remedy. The devolved public service schemes contain identical transitional protections to equivalent schemes in GB and legal advice confirms they must be similarly remedied.

The Department of Finance has been working to address the discrimination. Simply putting all members back into their legacy schemes, would leave some members worse off – particularly lower or middle earners who are often better off in the reformed schemes. Therefore, the final policy design needs to allow members a choice of which scheme is better for them.

The Department of Finance ran a public consultation from 19 August to 18 November 2020 to gather stakeholder views on two policy proposals – a Deferred Choice Underpin or an Immediate Choice exercise.

The Department of Finance response to the consultation now announces its final policy proposal, to introduce a Deferred Choice Underpin and to move all affected public service employees into the reformed schemes from 1 April 2022.

### **Consultation Outcome**

The public service pension consultation response sets out how the Department of Finance proposes to remove the discrimination identified by the courts in the way that the 2015 reforms were introduced for some members.

Following a public consultation, it has been decided that affected members will receive a 'deferred choice' of which pension schemes benefits they would prefer to take at the point they retire, and this will apply across the majority of the main public service pension schemes.

Members will be able to choose to receive legacy pension scheme benefits, or benefits equivalent to those available under the reformed pension scheme, for service between 2015 and 2022. Not all members are better off in the legacy schemes, so it is important that individual members can choose which scheme benefits they want to receive.

From 1 April 2022, all those who continue in service will do so as members of the reformed schemes, regardless of age, meaning all members will be treated equally in terms of which pension scheme they are a member of.

### **Key Messages from the Response Document:**

When reformed schemes were introduced in 2015 those within 10 years of retirement were allowed to remain in their existing pension schemes. The court of Appeal in England and Wales found this to be discriminatory against younger members of judicial and firefighters' pension schemes. The Department of Finance is taking steps to remove the discrimination across the devolved public service schemes.

The Department of Finance published a consultation in August 2020 as part of that process. The consultation sought views on two methods for addressing the discrimination. Having considered the responses to the consultation, Department for Finance proposes to implement a '**deferred choice underpin**' (DCU) which was the approach favoured by the majority of respondents.

This means individuals, who were members of a public service scheme immediately before 1 April 2012 and were subsequently moved into the reformed pension schemes on or after 1 April 2015, will firstly be placed back into their legacy pension scheme in relation to any continuous period of service up to 31 March 2022. All members with relevant service in the legacy schemes between 1 April 2015 and 31 March 2022 will receive a choice at the point at which they retire whether to take legacy pension scheme benefits or reformed scheme benefits in relation to that period. Where eligible members have already retired before the changes can be introduced, they will be provided with a retrospective choice backdated to the date payment of their benefits commenced.

Allowing individuals to make their choice at the point their benefits are paid means they will be able to make their decision knowing what their entitlement will be under either option, reducing the risk of the member making the wrong decision. Individuals will be provided with information to inform their choice.

Where individuals retire from the reformed schemes before the introduction of the deferred choice underpin, schemes will seek to offer a choice of benefits for the 2015 to 2022 period at retirement, where this is possible. In time it may be possible for schemes to revisit cases of reformed scheme members who have already retired ahead of the introduction of the DCU. However, there are still some complex issues

to be resolved before schemes are in a position to process these cases. Further details of this will be provided in due course.

In addition to this, the consultation set out that from 1 April 2022, all active members, regardless of age, will be members of the reformed schemes and the legacy schemes will be closed. This approach ensures that schemes will be sustainable and affordable in the future and that public servants will still continue to receive a favourable defined benefit index linked pension for their years of public service.

In a related measure the impact of any ceiling breaches that arise as part of the 2016 cost control valuations will be waived. Pending the outcome of the Government Actuary Department's review of the mechanism, it would be inappropriate to reduce member benefits based on a mechanism that may not be working as intended. However, any benefit increases due as a result of any floor breaches will be delivered. This means that no member will see a reduction in benefits as a result of the 2016 valuations.

## **FAQs:**

The questions below provide more information for individuals should they wish to find out more about the Department of Finance response. FAQ's, specific to the HSC Pension Scheme have been shared with Employers and Scheme members and have been published to the Scheme website on 02/03/2021.

### **1. Why did the reforms to the main public service pension schemes lead to discrimination?**

- The 2015 public service pension schemes reforms included a policy of transitional protection. This meant members closest to retirement stayed in their legacy scheme as they had the least amount of time to prepare for the changes.
- The courts later found this policy to be discriminatory against younger members in some schemes. Following the ruling, the Department of Finance has been taking steps to address the discrimination in all affected devolved public service pension schemes.

### **2. Do members need to submit a legal claim to receive any pension changes to address the discrimination identified by the courts?**

- No, members do not need to submit a legal claim to receive any pension changes addressing the discrimination.
- Any changes will be applied across the main public service pension schemes and apply to both claimants and non-claimants who are eligible members.

