

Scheme Advisory Board
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Dear Amar

Pensions Challenge

The Police Pension Scheme Advisory Board for England and Wales and the Scottish Police Pension Scheme Advisory Board, working with representatives of stakeholders in Northern Ireland (whose SAB has submitted a separate response), appreciate the opportunity provided to make comments on the paper: Public Service Pensions-Addressing unjustified age discrimination in transitional arrangements to the 2015 pension schemes – working proposals. We have held three technical working group meetings to consider the two options: deferred or immediate choice, set out in the paper. We have also continued our discussion in correspondence.

To ensure that you are aware of all points made, we attach the notes of the three meetings and the helpful responses from officials to some of the points raised.

Our aim throughout has been to identify practical problems which may arise in applying either option and to note gaps in information which may be key to successful implementation. Overall, we believe that the paper seeks a binary response to a question where there are a number of related broad and complex issues at play and numerous dependencies and consequences, which may heavily influence choice, but where details are not available. Consequently, at this point it is not possible to provide a simple response.

As referred to in the Working Proposals paper requesting stakeholders' initial views, this response on behalf of our SABs does not represent final opinions and going forward should not be held as binding. Furthermore, constituent members may choose to submit their individual responses prior to commencement of the formal consultation process.

Overarching points

We appreciate that the formulation of the remedy is very much a work in progress, but it is essential to note that, while our collective opinion leads us to favour the deferred choice option

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for both technical and practical reasons, without further information and answers to the crucial questions raised we are not in a position to express a clear preference as between the immediate and deferred choice options.

Both options create opportunities for further challenge which we have sought to identify. We do not consider either to be without risk. Common to both options are:

- **Definitions** - There must be clear definitions of terms used in the consultation paper. For example, all will need to understand what is meant by the remedy period.
- **Information and communication** - There was considerable concern that no current players have the capacity or remit to offer advice to individuals. This will be crucial in either option, and the risk of expensive and possibly inaccurate advice being offered is a real risk. Has thought been given to establishing a limited life advice service on the lines of the Money Advice Service?

A large scale information exercise to support Immediate Choice would require significant automation by HMRC and Administrators, and Payroll to support the provision of information over a circa 7 year period of Pension Input Amounts, pension contributions and resulting tax adjustments. Pension tax is an extremely complex area and in the absence of clear proposals to streamline the provision of information across the workforce it would be prudent to focus on developing proposals that allow this workload to be spread over a longer period.

Having discussed the matter with a member of GAD, SAB members were unanimously of the opinion that it was vitally important that GAD should be commissioned by Government to produce an appropriate comparison calculator for use by members at the earliest opportunity. If possible, that calculator should incorporate both taxation and contribution adjustment implications in the comparison.

- **Feasibility –**

As set out in the document testing the ‘deliverability and technical feasibility with employers and administrators’, this is a key area of the process. The first point to note is the need to recognise the unprecedented range of work strands arising from any remedy:

- information exercise across majority of officer workforce,
- remedy implementation across majority of workforce including distinct workstreams covering urgent cases, ET related cases, inter and intra transferee workstreams,
- compensation process for ET claimants
- implementing post remedy arrangements
- new issues arising e.g. any subsequent discrimination claims

Given this, there is a need to develop proposals that consider the breadth of work strands required and the mitigations, rather than focus on alternative remedy models, as greater consideration of the overall change requirement may shape the resulting options.

At this stage there is not a critical path covering the above strands nor identification of the scale, lead-in time and duration of work strands, nor key dependencies (e.g. lead in-time on software development and establishment of final salary data link). Without visibility of this to aid modelling of the volume of work and peak workload there is limited ability to give assurance on the feasibility of implementing multiple work strands.

The proposals assume the introduction of choice for fully protected members. The utility of this strand of work seen against the importance and resource demands of other strands of work needs to be considered in the round.

Both Immediate Choice and Deferred Choice (as described with a 'move back' default treatment) require complex adjustments for the majority of officers within a short period of time. It is considered prudent to develop proposals which phase and spread this very high volume of work.

The capacity of Police Pension administration is a further important consideration in assessing the feasibility of undertaking multiple work strands at the same time alongside business as usual. It is important to highlight that as a locally administered scheme, and in this regard different from centrally operated schemes, the service does not have access to a sizeable central resource to co-ordinate and directly manage the implementation of these change projects. The breadth of outsourced and in-house provision and software providers brings complexity and risk to the implementation process. At this point some suppliers are leaving the police pensions sector. This may be in response to the growing complexity of pensions and hence there is a need to be prudent regarding the scope to increase Police Pension implementation capacity.

