

Report to	<b>North Wales Fire and Rescue Authority</b>
Date	<b>15 July 2024</b>
Lead Officer	<b>Helen MacArthur, Assistant Chief Fire Officer, Finance and Resources</b>
Subject	<b>Firefighters' Pension Scheme – update on legal challenges</b>



## PURPOSE OF THIS REPORT

- 1 The purpose of this report is to provide members of the North Wales Fire and Rescue Authority (the Authority) with an update on the statutory changes to Firefighters' Pension Scheme following significant legal challenges. These are more commonly known as the McCloud and O'Brien (Matthews 2) pension remedy exercises.

## EXECUTIVE SUMMARY

- 2 The recent legal challenges to the UK public sector pension schemes have resulted in regulatory changes to the Firefighters' Pension Scheme. These changes are necessary to address two main issues; age discrimination following the implementation of the Firefighters' Pension Scheme 2015 (McCloud Judgment) and an historic issue relating to the pension arrangements for part time workers (O'Brien Judgment).
- 3 The changes arising from the McCloud judgment require a retrospective review of the pension benefits of eligible pension members between the period 1 April 2015 and 31 March 2022. This includes the provision of pension options for retired members, beneficiaries, deferred members and active members. The work to reconcile the payroll and pension records of staff within scope has commenced and will allow for the production of remedial service statements by the deadline of 31 March 2025. However, the processing of the choice for some retirees cannot progress due to a national tax issue.
- 4 The changes arising from the O'Brien judgment require a review of the contracts relating to eligible part time staff who express an interest in receiving pension benefits from the commencement of their employment. Staff who wish to proceed will be permitted to buy back their pension entitlement. The regulations require that this work is completed by 31 August 2025.

## **RECOMMENDATION**

- 5 It is recommended that Members:
- i) Note the statutory requirements to implement the changes to the Firefighters' Pension Scheme regulations; and
  - ii) Endorse the proposals set out within this report for the management of cases impacted by the tax laws.

## **OBSERVATIONS FROM THE LOCAL PENSION BOARD**

- 6 The Local Pension Board receives regular updates on progress towards implementing the changes required and has noted the complexity of the issues and the significant challenges to achieving the statutory deadlines.

## **BACKGROUND**

- 7 The Public Service Pensions Act (2013) is the primary enabling legislation for all public sector pension schemes. As responsibility for the management of the Firefighters' Pension Scheme is a devolved function in Wales, the Senedd has responsibility for updating and maintain the regulations. The Authority is the Scheme Manager with responsibility for compliance with the underlying regulations.
- 8 There have been two significant legal challenges which are applicable to the Firefighters' Pension Scheme; the McCloud Judgment which relates to age discrimination and the O'Brien Judgment which relates to the pension arrangements for part time workers.

## **INFORMATION**

### **MCCLOUD JUDGMENT**

- 9 Following Lord Hutton's 2011 review of public sector pensions, the Public Service Pensions Act (2013) provided the legal framework to reform public sector pension schemes. Reforms included restricting existing final salary schemes, extending retirement ages, and introducing CARE (Career Average Revalued Earnings) Schemes.

- 10 In 2015 the majority of public service pension schemes were reformed to provide defined benefits, on a CARE basis, and extended the normal retirement age of members. The pension scheme regulations were amended to introduce these changes, with the amended regulations also providing protections for certain members of existing final salary schemes. This protection was age related and members reaching the normal pension age of 55 by 31 March 2012, were afforded full protection with other members receiving protection on a tapered basis depending on their age. This protection was known as transitional protection and members who did not qualify for protection, transitional or otherwise (unprotected), were moved out of their legacy schemes, into the new 2015 Firefighters Pension Scheme on the 1 April 2015.
- 11 In 2018 the Court of Appeal ruled that the transitional protection element of the 2015 public service pension reforms constituted unlawful age discrimination, in the Firefighters' Pension Schemes. This is now referred to as the McCloud/Sargeant case. On the back of this decision, the Government confirmed that it would remove the difference in treatment across all public service pension schemes
- 12 In October 2020 the UK Government undertook to consult the public on the way forward in relation to public service pension schemes and, in particular, how it should respond to the detail outlined in the judgement. The outcomes of the consultation were published on 4 February 2021, with an option called 'the Deferred Choice Underpin' being adopted. This means that members will make their decision between scheme benefit options shortly before their benefits are paid from the scheme, at the point of retirement. In the meantime, members will be deemed to have accrued benefits in their legacy schemes rather than reformed schemes, for the remedy period. The remedy period has been determined to be 1 April 2015 to 31 March 2022.
- 13 The Public Service Pensions and Judicial Offices Act 2022 (PSPJO) was given Royal Assent on 10 March 2022 and provides an overarching framework to allow public service pension schemes to remedy the impact of unlawful age discrimination.
- 14 There were two distinct elements to the changes in legislation; the first came into effect on 1 April 2022 and was known as Prospective Remedy, which meant that from that date all members of the Firefighters Pension Schemes would be automatically become members of the Reformed 2015 Scheme.

