



HM Treasury

Joanne Livingstone
Chair, Firefighters' Pensions (England) Scheme Advisory Board
By email

23 March 2022

Dear Joanne

Thank you for your letter of 17 December to HM Treasury regarding the processing of immediate detriment (ID) cases in the Firefighters' pension scheme. I apologise for the delay in replying.

You have asked for more detail on the factors behind the withdrawal of the Home Office's informal and non-statutory guidance on processing certain ID cases, and in particular the risks and uncertainties of relying on Section 61 of the Equality Act to remedy benefits in advance of retrospective regulations.

I appreciate that this is a difficult situation for scheme managers in the Firefighters scheme, for the reasons you have set out, and the SAB's understandable desire to have the best information possible to inform future discussions. I will therefore set out these issues in detail.

The fundamental difficulty is that retrospectively changing pension entitlement through section 61 of the Equality Act 2010 cannot mitigate all of the consequences that arise from that. Legislation is therefore needed to address these consequences, particularly in respect of the complicated interplay with the tax system which is dependent on changing facts. The tax system requires certainty about the nature of payments made to and from pension schemes in the past in order to operate predictably and to produce proportionate results.

In some situations, processing cases without the full remedy legislation, including on tax, could lead to disadvantageous outcomes. The Public Services and Judicial Offices Act addresses some of these issues but others will need to be addressed through secondary legislation, the Finance Act 2022 and tax regulations. Legislation is also necessary to allow compensation to be paid by scheme managers, for example where an individual has overpaid tax beyond the usual statutory time limits for claiming it back.

I will now set out some of the detail of the specific tax issues that may arise and will be dealt with through legislation:

1. Tax relief on contributions for members who paid contributions to the reformed scheme.
 - If section 61 was used so that these members never left the legacy scheme for the remedy period, the effect would be that amounts deducted from their earnings and paid as pension contributions to the reformed scheme were paid incorrectly, because they were not a member of that scheme. This matters for tax purposes because only active members of a scheme are entitled to tax relief on their contributions.

- Tax relief can be given at the point the contributions are paid, and the legacy scheme and reformed scheme are two separate registered pension schemes. It is unclear what effect section 61 has on the contributions that were paid to the reformed scheme; it is not certain that section 61 means they can be assumed to have been paid to the legacy scheme. If section 61 can't be interpreted in that way, there is a separation of the members' contributions and the service, which mean that members were not entitled to the tax relief they received on their pension contributions (as they were not active members).
- Employers would therefore need to correct their RTI submissions for the relevant tax years to remove the tax relief that was given incorrectly. This would probably require the contributions to be returned by the scheme to the employer and then for the employer to pay them to the correct scheme, which would give tax relief at that point, but this may not equal the tax relief that members were entitled to previously. In addition, any contributions payable by or due to be returned to the member in respect of the tax years 2015-15 to 2021-22 because differences in contribution rates will also impact on their tax position, meaning that those who submit self assessment returns will need to contact HMRC to amend the information they declared previously.
- The provisions to address this are made in the PSP&JO Act, which will require commencement through scheme regulations, and in forthcoming legislation to allow tax relief to apply to contributions made during the remedy period years and for any contributions corrections to be made without the need for correcting RTI submissions.
- The combination of the PSP&JO Act, scheme regulations and tax regulations will alleviate the administrative burdens on the member, the scheme and the employer but if ID cases were processed prior to those statutory changes, existing legislation will apply. The full amount of historic contributions to a scheme where the individual is not a member would be taxable and a tax charge will be due as a result, that may not equal the tax relief the individual will be entitled to when the contributions are made to the correct scheme. So individuals in this situation may still need to have their position revised when the provisions of the PSP&JO Act are brought in.

