

Mr Peter McCallion
Finance Committee Clerk
Northern Ireland Assembly
Parliament Buildings
Stormont
Belfast
BT4 3ST

Private Office
2nd Floor
Clare House
303 Airport Road West
BELFAST
BT3 9ED
Tel: 028 9081 6216
Email: private.office@finance-ni.gov.uk

Your reference: 2021:404
Our reference: GM – 0736-2021

Date: 28 September 2021

Dear Peter

LCM: PUBLIC SERVICE PENSIONS AND JUDICIAL OFFICES BILL

Following its meeting of 22 September 2021, the Committee sought clarification in writing on a number of points in respect of the above named Bill. A response on each point is provided in sequence below:

1. Whether public sector scheme members will be required to meet the costs of the McCloud/Sargent remedy either through increased contributions or the redirection of scheme benefits that might have reasonably been expected to accrue to all public sector pension scheme members owing to breaches of the cost cap floor

The Public Service Pensions & Judicial Office Bill will legislate for increased payments to public service pension scheme members over the next five to six decades as a consequence of the remedy. The remedy on age discrimination increases the value of benefits payable through the higher entitlements now available to many members as if the McCloud discrimination had not occurred. These higher payments to members also increase the cost of the schemes (estimated at £680M in the case of the devolved schemes in NI). However, the Bill will include provisions to ensure that scheme members will not experience an increase in their contributions as a consequence of how these additional remedy costs are accounted for in the scheme cost control process for the 2016 valuations.

Each scheme operates an employer cost cap. Once scheme costs increase beyond a level which breaches this cap scheme members would normally become liable for additional costs, through increased contributions or a cut in the scheme accrual rate. This Bill makes clear provision that any cost breaches of the upper margin of the cost cap for the schemes will not trigger the corrective action which would normally be required to rectify such a breach, and which could otherwise result in an increase in

member contributions due to the inclusion of McCloud related costs in the 2016 valuations.

The provisional results of the 2016 valuations are still being processed in terms of the effect of the increased costs associated with the remedy. However indicative findings indicate significant breaches of the cost cap ceiling in at least 2 of the devolved schemes (Police and Firefighters). Rather than increasing member contributions the LCM for the Public Service Pensions and Judicial Offices Bill will provide an effective waiver which ensures members will not be required to meet these remedy costs through increased contributions.

The Bill also does not redirect scheme benefits which might have reasonably been expected to accrue to public service pension scheme members due to breaches of the cost cap floor, in order to meet the cost of remedy. The cost cap provisions in the Bill mean that any benefit improvements due to a breach of the cost cap floor, which result from the finalised 2016 valuations will be honoured, if they occur.

The Department acknowledges that indicative findings for the 2016 valuations which emerged in 2019 did indicate a potential breach of the cost cap floor. However these indicative findings can be now seen to be based on incomplete information on actual scheme costs and liabilities due to uncertainty about the full cost of remedy and future scheme design, and which at that point made any accurate or reliable assessment of those costs not possible.

In his recent report on the operation of the cost cap mechanism the Government actuary notes that in reality the cost of schemes rose at the 2016 valuations insofar as employers contribution rates increased by up to 9% of pensionable pay even before the impact of the cost control mechanism. The fact that the preliminary cost cap results for all schemes then showed a breach of the cost cap floor, which would further increase employer contribution rates and the cost to the taxpayer, was indicative of a perverse outcome insofar as the cost cap was evidently not operating in line with its original objectives to protect taxpayers from unforeseen costs and to provide stability to benefit levels¹.

The Government Actuary's report also indicated that the main drivers of change in the provisional cost cap outcomes which led to the apparent floor breaches were caused by lower pay increases and reduced life expectancy trends which had the effect of suppressing final salary costs for members of the legacy schemes. The Government Actuary noted this gave rise to a second perverse outcome insofar as the current cost cap rectification process only provides that improvement to benefits can be made in the reformed schemes. Therefore, members of the legacy schemes, wherein the cost savings were mostly attributed, would see no benefit from the floor breach. Whereas, members of the CARE schemes, where the risks associated with final salary had

1

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/993416/Cost_Control_Mechanism_-_GA_Review_-_Final_Report_-_27_May_2021.pdf

already been addressed through the adoption of the career average design and higher normal pension age linked to state pension age, would be the sole beneficiaries.

