

The British Medical Association's response to the cost control mechanism consultation

August 2021



FOREWORD

The BMA is a professional association and trade union representing and negotiating on behalf of all doctors and medical students in the UK. It is a leading voice advocating for outstanding health care and a healthy population. It is an association providing members with excellent individual services and support throughout their lives.

Most BMA members are members of the NHS Pension Schemes. This is a response from the BMA to the proposed changes to the cost control mechanism consultation and the proposals to reform the mechanism for public sector pension schemes.

We would from the outset note our disagreement with the inherent approach taken by the Government. We have maintained since the cost floor breach was discovered in 2018 that the Government had to comply with the regulations agreed regarding this mechanism to ensure the value of the pension scheme was maintained for members within the set control limit.

We remain disappointed that the Government have shown no sign of addressing this cost floor breach and believe that amending the cost control mechanism does not address the fundamental issues experienced by members of the scheme that led to the cost floor breach in the first place.

We would also note that a 'one size fits all' methodology may not be the correct approach for the public sector pension schemes. With 14.5% employee contribution rates in the NHS compared to 8% in the civil service, it is clear that there are significant differences between schemes that will produce unique sets of benefits to their members. This should be recognised through tailored solutions rather than implementing generic modifications that will result in different impacts on pension schemes due to the inherent variances between these schemes.

We also note the distinct absence of any proposal from the Government concerning how this amendment to the NHS Pension Scheme in any way incorporates or provides opportunities to implement remedies on the back of the McCloud decision. We feel any proposed amendment to the pensions scheme must be undertaken with this in mind.

We would therefore urge the Treasury to reconsider these proposals and instead pursue a tailored solution that addresses the cost floor breach in 2018, and ensures members of the NHS Pension Scheme remain incentivised and are provided fair value for their contributions to the scheme.

RESPONSE TO CONSULTATION

Question 1: Do you agree that a reformed scheme only design would achieve the right balance of risk between scheme members and the Exchequer (and by extension the taxpayer), and would create a more stable mechanism?

We do not view this proposed change as achieving a fair balance of risk between scheme members and the Exchequer. It is clear that these changes are designed to instead benefit the Government and employers over the interests of scheme members.

Firstly, despite there being legacy schemes alongside the present 2015 scheme, from a member perspective these essentially function as a single scheme. Many members have significant legacy membership as well as membership within the 2015 scheme. There are significant interactions between the schemes and, in particular, the common contribution rate structure across both schemes.

Furthermore, the impact of retirement of these members has to be considered in terms of the impact on both the 2015 and legacy schemes which, given the differing normal pension ages and, in some cases, the restrictions on ongoing scheme membership, does clearly require that each scheme be considered as one whole scheme, rather than separately.

In addition, the cost floor breach that occurred at the last valuation was across the NHS pension scheme as a whole. This breach should have mandated a reduction in member costs or an increase in member benefits - something that the Government chose to ignore. It is wholly unfair on members to have these schemes separated within the cost control mechanism and suggests the Government are simply seeking to avoid having to properly rectify the clear inherent issues within the pension scheme that have led to their own cost control mechanism demonstrating that NHS scheme members are paying too much for their pension benefits.

If the Government were to separate out these schemes from the cost control mechanism, we believe you would have to also separate the contribution rates and costs. With the current proposal, there is a significant risk that those members with both legacy and reformed scheme benefits will pay increased costs in the event of a cost ceiling breach, even if their legacy scheme benefits had reduced. Conversely, members of only the reformed scheme may not see their benefits increased in the event of a cost floor breach occurring across the whole pension scheme if this was driven by legacy scheme benefits being lower than expected.

We would also highlight that the cost floor breach at the last valuation was primarily a result of a reduction in the expected pensionable pay received by doctors - as a result of the Government not uplifting pay fairly, as well as the expected increase in life expectancy not occurring. Within the consultations, it is stated that the Government actuaries did not understand why risks in the legacy schemes should continue to impact the reformed schemes. This comment seems to ignore the impact of the final salary link that exists and the interactions between the schemes for those who are members of both the legacy and reformed schemes.

The reduction in pensionable pay relative to expected levels has a disproportionate impact on the legacy final salary schemes (as this affects all accrued pension) and highlights the risk of separating the legacy and reformed schemes to members.