2. Payment of benefits to date.

- Where an ID case is processed before legislation, there is uncertainty as to the status of payments that have been made from the Reformed Scheme to an individual who, according to section 61, is not a member of that scheme. It is not clear whether under section 61 the amounts paid would be assumed to have been paid by the legacy scheme. There is a risk that if the amount that was paid as a tax-free lump sum is seen as being paid from the reformed scheme, it would be taxable because it does not meet the conditions to be paid tax free as the individual is a member of the legacy scheme. Once commenced through scheme regulations, provisions in the PSP&JO Act will have the effect of treating pension benefits arising from remediable service paid out of the Reformed Scheme as having been paid out of the Legacy Scheme, clarifying the section 61 position.

3. New or increased lump sum payments.

- There could also be issues where the operation of section 61 Equality Act 2010 means that an individual has not been paid sufficient lump sum under the legacy scheme, because any further lump sum payment will be tax free only if the pension supporting the lump sum started no more than 12 months prior to the adjustment. If it is outside this time limit the adjusted lump sum would also be an unauthorised payment and an unauthorised payments charge would apply before tax legislation is in place to address this.

4. Annual allowance tax charge.

- An individual's liability for an annual allowance tax charge is calculated by deducting their pension value at the start of the year from the value at the end of the year in that pension scheme. If ID cases were processed using section 61 this could lead to a situation where those values were incorrectly reported because the member was recorded as building up service in the Reformed Scheme instead of the Legacy Scheme.
- This could lead to considerable difficulties where the Reformed Scheme had reported and paid an individual's annual allowance charge. The whole payment would need to be unwound as there would be no basis for the Reformed Scheme to pay the individual's tax charge as they were not a member of the scheme. The scheme would have to adjust the return on which they originally paid the charge (which may also have an administrative impact on the scheme in relation to any tax they have paid subsequently as tax is paid on a scheme basis). The individual would then owe their annual allowance charge and interest for late payment. Similarly, any overpaid annual allowance charges for out of scope years would need to be compensated, and as set out above, in advance of legislation there are no provisions in place to enable this.

5. Lifetime Allowance Charge

- Issues might arise with respect to lifetime allowance charges paid by the reformed scheme in relation to a member who, as a result of the operation of section 61, was always a member of the legacy scheme. The reformed scheme would need to claim a refund of the tax paid (where they were in time to do so), adjusting the return on which they originally paid the charge (which may also have an administrative impact on the scheme).
- The legacy scheme would now be liable to pay (i) any lifetime allowance charges in relation to that member's rights. and, (ii) any benefits payable under those rights. It is unclear what effect section 61 would have on the benefits that have been paid to the individual, whether it follows that these benefits must have been paid by the legacy scheme or the reformed scheme made payments to individuals who were not members. Depending on the interpretation of the operation of section 61 in relation to pension benefits already paid, the legacy scheme may be liable to pay benefits including amounts already paid by the reformed scheme. Legislation will be required to address these issues.
- In addition, if a member has paid their lifetime allowance charge themselves and section 61 provides that they were a member of their legacy scheme, where this provides for a lower charge, they can notify HMRC to claim for the overpayment. However, where the charge was paid for a year beyond the usual statutory time limits for correction of tax, compensation for this would not be available until the full remedy legislation is in place.

I hope that this gives you further insight into the tax issues that are likely to arise where ID cases are dealt with prior to legislation being in place and assists in future SAB discussions.

I would also note that, in addition to these tax issues, there are also other aspects of the remedy that remain to be determined and/or consulted upon on a scheme specific basis, such as how interest is to be calculated and paid on amounts that are owed to the scheme or by the scheme to a member or the specifics of rights of appeal.

For all of these reasons, the Government's view remains that processing immediate detriment cases before all of the necessary legislation is in place could give rise to significant consequences for schemes and members, although that ultimately is a decision for individual scheme managers. I also

recognise that this places scheme managers in a difficult position and we will continue to work with Home Office colleagues and others to explore any mitigations, where this is possible.

Finally, I would like to thank you for the Scheme Advisory Board's continued constructive engagement in helping to resolve the complex and difficult issues necessary to design and implement a legislative remedy.

Yours sincerely,

Henry Elks
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HM Treasury