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Circular: 2025HOC0022MR

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To: All Members

McCloud/Sargeant Remedy: payment of arrears of contributions and interest

Dear Brother/ Sister

The issue

Members have raised a number of interconnected concerns regarding the obligation to pay arrears of contributions and interest as a consequence of "rolling back" into the FPS 1992 under the Public Service Pensions and Judicial Offices Act 2022 ('the Act').

Rolling back means the process of treating unprotected and taper-protected members as if they had never left the FPS 1992, effectively meaning that they are treated in the same way as their (older) fully protected colleagues. They are returned to the FPS 1992 for the period between 1 April 2015 and 31 March 2022 if they were unprotected or, for taper-protected members, the period between the date when their tapered protection ended and 31 March 2022 – usually referred to as the "remedy period". The significance of 31 March 2022 is that all members transferred to the 2015 Scheme with effect from 1 April 2022, regardless of their age.

The concerns raised include the questions:

1. Why should arrears have to be paid at all;

2. If arrears must be paid, what is the justification for charging interest; and

3. Why are members only allowed a limited period after receiving a remediable service statement to decide whether to pay arrears as a lump sum now, rather than as a lump sum at the point of retirement?

Similar questions arise in connection with former members of the FPS 2006 (the NFPS), with two important differences. The first is that these members have rolled back into a scheme with lower contribution rates than the FPS 2015, meaning that they have overpaid contributions during their remedy period. They are owed a refund of their overpaid contributions. The second is that because this is an amount owed by the scheme administrators to the members a different rate of interest is applied.

Former members of the FPS 1992

These members have recently received a remediable service statement ('RSS') explaining that they have been returned to the FPS 1992; that when they retire they will be given a choice as to whether the period of their remediable service should be treated as membership of the FPS 1992 or the FPS 2015; and that because they have been rolled back into the (more expensive) FPS 1992 they owe arrears of contributions and interest.

Interest is charged at the direct access National Savings and Investment account rate, which is currently 4% compound.

Compensation awarded in tribunal or court proceedings is almost invariably awarded at 8% simple. Direct access National Savings and Investment interest has been specified because it is the rate of return a reasonably cautious investor would earn if they made savings without tying their money up in a 90-day account.

It is important to note that the court and tribunal rate is simple interest. The National Savings and Investment rate is compound, meaning that interest is added on past interest already earned. As a comparison, 8% simple interest on £100 over a 10 year period amounts to £80; 4% compounded daily over ten years amounts to £49.18. After 20 years the numbers are £160 and £122.49. They begin to converge therefore, but for the first 31 years or so the 8% simple rate is higher than the direct access National Savings and Investment rate.

Why should members have to pay arrears at all?

The answer is that if they did not, they would be treated more favourably than the older, protected members who did not have to transfer. These older members paid contributions at the higher FPS 1992 rate throughout the period 1 April 2015 – 31 March 2022. Younger members paid the lower 2015 Scheme rate, and if they did not have to pay arrears, they would have built up the same period of 1992 Scheme membership for less money.

Unless that difference in treatment could be justified – and it is hard to see how it could be – that would amount to discrimination on the grounds of age, to the detriment of the older protected members.

Why should members have to pay interest?

This is an extension of the point made above. An older member who paid a contribution of say £100 in April 2015 has not had the use of that money ever since it was paid. The younger member has had the same £100 in his or her bank account; or he or she spent it on something which was cheaper in April 2015 than it would be if he or she bought the same thing now. Looked at in terms of savings or expenditure, money has a time value.

Why choose this rate of interest?

Using the example of putting the money in a bank account explains why the direct access National Savings and Investment rate has been used. That is what a cautious investor would earn. Putting the money in a current account earning no interest would be irrationally cautious. National Savings and Investment accounts are backed by the Government.

The main point to note however is that this rate was specified in Treasury Directions after consulting the Government Actuary's Department, as required by the Act. They could not be challenged. It is also the rate of interest used in the Matthews litigation.

Why allow only three months to choose to pay arrears as a lump sum?