### **3. What steps have been taken so far to address the discrimination?**

- Since the judgment work has been ongoing on different methods to address the discrimination.
- The Department of Finance set out two proposals in a public consultation in August 2020 to gather views on which proposal would be better to remove the discrimination.
- Since the public consultation closed in November 2020, the Department of Finance has been working through all the responses and has now published its response setting out its final policy decisions. The discrimination will be addressed through a 'deferred

choice underpin' which will allow eligible members a choice when they retire, of which pension scheme benefits they would prefer to take for the remedy period.

**4. What is a deferred choice underpin (DCU) and why has this approach been chosen?**

- To address the discrimination identified by the courts, eligible members who were moved to the reformed pension scheme in 2015 (or later if they had tapered protection) will be moved back into their legacy pension scheme for the period during which the discrimination occurred, i.e. between 1 April 2015 and 31 March 2022.
- When those members, or members who were originally protected, reach retirement, they will then receive a choice of which pension scheme benefits they would prefer to take for the period. This is called a 'deferred choice'.
- The choice will be between the member's legacy pension scheme benefits and their reformed pension scheme benefits.
- Deferring the choice until retirement allows individuals to make their choice of which pension scheme benefits are better for them, based on facts and known circumstances as opposed to assumptions on their future careers, health, retirement and other factors. The level of both pension scheme benefits will be known at retirement.

**5. Who is in scope for these pension changes and will receive the 'deferred choice underpin'?**

- Individuals that meet the following criteria are in scope of the changes:
  - were members, or eligible to be members, of a public service pension scheme on 31 March 2012;
  - were members of a public service pension scheme between 1 April 2015 and 31 March 2022; and
  - the two periods above were continuous (or treated as continuous under the scheme regulations, including those with a qualifying break in service of less than 5 years).

**6. Why are members being asked to make a choice between their legacy and reformed pension scheme benefits?**

- The differences between the legacy and reformed pension schemes mean the set of benefits that is best for members depends on personal circumstances and preferences. This is why the remedy is providing members with a choice, to ensure they can choose which scheme benefits are better for them.
- Schemes will provide information to members setting out their entitlement under both options, so members will have a clear understanding of the benefits available to them.

**7. Why isn't the remedy solution just returning everyone to their old schemes?**

- The remedy cannot simply place all members into their legacy scheme without allowing them access to their reformed scheme benefits, because some members are better off in the reformed schemes.

**8. What are the differences between the legacy and reformed schemes?**

- All public service pension schemes have different arrangements, however, for most schemes the main changes between the legacy and reformed arrangements included a change from final salary to career-average pension schemes and an increase in normal pension age.
- The change to career-average means member's pensions are now calculated on their average salary throughout their career as opposed to their final salary.
- The reformed schemes were designed to make public service pensions more affordable and sustainable for the future, while still ensuring public servants received appropriate pension provision at retirement. The reforms created a fairer system. Although some members are better off in legacy schemes, the reformed schemes are more beneficial for others, particularly many lower paid members.

**9. Will members who had 'tapered protection' also be asked to choose between legacy and reformed scheme benefits?**

- Members who received tapered protection in 2015, or would have received such protection but for the provision that unlawfully excluded

younger members from transitional protection, will be offered a choice of whether to receive legacy or reformed scheme benefits in relation to any continuous service between 1 April 2015 and 31 March 2022.

- This will remove the discrimination that arose between older members who were subject to transitional protection and younger members who were not.

#### **10. How will people who retire before the introduction of the DCU be treated?**

- Members who have retired before the DCU is implemented and have a period of relevant service between 1 April 2015 and 31 March 2022, will be offered a choice once the legislative changes have been made to implement the DCU. The choice will be retrospective and backdated to the point that payment of pension benefits began.
- In some cases, it may be possible for schemes to offer members a choice before the DCU is implemented.
- However, the legislation that allows schemes to do this is limited in effect. It allows schemes to return eligible members who retired from the reformed schemes to the legacy schemes in relation to service after 1 April 2015 but does not allow for all consequential matters to be dealt with fully in all cases. So, for example, in cases where there are interactions with the tax system, perhaps where members have incurred or will incur tax charges or where contributions differ between the schemes, it might not be possible to address all these issues before new legislation is made to implement the DCU.
- Where possible, schemes will seek to offer reformed scheme members who retire before October 2023 a choice of legacy or reformed scheme benefits for the relevant period at retirement.
- In due course it may be possible for schemes to revisit cases of reformed scheme members who have already retired ahead of the introduction of the DCU.
- However, there are still some complex issues to be resolved before schemes are in a position to process cases - further details will be provided as soon as possible.

- In all cases where an individual receives a revised pension award, this will be backdated to the date their pension award relating to the remedy period was originally made.

