CHESHIRE FIRE AUTHORITY

MEETING OF : LOCAL PENSION BOARD – FIREFIGHTERS PENSION SCHEME
DATE : 23 MARCH 2022
REPORT OF : PENSION SCHEME MANAGER
AUTHOR : JILL SWIFT

SUBJECT : FIREFIGHTER PENSION SCHEME UPDATE

Purpose of Report

1. The purpose of this report is to provide the Pension Board with an update on current issues relating to the Firefighters' Pension Schemes and the local governance arrangements in place to ensure effective administration of the schemes.

Information

Membership Statistics

2. Membership statistics are detailed in Appendix A. When comparing the data from Q3 with Q2 there do not appear to be any significant trends.

McCloud – Immediate Detriment Update

3. On 8 October 2021 the Local Government Association (LGA) and Fire Brigades Union (FBU) introduced the Memorandum of Understanding (MOU) and the Immediate Detriment Framework (IDF).
This built on the Home Office guidance released in June 2021, but provided a more detailed approach which aligned with the remedying legislation and a description of how immediate detriment cases should be dealt with. It was expected that all FRSs would adopt the framework and follow the processes for payment. On 8 November, the Fire Authority elected to adopt the IDF.

4. However, on 29 November, HM Treasury and the Home Office released a statement advising that in the course of drafting the McCloud Bill, it had become clear that there were a number of gaps and uncertainties in current legislation, which posed significant risks to operating the remedy smoothly and predictably for both members and schemes. These risks are predominantly related to taxation and may result in members receiving unforeseen tax bills or having their case reviewed multiple times in the future.

5. The Home Office confirmed that they had withdrawn their immediate detriment guidance, and advised FRAs not to proceed with immediate

detriment cases prior to the remedy legislation being finalised. They also concluded that due to the complexity of the issues, it is reasonable to expect more issues to emerge as they continue their work drafting secondary legislation.

6. In addition, they advised that they would not be able to provide additional funding for any immediate detriment costs incurred by any FRAs who opted to continue processing cases. Costs are those that will need to be borne by an FRAs operating account and will include any compensation payments, scheme sanction charges or interest payments.

7. Whilst the withdrawal of the Home Office guidance did not impact the MOU or IDF, it did raise concerns for FRAs who had elected to adopt the IDF and further legal advice was sought from the LGA. As a result of the uncertainty for members and schemes, CFRS have paused processing any immediate detriment cases until further clarification is received on the potential risks. Anyone in scope for immediate detriment will therefore retire under the current rules and their case will be reviewed and recalculated in the future.

8. The Scheme Advisory Board wrote to the HM Treasury in December requesting further detail on the risks but has not yet had a response. The legal opinion received in December confirmed that FRAs can continue to utilise the IDF as a mechanism to progress immediate detriment retirements but it was not able to provide full clarity on taxation matters or provide assurances on the funding position.

9. FPS Bulletin 54 confirmed that there are no further changes in the current position. Therefore at this time, the IDF process remains paused.

10. The FBU has indicated its intention to bring claims against FRAs who do not proceed with the IDF. This may take the form of complaints to the Pensions Ombudsman where compensation would be sought for the distress and inconvenience caused by late payment or non-payment, or possibly test cases in court.

McCloud – Prospective Remedy

11. The McCloud Remedy will be implemented in two phases, prospective and retrospective, delivered through primary and secondary legislation. The first phase of remedy is to make changes to the scheme regulations, in line with the Public Service Pensions & Judicial Offices Bill (PSP&JO Bill), which will close the legacy pension schemes to future accrual from 1 April 2022 and ensure all members who remain in service from 1 April 2022 do so as members of the reformed scheme (the 2015 Scheme). This will ensure future equal treatment going forwards.

12. In November, the Home Office launched a consultation on the draft regulations needed to enact this phase of remedy. From 1 April 2022 any remaining members with full protection will be moved to the 2015 scheme.

13. The LGA Fire Communications Working Group have developed a suite of letter for FRAs to use to communicate the changes to affected members. Our intention is to write to all remaining fully protected members to advise them of the changes to their scheme from April, and for all other members a communication will be published in the Green Bulletin and on the Firefighter Pensions hub on the intranet.