In this context it is clear that the benefits of the floor breach could not accrue to all public service schemes members and certainly not to those members in the schemes which had in the main effected the floor breach. Due to the contradictory operation of the cost cap mechanism against its original objectives then, the premise that the CARE scheme members should be 'reasonably expected' to have accrued benefit improvements from the 2016 valuations, is open to challenge.

The Government has now consulted on options to address the fundamental flaws in the operation of the cost cap mechanism with reference to its original objectives. These proposals are based on recommendations made in the Government Actuary's recent report. The main recommendation would remove the effects of the legacy schemes so that for its future operation the mechanism would only consider the reformed schemes. This would ensure consistency in that only cost movements in that scheme would lead to adjustments in contributions for its members. This would go some way to address the levels of intergenerational unfairness between legacy and CARE scheme members inherent in how the cost cap mechanism currently operates. The Government is expected to publish its consultation response shortly.

The Department acknowledges TUS concerns at the inclusion of the McCloud remedy costs in the 2016 valuations and that improvements in benefits have not followed the previously indicated provisional 2016 valuation results. However, it maintains the view that the apparent floor breaches previously indicated represent incomplete outcomes for the 2016 valuation process which cannot now reasonably be used as an accurate measure of costs leading to a justified entitlement to additional benefits. Whilst these preliminary results may have indicated potential floor breaches the cost cap work was not completed, and therefore no floor breaches actually occurred.

Finally It should also be emphasised that the decision for remedy costs to be included in the 2016 valuations is in itself not implemented by the Public Service Pensions and Judicial Offices Bill, but rather only the decision to waive the effects of any ceiling breaches that might occur as a result of the 2016 valuations when they are finalised, and which would unfairly penalise scheme members.

In the event that the Assembly declines to agree an LCM on this matter the relevant clauses for the devolved schemes will be removed and these protections will not be automatically applied. In this context the circumstances where devolved scheme members could most likely be made liable to meet the costs of any ceiling breach would occur if the Assembly chooses to take a separate approach on the remedy.

The Treasury has confirmed to the Department that where the NI devolved administration takes a separate approach on remedy and decides to adopt a policy that leads to higher scheme benefits compared to the policy adopted by the Westminster Government, any change in generosity compared to the England and Wales schemes will be required to feed into scheme valuations in the usual way, and imply higher contribution rates in the future. As set out in the Statement of Funding Policy for devolved administrations: *"Where a devolved administration wishes to offer more generous terms for an AME programme, then the excess over that implied by*

adopting broadly similar terms for that programme (and therefore broadly comparable costs) must be met by the devolved administration”².

2. Whether all relevant subordinate legislation and technical guidance associated with the legislation will lead to statutory rules which will be scrutinised by the Assembly rather than statutory instruments which will be scrutinised at Westminster?

The Public Service Pensions and Judicial Offices Bill makes provision for each Department with responsibility for a devolved NI public service pension schemes to make its own secondary regulations which would implement the remedy on age discrimination for their members. These regulations will be subject to the full requirements of the Assembly under the terms of the negative resolution process and subject to scrutiny by the relevant NI Assembly Committee in the same way as any other scheme regulations which would be made under the Public Service Pensions Act (NI) 2014.

Each department will be required to undertake full consultation with scheme members or their TUS representatives before the regulations are made. Where Treasury responsibilities will now also exist under the Bill for directions and technical guidance to the schemes in Britain, the Department of Finance will retain responsibility for all directions and technical guidance on equivalent matters for the devolved schemes.

3. Whether assurances can be provided that interest payments will be waived in respect of those scheme members who are required to make additional payments?