**11. Will the survivors of eligible members who have died since 1 April 2015 also be asked to make a choice between the different pension schemes?**

- Where an eligible member has died since 1 April 2015, schemes will review these cases as a priority. Where the member retired from the reformed scheme, schemes will seek to revisit cases ahead of the introduction of the DCU where this is possible. Individual schemes will check whether a higher pension or lump sum amount would be due under the alternative scheme.
- In the case of any increase, schemes will inform surviving beneficiaries, and the higher amount will be paid with their agreement. If the higher amount is already in payment, the survivors will be notified.
- The choice between benefits will fall to the late member's surviving spouse or partner. If there are children also in receipt of a survivor pension, and the decision maker lives in a separate household to the child, any decision taken will not affect the child's pension. Where the child and decision maker live in the same household, the usual rules around total survivor benefits payable will apply.

**12. What was the other proposal set out in the consultation and why was this approach not chosen?**

- The other proposal set out the consultation was called an 'immediate choice' which would allow members to choose which pension scheme benefits they would prefer to take for the period between 2015 and 2022 soon after the point at which schemes implemented the changes.
- While this approach would have resolved the issue sooner, it would have placed higher risk on the member. This is because they would be basing their choice around assumptions on their future careers, health, retirement and other factors, rather than the facts and known circumstances that will apply at the point of retirement. This could have meant some members may have been much more likely to have chosen the scheme benefits that did not turn out to be best for them.



**13. Why is the period when members will be receiving a choice of which pension scheme benefits they would prefer only from 2015 to 2022?**

- Members will receive a choice for the period between 2015 and 2022 because 1 April 2015 is the date when the reforms were introduced, and 31 March 2022 will be the point at which the legacy schemes will be closed to future accrual.

**14. What pension scheme will individuals be a member of from 1 April 2022?**

- From 1 April 2022, all those who continue in service will be eligible to do so as members of their respective reformed pension schemes (i.e. those introduced in 2015, of which many are already members), regardless of age. This includes members who were previously covered by 'transitional protection'.
- This means that members will keep any service earned within the legacy schemes up until that date and will be able to access those benefits in the same way and at the same time as they are currently able to, but any pension benefits earned after will be within the reformed pension schemes.
- The legacy schemes will be closed to future accrual from 1 April 2022.

**15. Why will all members be in the reformed pension schemes only from 1 April 2022?**

- The reasons for the 2015 reforms still stand: the commitment to ensuring generous public service pension provision remains, but this has to be affordable and sustainable in the long term. The 2015 reforms aimed to achieve this, whilst also being fairer to lower and middle earners.
- The 2015 schemes that were introduced following the recommendations of the Independent Public Service Pensions Commission (the reformed schemes) offer generous pension provision, improve affordability and sustainability, and are fairer to lower and middle earners.
- The reformed schemes are some of the most generous available in the UK: backed by the taxpayer; index-linked; and offering guaranteed benefits on retirement; comparing very favourably to the typical private sector scheme.

- The reforms created a fairer system. The move from (mostly) final salary to career average pension means members accrue their pension at a typically higher annual rate based on their average salary. Although some members are better off in legacy schemes, the reformed schemes are more beneficial for others, particularly many lower paid members.
- The transitional protection policy, which gave rise to discrimination, will have been removed and, from 1 April 2022, all those who remain in service will do as members of the reformed schemes, treating everyone equally in this respect, and ensuring the aims of the 2015 reforms are met.

#### **16. Will these pension changes result in any tax changes for members?**

- The majority of members will see no change to their tax position over the remedy period.
- For a minority of members, the pension changes will cause their tax position to change, which could result in tax charges for the member, or the member becoming entitled to a reimbursement of tax previously paid.
- In some cases, the pension changes may mean that individuals will have to pay new or higher annual allowance charges, but typically only where their projected pension at retirement has increased. Adjustments to lifetime allowance charges may also be required, where retired members' accrual changes.
- Some members may also face changes in their contributions in respect of the remedy period, which may also affect their income tax position.
- Where a member has already retired, their total pension income may also change, and tax will be payable on any increase in pension.

#### **17. When will the pension changes be implemented and introduced?**

- Legislation is required to implement a DCU in the schemes to ensure that all eligible members are treated equally and are able to choose to receive pension scheme benefits from either scheme. Where necessary, payments will be backdated to 2015.
- Provisions for the deferred choice will be implemented by 1 October 2023 for all members. Schemes may implement provisions for DCU earlier where it is possible to do so.

- Where possible, schemes will also seek to offer a choice to members of the reformed scheme who retire before October 2023 before the legislation is implemented.

**18. What are the next steps after the consultation response?**

- Following the consultation response, new primary and secondary legislation is required.
- The intention is that the DCU will be implemented by 1 October 2023, or earlier where schemes are able to implement legislative change and processes ahead of that date.

**19. How has COVID-19 affected the project?**

- COVID-19 has not caused any major delays to the project timeline.