In the context of the above factors it is considered prudent to develop proposals which allow for the phasing and spreading of work over a longer period such that capacity can be developed over a longer time period recognising the capability and capacity of administrators and software providers. The impact of maintaining dual records for a longer period of time would also need to be considered alongside the scope to put in place more efficient processes to manage this.

- **Effect of the pause of cost cap** - At this point in time there is uncertainty regarding the impact of resolving the treatment of the cost cap and specifically the impact on pension Scheme accruals. In order for members to make a fully informed choice they need to be certain about the comparison they are making. This is not going to be possible until such time as there is certainty about the fate of the cost cap and the remedy that would have applied to its breach with effect from 1 April 2019. If the pause on the application of the cost cap mechanism is removed retrospectively then the accrual under the 2015 CARE Scheme will be 1/47 rather than 1/55.3 for the period

from 1 April 2019 until 31 March 2023. This may mean that even more members are inclined to choose benefits under the 2015 CARE Scheme than their former scheme for the remedy period. It is important a critical path is developed which shows how the resolution of the cost cap / pension accrual issue is factored into the valuation process and alongside the remedy process. This is essential so as to be able to inform scheme members of the level of accrual under the 2015 Scheme. Without this it would not be possible to implement the remedy.

In addition, it is essential for employers to have early sight of how valuation and the cost cap processes will be taken forward and operate in the future in order to assess likely impact on employer contributions and funding of contributions going forward.

- ***Effect of what would happen next*** - The ability to respond meaningfully to the document is limited by the lack of a model for post-remedy pension provision. If there were visibility on the principles of the post remedy arrangements e.g. operation of CARE scheme with adjustments limited to benefit accrual and contribution rates, it would be possible to gauge the overall considerations for scheme members and feasibility of implementation better. While appreciating that the purpose of the remedy is to correct the unlawful discrimination caused by the transitional protections, we cannot ignore the obvious question about the Government's intentions for the future of benefit provision for police officers once the remedy period comes to an end.
- ***Complication in the element of choice*** - It is clear to all involved that this is not just a simple choice between one basis of accrual or another for the member during the remedy period; many other factors are relevant and should be brought to the attention of members in a clear and accurate manner to ensure that when members make their choice, it is a fully informed one. In addition to potential adjustments to contributions, there are unanswered questions as to how amendments to income tax, national insurance contributions, annual allowance usage and lifetime allowance changes (including those with HMRC LTA protection certificates) will be addressed. The timescales for exercising immediate choice and working out the taxation need to be correctly aligned.

The immediate choice proposal is problematic from many perspectives. Officers are expected, under immediate choice, to balance up factors such as CPI growth, mortality rates, pay growth, future CARE Scheme accrual, contribution rates, automatic lump sum, choice of commutation lump sum, tax free limit on lump sums, pension age, actuarial reduction factors, when they are likely to retire and their chances of promotion in order to form a view on the most beneficial scheme. No matter how good the information and how qualified all the assumptions presented were, this is too complex a question to present. There is an argument also that immediate choice favours the older member, who will have a much clearer line of sight to his or her retirement.

CARE Scheme benefits accrued during the period may be expressed as a cash sum, since, at the end of the Remedy Period, accrued benefits will be known. Future CPI movement will not. In respect of final salary benefits, however, future salary progression will be unknown, and the impact of any final salary link provided will also be unknown. So, it is difficult to provide a realistic forecast of benefits in future on which the individual member might make a choice.

The main question posed by the consultation is when members should have choice. It relates solely to a 7 – 10 year slice of their pension saving. This ignores that, for an increasing number of members, life events are occurring each day to members in scope for the remedy and these issues will need to be addressed retrospectively. These crystallisation events do not require the exercise of choice to the same extent.

- **Double accrual** - This (along with the equivalent scheme for firefighters) is a feature which is unique to the PPS 1987. Our assumption is that the application of double accrual will continue to apply to those with in excess of twenty years of membership during the remedy period (including those being placed back into PPS 1987 as part of the remedy). However, as part of the transitional arrangements introduced alongside the 2015 CARE Scheme, weighted accrual for those transferring from PPS 1987 to the 2015 CARE Scheme also provided some redress for those being forced to switch scheme. As well as weighted accrual, those members also benefitted from the application of “final final” salary and the ability to access their PPS 1987 pension at an earlier date than under the 2015 CARE Scheme. When the remedy period ends, if those who have been in the PPS 1987 until that point are forced to move into a replacement scheme, whether that is the 2015 CARE Scheme or some other arrangement, will they be provided with these same compensatory benefits, i.e. weighted accrual, “final final” salary and early access? The availability or otherwise of such additional benefits after the end of the remedy period may well prove to be a relevant factor in the making of any choice in respect of the remedy period by such members.