Indeed, the Government once again has frozen pay for the majority of public sector workers. and NHS workers have received a pay award that the Bank of England predict will be below the level of inflation. Coupled with the fact that life expectancy of NHS staff is unfortunately likely to be further adversely impacted by COVID amid increasingly difficult working conditions, the impact of these factors on the legacy schemes are far more likely to exert pressure on the cost floor rather than the cost ceiling. This highlights the fact that separating the legacy scheme from the cost-control mechanism overwhelmingly favours the Government and adversely impacts scheme members.

The BMA believe that, had the cost floor breach not occurred and the Government were not in effect liable for changes to ensure the scheme retained value, a change to the cost control mechanism would not be proposed at this time. Indeed, we also believe that, had a cost ceiling breach occurred, the Government would not have 'paused' and instead moved swiftly to reduce member benefits or increase member costs, and similarly would not have proposed to review the cost control mechanism.

We therefore wholeheartedly reject the proposed changes and the premise that these changes would achieve the right balance of risk between scheme members and the Exchequer. We also note that you state the need to be fair to the taxpayer. NHS pensions scheme members are of course also taxpayers, with doctors paying not only one of the highest contribution rates across the public sector (rates which in effect remove the benefit of tax relief in its entirety) but also are hit harder than any other group with respect to the annual allowance, and are still subject to the lifetime allowance. It is vital that the scheme structures are fair to all scheme members and allows members to save for their retirement in a viable and progressive way.

Question 2: Do you agree with the Government's intention to widen the corridor? If not, why not?

We do not agree with the intention to widen the corridor. We believe that the widening of this corridor, alongside the desire to take the legacy pension schemes out-with the consideration regarding the cost floor and ceiling, are purely being designed to prevent the possibility of there being a cost floor breach, without equally and fairly being set up to prevent a cost ceiling breach. We feel this design heavily favours the Government over the scheme members and would be grossly unfair.

We again would emphasise that these are reactive measures to the mechanism that was put in place actually working to identify the lack of value to members of the scheme. None of these measures addresses this crucial point around the mechanism identifying the lack of value for members of the scheme.

We also believe that the changing of the mechanism is not helpful whatsoever to maintaining the stability of the scheme, and instead greatly reduces the fairness of the scheme for scheme members. We would instead encourage the Government to examine the underlying issues that led to the floor breach and seek to solve these, noting that, particularly on pay, it is within the Government's remit to solve this issue.

We note that the Government Actuary in table 5.A in the consultation estimates that a +/-3% corridor would lead to a breach of the cost control mechanism every 10 valuations, equivalent to a breach broadly every 40 years. Under this proposal, there is therefore potential for an

individual to spend their entire career paying 2.9% more for their pension benefits without the cost control mechanism being triggered. Whilst we therefore note the desire for stability and a long-term view, this must not be at the expense of members paying the correct amount for their benefits.

Retaining the +/-2% corridor but with a fairer, more robust mechanism in place could be a more preferable route to take, whilst also compensating members for the cost floor breach that has taken place.

We do not agree with the subsequent suggestion to have a fixed corridor of +/- 3%, with a flexible corridor of +/- 2% that required agreement between the Government and Scheme members to make changes to bring the scheme into balance. The actions of the Government in 'pausing' the cost control mechanism following a breach of the fixed cost floor at the last valuation highlights that this is unlikely to be a viable solution, as it is doubtful that an agreement would be reached in the future if the 'soft' cost floor was breached.

We note that one previous solution that was considered was different corridors (in terms of percentage points of pensionable pay) for different schemes, such that they represented the same % of scheme costs. However, HMT rejected different corridors on the grounds of requiring simplicity. We would highlight again that a tailored approach is needed to these pension schemes for the reasons stated in our foreword, and that the solution as presented would not work within the NHS Pension Scheme.

Question 3: Do you think that a corridor size of +/-3% of pensionable pay is appropriate? If not, why not?

We would reiterate our position in the prior question around this widening of the corridor being unnecessary and unfair, and note that it is too early to review this mechanism, given that there has been one review, which took place a number of years ago. The proposed change does not deal with any of the underlying issues and instead simply changes the measurement in terms of the schemes success and failure when it has already been found to have failed scheme members.