- 15 The second was known as Retrospective Remedy, which came into effect on the 1 October 2023 and meant that those that had membership, in a fire scheme, during the remediable period will have the choice of taking those benefits in either the final salary legacy scheme or the reformed career average scheme.
- 16 It is these complex changes, that fall under Retrospective Remedy, that form a large part of the national remedial exercise that is currently underway. The McCloud Remedy Exercise timelines are set out in the new legislation and dictate that active pension scheme members, those that have already retired and member dependents must have received a Remedial Service Statement, no later than 31 March 2025.
- 17 The work to provide the Remedial Service Statement involves a full review of each payroll record for the period 1 April 2015 to 31 March 2022 to determine the pensionable elements for both the legacy and career average scheme.
- 18 In order to facilitate progress through the project, members have been grouped into cohorts, with different milestones set and support provided nationally by the Local Government Association. These milestones are intended to keep the project on track, to complete on time and also assists in managing member expectations.
- 19 The changes to the pension legislation may also have a consequential tax implication for those affected and the legal updates have also included changes to tax legislation. However, it has become apparent that the current tax legislation does not sufficiently address all circumstances and requires further changes to the underlying tax legislation or Written Ministerial Statement. This was not progressed in sufficient time before the UK general election was called and a resolution is not expected until the early Autumn.
- 20 The current tax regulations do not allow for tax already paid on lump sums to be offset against sums due when the lump sum is recalculated for remedy purposes. Without a solution this will mean that a member is liable for more tax which is not currently reclaimable. This issue only affects members who have already retired and received an unauthorised lump sum when they retired (i.e. due to the scheme rules the lump exceeded the tax-free lump sum allowable under HMRC rules).

21 The table below provides an overview of cases and the risk associated with the tax issue and it is proposed that those in the green category will progress in accordance with the agreed priorities. The amber cases will be considered on a case by case basis whilst the red cases will be temporarily paused until such time as the tax implications are resolved.

Green	Amber	Red
<ul style="list-style-type: none"> <li>• Legacy FPS 2006 members with <b>no</b> eligibility for Matthews 2 or outstanding election</li> <li>• Legacy RDS modified members with <b>no</b> eligibility for Matthews 2 or outstanding election</li> <li>• Legacy FPS 1992 members who retired with restricted commutation (i.e. age 50 with 25 years service)</li> <li>• Legacy FPS 1992 members who remain within authorised limits (i.e. no lump sum or with HMRC limit)</li> </ul>	<ul style="list-style-type: none"> <li>• Higher tier ill health (single source ill health)</li> <li>• Protected and *taper protected legacy FPS 1992 members who elected for maximum lump sum (i.e. paid an unauthorised tax charge) <i>*who at point of retirement had <b>not</b> tapered into FPS 2015</i></li> <li>• Legacy FPS 2006 members <b>with</b> an outstanding Matthews 2 election</li> <li>• Legacy RDS modified members <b>with</b> an outstanding Matthews 2 election</li> </ul>	<ul style="list-style-type: none"> <li>• Unprotected and *taper protected legacy FPS 1992 members who elected for maximum lump sum (i.e. paid an unauthorised tax charge) <i>*who at point of retirement had tapered into FPS 2015</i></li> </ul>

22 There is a significant administrative burden arising from the changes to the regulations which has required the prioritisation of cases. All staff retiring from the Service receive the choice of taking their legacy or career average benefits for the remedy period. Thereafter, work is ongoing to achieve the deadlines set which includes the provision of remedial service statements and includes retired members, beneficiaries, deferred members and active members.