The above reference to the application of “final final” salary will equally apply to the 2006 Scheme members.

- **Beneficiaries** - The benefits payable from the three police schemes on the death of a member vary. More specifically and problematically the PPS 1987, unlike the other two, does not allow for the payment of an adult survivor pension to an unmarried partner. The PPS 1987 also still provides for the cessation of a spouse's pension on remarriage, formation of a civil partnership or cohabitation. These differences take us into the emotive realms of members' domestic arrangements. Although not required as part of any remedy to the unlawful discrimination, does this situation present an opportunity to reconsider the possibility of the payment to unmarried partners under PPS 1987 and also the cessation provision in order to adopt a more modern and sympathetic approach? There is a further complication (mainly in respect of the

deferred choice option) in respect of any member who has died or dies within the remedy period: who exercises the choice on behalf of the deceased member- next of kin, legal personal representative? In both of those instances there is a distinct possibility of conflict of interest as the person exercising the choice may potentially be a beneficiary.

- **Guidance for administrators on how to process immediate cases** - How should retrospective pension growth be calculated and allocated for the remedy period, and how will the tax consequences of retrospectively exceeding the annual allowance be dealt with? In particular, whether the liability for tax charges as a direct result of the remedy process which would not otherwise have arisen would be borne by the Government as per the Milne v GAD judgement cases and the FPS 1992 contribution holiday.
- **Scale** - Has any work been done to assess the scale of the caseload? For example, if the deferred option were preferred, how many people over what period of time would need information provided to them?
- **Urgent cases** - There is an acknowledged need for cases to be dealt with as a priority where members have already retired; especially ill-health retirements, members who have died within the remedy period, and those who are about to retire.

Deferred option

- What is the end date for the remedy period?
- A unique provision in the police schemes is the ability to retire at 30/35 years' service; it is imperative that this provision is honoured regardless of how the remedy is ultimately applied.
- When will any contribution adjustment be made? If affected members are automatically moved back to their original scheme as part of the remedy, will member contributions be altered with immediate effect, and then adjusted at retirement (if the member opts for benefits under the other scheme)?

In relation to contribution rate adjustments, there ought to be flexibility for those officers who move into a higher contribution bracket.

- Page 3: *“There are tax implications and interactions with the ongoing litigation for both options that are still being worked through and may fundamentally impact member choice.*

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- If there are any additional costs incurred in resolving tax issues, who would bear costs for advice?
- Tax issues would inevitably affect the highest earners more.
- How would a pension debt or credit be dealt with? Would interest be received?
- There needed to be clarity about the interrelation of the handling of the cost cap breach, the impact of current issues on the next valuation and the implementation of the chosen remedy option.
- Members need to understand what the tax implications are before a choice is made. How will the issues be resolved or addressed? Will members be given the option to delegate their reporting responsibilities to pension administrators to notify HMRC of changes to their Annual Allowance/LTA/tax relief?
- Are HM Treasury going to do an actuarial valuation of the pension schemes taking into account the cost cap pause?
- How long will the pause in the cost cap continue? When the pause is ceased will the cost cap be reapplied retrospectively so that the breach will need to be remedied? Will the cost cap mechanism be reintroduced and if so, in what form?
- Moving forward how will actuarial valuations of the schemes be carried out? How do we have confidence that the cost of the remedy will be attributed fairly and not be borne disproportionately by ongoing and new members?
- If a decision is made to take a non-pensionable honorarium, can that decision be revisited? If any choices are made on assumptions which are later invalidated can they be revisited?
- Paragraph 10: Where do equitable rights start and finish? What do we call equitable treatment?
- Has HM Treasury taken into account the complexities of double accrual and variations in the way accrual has been handled (e.g. weighted accrual)?
- Paragraph 29: Why does the general principle of the remedy not just say that members should be better off?
- Paragraph 38: Clarification that if “pension debit” is exercised, this is not dealt with in the same way as scheme pays tax debits which are open ended, but rather that members only pay what they owe. Any outstanding Annual Allowance tax collected

by way of pension debit should cease once the outstanding sum has been paid, and there should be no interest charges.