We note the GAD calculations suggest the change from +/-2 to +/-3% to reduce breaches from broadly every 5 to every 10 valuations. Given the 4-yearly valuation cycle, this would mean potentially 40 years between expected breaches - this could very well be perceived as going too far the other way and entirely negating the point of a cost control mechanism, as, in this case, it would likely be very rarely triggered.

We therefore reiterate our position that retaining the +/-2% corridor but with a fairer, more robust mechanism in place could be a more preferable route to take, whilst also compensating members for the cost floor breach that has taken place.

Question 4: Do you agree with the proposal to introduce an economic check?

We do not agree with this proposal. We would note that, when joining the scheme, the member is anticipating membership of 20-30 years (and beyond) in terms of their working life. The scheme itself in turn must commit to providing value to the member throughout their working life, thereby ensuring they wish to remain a part of the scheme. The long-term undertaking of the member towards the NHS needs to be properly reciprocated by the pension scheme.

This commitment of ensuring value to the member though has been broken throughout the last 13 years, with numerous changes made in 2008 and 2015 that greatly reduced the value of pension available to members of the scheme. This is before the utilisation of the Annual Allowance Tax and Lifetime Allowance Tax that has greatly reduced the value of the pension scheme to its members, particularly those doctors at the higher end of the salary scale.

This change would further reduce the safeguarding of the value of the scheme to its members. Furthermore, members plan their pensions savings for retirement which may be decades into the future. Given not only that, under the current proposal, a triggering of the cost control mechanism may only occur once every 40 years, but that there would also be an economic check that may be based on a short term, fully reversible event, we feel this proposal is wholly inappropriate.

We would also highlight the lack of objectivity around the measure. In addition, there is no converse suggestion that, in times of strong economic growth, member benefits could be increased if the scheme was in surplus but at a lower level than the cost floor. This proposal therefore is wholly one sided and is purely a measure to ensure any cost floor breach can be mitigated and in effect prevented. We would therefore oppose this economic check.

We would also emphasise that, with this change, members of the scheme would be no longer protected from wider economic factors which impact the costs of providing pensions. This would be a fundamental shift from the previous approach, and would be a change in direction that the BMA could not support.

Question 5: Do you think that the SCAPE discount rate, as it currently stands, is an appropriate economic measure for the cost control mechanism?

We believe that the SCAPE discount rate should be considered separately to the cost control mechanism. We feel it is inappropriate for this to feed into the cost control mechanism. Indeed, we are concerned that this represents yet another measure that enables the Government to mitigate or indeed prevent a cost floor breach from ever occurring.

We therefore strongly oppose the proposal for the SCAPE discount rate to be used as an economic check, and feel that the SCAPE discount rate should be considered entirely separately to the cost control mechanism.

Question 6: If the SCAPE methodology changes, and the Government considers that the SCAPE discount rate is therefore not an appropriate measure for the cost control mechanism, then do you think that a measure of expected long-term GDP should be used instead? If not, please set out any alternative measures that may be appropriate in this scenario. Please consider in the context of the separate review of the SCAPE methodology currently being undertaken by HM Treasury.

As set out previously, we feel it is inappropriate for there to be any further measure put in place and would again stress that we feel the SCAPE methodology and SCAPE discount rate should be examined separately.

Question 7: Do you envisage any equalities impacts from the proposals to reform the cost control mechanism that the Government should take account of?

We would note the overwhelmingly negative impact these proposals would have on older members of the pension scheme. As highlighted above, there is a real risk that they will receive lower than expected benefits in the legacy scheme and yet pay increased costs for the reformed scheme as a result of the separation of the legacy scheme from the cost control mechanism.

This would be clearly harmful, unfavourable and disadvantageous to them. Our position would be that we must safeguard and improve the attractiveness of the scheme to older members to retain them not only within the scheme but within the NHS. These measures would instead prevent this and would greatly limit the value of the scheme to older members.

Furthermore, these measures seem to have been geared towards purely seeking to avoid a cost floor breach and in turn have created conditions that would heighten the chances of a cost ceiling breach with little justification. This, alongside the proposed economic check, will have a negative impact on younger members of the scheme whose value of pension by the time they are able to receive it will be left at the whim of short-term economic fluctuations.

Notwithstanding the above, despite the Government acknowledging the disadvantage that these proposals would cause to older members, it is of note that it does not outline how it alleges that the proposals would constitute a proportionate means of achieving a legitimate aim. We would infer that the Government acknowledges that there is no such argument.