14. The consultation also sought feedback on the implications where ill health cases commence whilst members are still in their legacy scheme, but conclude after they have been moved to the 2015 scheme. The proposal is to implement a protection to ensure these members are not at a disadvantage. We do not currently have any pending ill health cases that will be affected by this change.

15. At the time of writing, the consultation response has not yet been published, but it is expected that these regulations will come into force on 1 April 2022.

Pension Administration Contract

16. The current contract with XPS group is due to expire in August 2022. We are not intending to do a full tender process but will instead direct award through a framework. This will allow a seamless transition and will reduce any risk associated with ongoing projects such as the McCloud Remedy and GMP rectification exercise.

Remedy Self-Assessment Survey

17. In May 2021, the LGA launched a self-assessment survey to gather information on the readiness of the fire sector to deal with the McCloud remedy. The survey looked at a number of key areas such as current administration arrangements, data quality and availability, business processes for calculations, legal and finance matters, member communications and levels of knowledge, capability and capacity. Cheshire's response is at Appendix B and C.

18. In the area of administration, a large proportion of FRAs are administered by West Yorkshire Pension Fund. Whilst LLP and XPS have a smaller market share. There are only 2 FRAs who administer pensions 'in-house'. It was noted that the marketplace for firefighter pension administration is shrinking, namely due to the time and expertise needed to deal with what is a very complex scheme and the number of administrators is likely to shrink further.

19. The survey highlighted issues such as availability of pay and contribution data where services have changed HR systems or payroll

providers since 2015 and the resources required for the data collection exercise. Most FRAs indicated that they would need additional resource to obtain and assess data for McCloud and also the remedy for the Matthews case, which is likely to commence in 2023.

20. FRAs indicated concerns about the processes that will be needed to recalculate pensions, in particular for taxation. It is also clear that FRAs are struggling to identify the potential costs of remedy and therefore the majority did not have an allocated budget for direct and indirect remedy costs.

21. In the area of communications, most FRAs felt that the LGA should provide information such as FAQs at key points during the remedy process and there was an appetite for modellers or online tools to allow members to project benefits. The majority felt that FRAs should provide information to the workforce on timescales and next steps. Most FRAs had a remedy project team or working group and that included input from administrators.

22. Responses on knowledge, capability and capacity were mixed but on average FRAs rated their internal knowledge and capacity as 5.67 out of 10. Most had identified this as a risk on their corporate risk register and were looking to access additional training and some indicated that they would seek external expertise to help.

23. The key risks highlighted for Cheshire Fire and Rescue Service related to data and internal knowledge. Since the survey launch, further work has been completed to identify members impacted by McCloud and a pensions manager role is in place to increase knowledge and capacity within the team.

24. Work has not yet commenced on identifying members affected by the Matthews case. However, the data used in the first options exercise in 2014 is still available and this is likely to be sufficient for the second options exercise. A lot of the data required is stored in an old HR system called PP, which is no longer supported on the current IT infrastructure. Work has commenced to copy this database into a more sustainable format to ensure this data remains available in the future.

Updates to Pensions Tax Legislation

25. On 27 October, HMRC released a policy paper outlining a number of updates that would be provided for in the Finance Bill 2021-2022 to mitigate the impact on individuals affected by the McCloud case. This will allow detailed technical changes to be made in secondary legislation, likely to come in later in the year with retrospective effect to 6 April 2022.

26. The proposed changes include:

- a tax exemption on compensation payments
- allowing an individual to protect their pension from lifetime allowance charges
- additional annual allowance to ensure members do not pay more than they would have done if they had remained in their legacy scheme
- allowing arrears of pension and lump sums to be deemed authorised payments, thereby meaning an unauthorised payment tax charge will not become due
- removing anomalies from existing legislation which don't currently allow certain tax events to be reported and paid retrospectively.

27. Under the IDF, FRAs have to compensate individuals who have incurred certain unauthorised payment charges and have to gross up compensation payments to account for income tax, leading to additional cost burdens. The introduction of this legislation will remove some of these costs. However, prior to the implementation of these provisions, all current tax rules have to continue to be applied and there is no indication of when the secondary legislation will be available.