- Where the member chooses to pay the recovery of outstanding contributions from their pension, they should have a choice to pay it from either their commutation/lump sum or post commutation reduced pension.
- What is the commutation worked out on?
- Annual Allowance tax inputs should now be calculated over the lifetime of the officer's service, for example 25 years equates to £1 million. Any greater pension input should then be taxed at the point of retirement.
- Officers transferred into the 2015 pension may well have contributed in good faith into a SIPP up to the £40k annual allowance. Consequently, any retrospective 1987 pension increases should now not attract any Annual Allowance/life time allowance.
- Paragraph 43: What is HMT envisioning after the remedy period?
- Is there any possibility of a government funded, time limited, advisory scheme?

Immediate option

- Paragraph 46: How can default choice be justified if members are supposed to make an informed decision? Has HMT considered the implication of implementing a default choice even where this would result in the member incurring additional charges (whether through contribution deficit, AA excess charge, breach of LTA protection including those who hold LTA protection certificates)?
- Paragraph 50: In relation to the cost cap 'pause' - When will members receive the increased accrual rate the SAB proposed to resolve in response to the initial results of the valuation which showed a breach to the cost cap floor?
- Paragraph 51: What kind/type of information will a member receive (before they make their decision) to help them make their decision? How will the government ensure they have the correct/sufficient information to allow members to make an informed choice and prevent any subsequent legal challenge?

Exactly what advice/assistance will members receive?

How confident can we be in relation to the development of a useful online tool?

Any statement about choice that is issued to members needs to include a clear indication of the taxation implications including changes to AA and adjustments to carry forward.

Do outstanding regulatory changes relating to the earlier pension schemes need to be addressed as a matter of urgency bearing in mind that these schemes will now remain “live” until the end of the remedy period?

- Paragraph 52: We need to see all the issues, not just the ‘summarised’ issues. What are the other issues referred to here?
- Paragraph 57 – 58: Would there be the option to meet any tax bill over a period of time rather than as a lump sum?

How would any contribution/refund/tax adjustment affect other benefits – e.g. Child benefit?

In relation to tax relief on over payments/underpayments - what is the detail of the ‘tax adjustment’ being suggested?

The Scheme Pays analogy is inappropriate. Any shortfall should be paid via an interest free loan or members ought to be able to pay in interest free instalments. Members should not bear the cost of any remedy to the discrimination.

Will interest be paid on refunds, as the member is not at fault?

- Paragraph 59 – 60: What happens if it is not possible to re-apply voluntary contributions paid to secure additional benefits under a different chosen scheme? Is a refund paid and will it include any compensation/interest?
- Paragraph 63 – 64: How will the timings be planned to allow a member to complete an accurate tax return? How will historic returns be corrected?

Annual allowance costs should be spread over the same number of years going forward, rather than be paid in that year. The retrospectively adjusted ‘carry forward’ needs to be used.

How will the annual allowance be recalculated – it should be in the relevant year and not in the final remedy year.

- Paragraph 65 – Members expressed views that communications should be delegated to the relevant schemes so that employers could be responsible for appropriate communication.
- Paragraph 66 – 67: ‘Tax assessments are ultimately the members responsibility.’ The individual should not be responsible for remedying the issues, especially as they are complex and costly and were not caused by the member. Where a Scheme Sanction

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Charge arises from the remedy this should be chargeable to the Police Pension Fund.

- Can members who have no other pensions delegate their tax responsibilities back to the scheme?
- How can there be confidence that immediate choice, if challenged by a member who later believes they were misled into making the 'wrong' decision, can be defended in the future?
- What will happen with transfer values? How will issues around pension sharing on divorce and the need for readjustment be dealt with? This applies similarly to those who have transferred their benefits to other Occupational Pension Schemes, given that schemes have no legal requirement to accept additional transfer value payments. In such circumstances who will the remedy ensure that these members are not adversely affected, not just in terms of pension accrual but AA implications.
- Would it be possible to allow an officer to apportion their membership during the 'remedy period' between their old scheme and the 2015 CARE Scheme?
- There is no reference to protection certificates for the LTA.

We look forward to responding formally, both as SABs and as separate representative groups, to the formal consultation and will be pleased to assist if any of our questions would benefit from further elaboration in the meantime.

Yours sincerely,

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