## BACKGROUND – O'BRIEN

23 In April 2006, the Firefighters Pension Scheme 1992 (FPS 1992) was closed to new members, and the Firefighters Pensions Scheme 2007 (FPS 2007), came into force, which enabled On-Call Firefighters to be become pension scheme members from that date. Although the FPS 1992 Scheme remained unchanged for those regular firefighters who were already members.

24 Historically, On-Call firefighters were excluded from the Firefighters Pension Scheme 1992 (FPS 1992), which was challenged under the Part-Time Workers (Prevention of Less Favourable Treatment) Regulations 2000. This resulted in a determination that enabled certain On-Call firefighters, with service between 1 July 2000 and 5 April 2006, to become members of a pension scheme.

- 25 Between 2014 and 2015 an options exercise was undertaken, which gave those that were eligible the opportunity to join the firefighters' pension scheme. As the 1992 scheme had been closed to new members, the FPS 2007 scheme was modified to provide benefits analogous to the 1992 scheme (known as the 2007 modified scheme). This was the first options exercise, which is often now referred to as Matthews 1.
- 26 More recently, this judgment was challenged at the European Court of Justice in relation to fee-paid judges. The Court ruled, in that case, that service going back to the start of employment should be considered and the UK government accepted that the same principles applied to certain On-Call firefighters, whether they had made a legal challenge or not.
- 27 As a result, a second options exercise will now take place to allow eligible On-Call firefighters to buy pensionable service, backdated to the start date of their employment. As part of this exercise the following individuals are eligible for the second options exercise:
- I. On-Call firefighters employed on any date between 7 April 2000 and 30 June 2000 (inclusive);
  - II. On-call firefighters employed on any date between 7 April 2000 and 30 June 2000 (inclusive) as well as on any date between 1 July 2000 and 5 April 2006 (inclusive); and
  - III. On-call firefighters employed on any date between 1 July 2000 and 5 April 2006 (inclusive), but not on any date between 7 April and 1 July 2000, who were eligible to take part in the first options exercise but were not given opportunity to do so.
- 28 To enable the second options exercise to proceed, the Senedd has made the necessary regulatory changes to the pension regulations. These came into force on 1 February 2024 with an 18- month timeframe for full implementation of this project.
- 29 The Service has written out to all eligible staff to confirm that they are considered to be in scope. Those wishing to be included are required to complete an expressions of interest form to facilitate a calculation of their benefits should they wish to buy back pension entitlement. This is extremely complex given that the length of service can date as far back as the 1960s. The Service has three months, from receipt, to provide the individuals with the necessary information.

- 30 Staff who are considered to be out of scope (i.e. On-Call firefighters whose service commenced between 1 July 2000 – 5 April 2006 who did not take part in the first options exercise but were given the opportunity to do so) have also been communicated with and will be dealt with on a case by case basis.
- 31 There are interdependencies between the McCloud and O'Brien Remedy exercises for some On Call firefighters which may pose some complications in meeting these timelines, on a purely individual basis.
- 32 The Government Actuary's Department has provided a calculator that enables Services to provide information on the purchase of previous service for eligible staff. This process is very complex and requires salary information for each year of employment, the calculation of contributions that should have been paid, tax and interest that applies, alongside the benefits that those individuals would be entitled to receive should they proceed in buying back this service.
- 33 There are a number of unresolved tax queries including the tax consequence of retrospective payments made in one tax year, which may have impact on an individual's tax position and rate of tax applied.
- 34 Due to the tax issues raised and the protracted discussions that are underway it is not yet clear whether the processing deadlines will be revised.

## IMPLICATIONS

Wellbeing Objectives	The effective operation of the pensions schemes support staff wellbeing.
Budget	There are no budget implications directly related to these timelines.
Legal	The Authority has a statutory requirement to ensure that all legislative changes are implemented accurately and within the given timescales The Authority is required to administer the scheme in accordance with existing and new scheme regulations.
Staffing	Transparent and effective operation of the pension schemes ensures that staff are treated fairly and equitably.
Equalities/Human Rights/ Welsh Language	It is not considered that there are any issues that need addressing as the recommendations apply equally to all Members regardless of protected characteristics under the Single Equality Act.
Risks	Given the complexities of these projects, the resource considerations and timescales, there is a risk that the statutory deadlines may not be met.