Cost Cap Mechanism

28. Every four years, two valuations are carried out for the firefighter pension schemes. The main valuation determines the employer contribution rate and the other is called the 'employer cost cap' valuation which assesses how much it costs to run the scheme. If the costs exceed +/- 2% action needs to be taken. In the 2012 valuation, the cost cap was set at 16.8%.

29. If the scheme is more expensive, benefits may be altered to bring the costs down such as accrual rates being altered, or contribution rates increased. If the scheme is cheaper to run, benefits may be improved such as changes in early retirement factors or a reduction in contribution rates.

30. Following the 2016 valuation, the main valuation costs went up meaning employer contribution rates would rise. However costs went down for the cost cap valuation meaning that benefit improvements were needed. This was not how the cost cap mechanism was designed to work and the Government Actuaries Department described it as a "perverse outcome". They subsequently consulted on ways to improve the mechanism to ensure this is more stable and fair in the future.

31. Following this valuation, changes to benefits should have been implemented from April 2019. However the Government paused the cost cap mechanism due to the ongoing McCloud case, and any potential impact the outcome of the case could have on the cost cap.

32. In July 2020 the cost cap process was unpaused. HM Treasury advised that the costs associated with the increased value of schemes as a result of the McCloud ruling, would be taken into account as they are

‘member’ costs. Following review of the 2016 valuation, all schemes saw significant breaches, mainly due to legacy scheme benefits and projections for the McCloud remedy costs.

33. In December 2021, a number of unions including the FBU issued formal proceedings for a judicial review. Unions have made it clear that they do not think costs for remedy should be passed to members and that the benefits improvements that would have applied following the initial 2016 valuation should stand. This is currently ongoing.

Pension Dashboard Programme

34. The Department for Work and Pensions are currently undertaking a project to create pension dashboards which will allow anyone with a pension scheme to view all their pension information in one place, alongside information about their State Pension.

35. Statistics show that on average people have 11 different pension pots by the time they reach retirement age. The dashboards will help people get a consolidated picture of their pension savings and allow them to make more informed financial decisions. It will also encourage people to save for their retirement.

36. Whilst the concept of pension dashboards is widely viewed as a positive step, there will be a number of challenges for public sector pension administrators in providing the data in the necessary format and within the timescales proposed in the draft legislation.

37. Due to the McCloud remedy, projections of member’s benefits will be more complex to report as they will have two options of benefits. It’s unlikely that the dashboard will allow for this. Therefore members may benefit more from using the XPS self-service facility rather than the pension dashboard. This calls into question what the take up of the pension dashboards will be for those with public sector pensions.

38. The proposed go live for public sector defined benefit schemes is April 2024. However due to the fact administrators are likely to be in the middle of the retrospective McCloud remedy exercise at this time, these timescales may be difficult to achieve.

39. There is the added challenge that we currently only provide data to XPS on an annual basis, therefore any information provided to the dashboard will not be real-time. However, XPS are exploring the potential to provide FRAs with the facility to report on a monthly basis in the future.

40. In January 2022, the Department for Work and Pensions published a consultation seeking views on a range of policy questions relating to the creation of the dashboards. The LGA and Scheme Advisory Board will be responding to this consultation to advise that April 2025 may be

a more realistic date for public service pension schemes to work towards.

XPS Business Continuity

41. In light of the pandemic and ongoing fears around cyber attacks, XPS have provided an update on their business continuity plans to provide assurance that the necessary processes and tests are in place to protect member's data and maintain business critical functions in the event of a major operational disruption (Appendix D).

General Updates

42. The LGA issued two surveys in February 2022. The first sought feedback on what the current position is in each FRA in respect of how they're processing immediate detriment cases. This information will aid the LGA to better understand the current landscape, and will help in their discussions with other parties to identify any necessary solutions. The second is an administrator self-assessment survey which has been sent directly to administrators with a closing date of 18 March 2022.

43. Public service pensions will be increased by 3.1% from 11 April 2022. CARE scheme pensions will be revalued by 4.1% on 1 April 2022.

44. Employee and employer contribution rates will remain the same for the 2022-23 financial year. Any changes to the employer rate as a result of recent valuations will be implemented from 1 April 2024.

CONTACT: DONNA LINTON, CLEMONDS HEY, WINSFORD
TEL: [01606] 868804

BACKGROUND PAPERS: NONE