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Public Sector Pensions – Briefing Note

The Impact of McCloud & Sargeant Judgements on Public Sector Pension Schemes

Background

Public Sector Pension Schemes have been subject to the same funding issues that were impacting on the Private Sector, essentially that the cost of providing benefits through defined benefits schemes was steadily increasing. Whilst the many private sector schemes closed their doors to new members or shut completely the Public Sector schemes took a different approach.

The approach was that from April 2015 (April 2014 for the Local Government Pension Scheme (LGPS)) a new basis of benefit accrual was introduced within Public Sector Pension Schemes. Within the **Reformed Schemes** members typically built up benefits at a lower level than they had within the **Legacy Schemes**. In addition to changes made to the accrual rates, the Reformed Schemes also had later retirement ages than the Legacy Schemes.

To protect those who were closer to retirement, employees who were members of a legacy scheme at 1st April 2012 and were within 10 years of retirement were permitted to remain in the Legacy Scheme. For all other employees, they ceased to accrue benefits within the Legacy Scheme from April 2015 (April 2014 for LGPS) and began to accrue benefits in the Reformed Scheme. As always, there were additional exceptions where employees were more than 10 years from retirement but met other criteria relating to pensionable service and their age.

What was the problem with this?

The problem was that some of the reforms unfairly discriminated on grounds of age - Transitional Protection had been offered to older scheme members and thus younger members had not been afforded the same benefit.

Legal action was taken against the Judicial and Fire Fighters Pension Schemes (these were the cases raised by Messrs McCloud & Sargeant). In December 2018, the Court of Appeal found in favour of the Claimants and required that the unlawful discrimination be remedied by the Government.

Solution

The Government consulted on two options and in February 2021 announced how it was to solve the discriminatory issue. This document can be accessed here.

The solution will come in a number of steps:-

1. All individuals who were members or were eligible to be members of a Legacy Scheme immediately prior to 1st April 2012, and have a period of service after 31st March 2015, during which they became members of a Reformed Scheme will have their benefits in the Legacy Scheme reinstated for their period of service up to 31st March 2022.

2. Should it be found that the benefits accrued within the Reformed Scheme would have provided a higher benefit than the Legacy Scheme they will be offered a choice as to which benefits they wish to accept. This has been named the **Deferred Choice Underpin** or DCU.

3. Employees who were awarded Transitional Protection and remained in the Legacy Schemes beyond April 2015 will also have a DCU which will check whether they would have accrued a higher benefit in the Reformed Schemes.

With effect from 1st April 2022, all employees will be members of the Reformed Scheme and those employees who commenced employment after 1st April 2012 will remain in the Reformed Scheme from April 2015.

Legislation is yet to be passed with regards to the above but the timeframe laid down in the Government Response Document is that the reinstatement of employees in the Legacy Scheme will be completed by October 2023. The DCU will then be checked at the time they access benefits (retirement / transfer / death).

For employees who have already retired, their benefits will be checked and they will be given the option of increased benefits should the DCU provide a benefit greater than that which they are in receipt of.

Affect

Employees in employment at April 2012

These employees will be subject to the DCU and will receive the higher benefit of either the Legacy or the Reformed Scheme.

Employees who have joined after April 2012

They will remain as is, with benefits within the Legacy Scheme to April 2015 and within the Reformed from 2015 onwards.

Retired Members

Retirees after March 2015 will have their benefits checked to see whether they would have had a higher benefit within the Reformed Scheme if they were awarded Transitional Protection or within the Legacy Scheme if they were moved to the Reformed Scheme, their benefits will be uplifted accordingly.

Ex-Spouses awarded a Pension Sharing Order

'The CETV will be calculated as though the Pension Debit Member had become a Deferred Member and had elected to transfer their pension rights at the relevant date, so the transfer value will be based on whatever scheme, Legacy or Reformed, produces the higher amount in relation to any period of service during the period between 1st April 2015 and 31st March 2022.

Where the CETV produced to the Court would have been higher as a result of the implementation of the DCU, the Pension Credit Members benefits will be increased in proportion with the increase in CETV to reflect that additional amount. The changes will come into effect when the DCU is implemented in the Scheme Regulations' – a.112 Page 59 Government Response Document.

Example: For an employee who was actively in the Legacy Scheme as at 1st April 2012 and was enrolled into the Reformed Scheme from April 2015 of which the benefits were subject to a Pension Sharing Order in 2018. The member would be subject to the DCU and therefore may be subject to an increase. If the benefits are increased the CETV will be recalculated based on the increase and if this provides a better outcome for the Pension Credit Member then the Pension Credit Member's benefits will be uplifted, (along with the benefits of the employee).

Practical difficulties moving forward

Without an in-depth analysis, it is impossible to know or indeed to calculate the impact of the DCU. It is our estimation that in the majority of instances this will have limited impact but that benefits may be slightly increased. Where employees have received significant above inflation pay rises (e.g. due to promotion) since April 2015 this would in our view lead to a bigger enhancement.

The approach we intend to adopt

At present there is too much uncertainty for us to carry out bespoke calculations and due to this we will continue to carry out our calculations and produce our reports on the basis of the benefit details provided from the Public Sector Pension Scheme. We will view matters on a case by case basis and provide any insight and assistance where we feel we are able to.

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A part of the Pension Sharing conundrum can be resolved by sharing an equal proportion of the Reformed Scheme Benefits and then carrying out a further calculation to provide equality for all other benefits.

Where offsetting is sought we can see no other option than to use the information currently available in our calculations, unless there has been above inflation pay increases, in which instance we can look at this on a case by case basis.

There will be many Public Sector scheme members whose benefits will be unaffected by these changes (e.g. where they left service before April 2015) and for those, we can continue as normal.

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