In the same way that the Bill provides for adjustments to benefit entitlements for the affected members for the period 2015 to 2022, provision is also made for schemes to make related adjustments for interest where contributions which would originally have been due for the type of benefits received may now be required.

The aim is to ensure fairness for all scheme members, including for those who have already paid the appropriate amounts of scheme contributions for the period in question. To ensure that a reasonable and fair rate of interest is used and to minimise inequity that could arise as a result of schemes using different rates or adopting different processes, the rate of interest used must be exercised in accordance with Department of Finance directions.

The Bill does provide scope for the individual schemes to reduce or completely waive any underpayment amounts where it deems this to be appropriate e.g where this might cause hardship. This detail would be set out in scheme regulations by each individual Department.

2

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/943689/Statement_of_Funding_Policy_2020.pdf

4. Whether assurances can be provided that where additional contributions might be required of deceased scheme members, these will be waived for their relatives?

In the case of deceased members, overpaid and underpaid contributions may also arise where the beneficiary of the member elects to take higher remedy benefits available in the scheme. Again this provision is intended to ensure fairness for all scheme members.

The Bill also provides scope for the individual schemes to reduce or completely waive any underpayment amounts where it deems this to be appropriate. This detail would be set out in scheme regulations by each individual Department.

5. Confirmation that the Department will provide necessary assistance to pension schemes in order to ensure that correct additional benefits are paid to eligible scheme members?

The Department of Finance is already engaging departments with responsibility for the devolved schemes at its interdepartmental Northern Ireland Public Service Pension Group (NIPSPG) on measures to ensure correct remedy implementation. The Department is monitoring progress on secondary legislation to ensure schemes have necessary legislative provisions in place in their scheme regulations to provide for the correct remedy payments and any related adjustments to be made.

The Department is assisting departments with the development of scheme policy and provision definition documents which will be used to inform administration and payroll specifications required to ensure the correct payment of remedy amounts.

The Department will also provide directions to schemes for the completion of action for the correct payment of benefits and compensation amounts in respect of members remedy entitlements where this would involve: transfers; pension credit members; voluntary contributions, and other special cases.

Other initiatives matters being progressed at NIPSPG, to ensure robust process for accurate remedy administration, include requirements for schemes to provide consistency in remedial benefit statements and scheme calculators for member use to inform member decision making on remedy benefits.

6. Whether confirmation can be provided that financial advice will be provided to all scheme members by e.g. the Pensions Advisory Service when they come to make their deferred contribution underpin decision?

The Public Service Pensions and Judicial Offices Bill does not currently specifically legislate on this. It is acknowledged that outcomes on remedy can be made more complicated where there are tax implications which would impact member thresholds, allowances, and liabilities within the HMRC tax regime (including where breaches of the Annual Allowance may occur). In these circumstance central provision for

independent financial services may be appropriate. This issue has been raised at the second stage debate for the Bill and may be expected to feature again during the remainder of the Bill's passage.

The Bill does require that schemes must take steps to provide all members eligible for the DCU remedy with remedial statements on both legacy and reformed scheme benefits available to them and any other related information relevant to their DCU option. The Department will continue to work with schemes to ensure the tools and approaches made available to members, including in the provision of remedy calculators and formal remedial benefit statements, are fit for purpose and provide up to date and objective detail relevant to each individual's decision-making.

Public service pension schemes are not qualified to provide financial advice to members. Members of public service pension schemes will place different values on different features of scheme designs, depending on their personal circumstances. They may of course wish to seek additional independent financial advice in the same way that this option is already available to them for their financial planning.

7. The Committee would also welcome clarification in respect of the Department's likely preferred timing for the scheduling of the LCM in plenary.

The Department is content that the Assembly Business Office schedule the LCM in plenary at the earliest time of its convenience following the publication of the Committee's report.

You will wish to bring this update to the attention of the Committee.

Yours sincerely

Andy Monaghan

Andy Monaghan
DEPARTMENTAL ASSEMBLY LIAISON OFFICER