The consultation paper regarding the remedy in the firefighters' schemes did not address the question of the payment of interest (because it was dealt with in the Treasury Directions and beyond the Home Office's remit), but the FBU has raised the issue anyway: why not allow members the option to pay by periodical payments? The Home Office did not respond beyond saying that this was a matter for the Treasury and Treasury Directions.

What happens if a member chooses to take FPS 2015 benefits when they retire?

Although FPS 1992 members have rolled back into the 1992 Scheme, when they retire, they could choose to take their remedy period service as 2015 Scheme service. This is unlikely to be an attractive option in most cases (the 2015 Scheme pension and lump sum would probably be smaller; but having an unmarried partner, for instance, might make the 2015 Scheme more attractive).

If they do: they paid FPS 1992 contributions for their remedy period, but having chosen 2015 Scheme benefits they have overpaid – they should only have paid at the 2015 Scheme rate. They are owed a refund.

That is what they will be paid, with interest, but there is a bit of a twist to the interest tale. They are now in the same position as a younger member, although it is debatable whether there is anything discriminatory in this outcome (at least in most cases): it is the outcome the member has chosen. The legislation provides, however, that whenever a payment is made to a member as a consequence of the remedy, interest must be added at the tribunal rate – 8% simple.

That is what the member will receive as interest, at least until the 29th day after they receive their RSS. Thereafter it is the National Savings and Investment account rate. So far as I can detect no explanation has been provided, but the logic of the legislation is that once a payment has been offered, and the member has had a reasonable chance to consider their options, if they don’t take the payment they have effectively chosen to bank with the Government. Continuing to pay interest at 8% simple gives them an overgenerous rate of return.

Former members of the FPS 2006 (the NFPS)

The major difference between the position of FPS 1992 members and FPS 2006 members is that for FPS 2006 members the contribution adjustment leads to a payment to the member.

If a younger FPS 2006 member was transferred unlawfully to the FPS 2015, and as a consequence they overpaid pension contributions, the reason for their treatment is their age. The tribunal interest rate (8% simple) must be applied.

That is what the Treasury Directions provide for, at least until the 29th day after an RSS is supplied. Thereafter the interest paid is the direct access National Savings and Investment rate.
Again, the logic appears to be that if a member is offered a refund with interest at 8% simple and chooses not to take it within a reasonable period, they have effectively chosen to bank with the Government. 8% simple would give them an unjustifiably generous investment return.

If members are considering taking the contribution repayment figure, then members are strongly advised to seek independent financial advice with regards to scheme membership due to the differences in accrual rate, commutation factors, early retirement penalties and the age at which the pension can be put into payment if members leave the scheme before normal pensionable age.

Deferred Choice Underpin (DCU)

DCU allows eligible members a choice, at the point their benefits are paid (their retirement) as to which pension scheme benefits, they would prefer to take for the remedy period between 1 April 2015 and 31 March 2022 if they were unprotected or, for taper-protected members, the period between the date when their tapered protection ended and 31 March 2022.

Deferring the choice until the point benefits are paid allows individuals to make their choice of which pension scheme benefits are better for them at that time, based on facts and known circumstances as opposed to assumptions on their future careers, health, retirement and other factors. The level of both pension scheme benefits will be known at retirement.

A Remediable Service Statement will be provided to the member each year detailing their accrued benefits under both their current and their legacy scheme for the remedy period in order to enable an informed choice to be made. The member can change their selected choice each year should they so wish to address individual changing circumstances.

Conclusion

The choice of interest rates and periods are set out in the Treasury Directions and legal opinion is that, as such, they are likely beyond challenge.

The underlying logic – that arrears should be paid or refunded with interest – is (in the legal view) necessarily correct if Government is to avert further claims being brought for age discrimination (from fully protected members). The legal view is that the rates chosen seem to be realistic, and The Government Actuary's Department consider them to be reasonable.

If members require further explanation in relation to the content of the RSS they have been provided with they should, in the first instance, raise this with their pension administrator. Similarly, if members wish to receive an explanation of DCU, additional to that contained within this circular, they should contact their pension administrator.

The contact details for all pension administrators can be found here: **https://fpsmember.org/contact**

Yours in unity,

Mark Rowe
National Officer

MR/am