EXPLANATORY MEMORANDUM TO

THE PUBLIC SERVICE PENSIONS (EMPLOYER COST CAP AND SPECIFIED RESTRICTED SCHEME) REGULATIONS 2022

2022 No. 787

1. Introduction

1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

2.1 These Regulations widen the cost control mechanism's cost corridor from +/-2% to +/-3% of pensionable pay. This increases the amount by which a scheme's cost must diverge from the employer cost cap before triggering a breach of the mechanism. The change will take effect from the 2020 valuations.

2.2 These Regulations also specify the New Judicial Pension Scheme 2015 as a restricted scheme for the purpose of section 12A of the Public Service Pensions Act 2013, thereby removing the requirement that it operates the cost control mechanism and undergoes valuations that are separate from those of the scheme that will replace it.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The territorial extent and application of this instrument is the United Kingdom.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

6.1 Section 12 of the Public Service Pensions Act 2013 provides for the operation of the cost control mechanism in regard to schemes made under section 1 of that Act. Specifically, section 12(1) states that scheme regulations "must set a rate, expressed as a percentage of pensionable earnings of members of the scheme, to be used for the purpose of measuring changes in the cost of the scheme" – known as the "employer cost cap" (section 12(2)). Section 12(5) then states that Treasury regulations must require the cost of a scheme (and, where appropriate, connected schemes) to remain within specified margins either side of the employer cost cap. The Public Service Pensions (Employer Cost Cap) Regulations 2014 (the "2014 Regulations") were made under these powers and provide for the +/-2% of pensionable pay cost corridor (or "specified margins"), meaning schemes must remain within 2 percentage points above or below the employer cost cap to avoid corrective action that would return the cost of the scheme to its target cost, which is specified in the 2014 Regulations as being the same as the employer cost cap.

6.2 With the coming into force of these Regulations (in particular, Regulation 3), the 2014 Regulations are amended to widen the specified margins in which schemes must remain to avoid corrective action being taken, from 2 percentage points above or below the employer cost cap to 3 percentage points above or below the employer cost cap. The cost corridor is thereby widened from +/-2% to +/-3% of pensionable pay for all public service pension schemes subject to section 12 of the Public Service Pensions Act 2013. This will take effect from the 2020 valuations. All 2016 valuations have been completed in line with the original design of the cost control mechanism.

6.3 Section 12A of the Public Service Pensions Act 2013 (as inserted by section 95(6) of the Public Service Pensions and Judicial Offices Act 2022) provides for the removal of the requirement that schemes undergo valuations separate from those of the schemes that will replace them and operate the cost control mechanism, if they meet the two conditions in section 12A(3): (i) the scheme is restricted; and (ii) it is specified for the purposes of section 12A in Treasury regulations.

6.4 With the coming into force of these Regulations (in particular, Regulation 4), the New Judicial Pension Scheme 2015 is specified for the purposes of section 12A. Given the New Judicial Pension Scheme 2015 became a restricted scheme on 1 April 2022 in accordance with section 90(2)(a) of the Public Service Pensions and Judicial Offices Act 2022, the coming into force of these Regulations means it is no longer required to operate the cost control mechanism or undergo valuations that are separate from those of the scheme that will replace it.

7. Policy background

What is being done and why?

<u>Cost corridor</u>

7.1 With regard to the widening of the cost corridor, the context of these Regulations is the Government's reforms to the cost control mechanism. The cost control mechanism is designed to ensure a fair balance of risk with regard to the cost of public service defined benefit pension schemes between members of those schemes and the Exchequer (and, by extension, taxpayers). It was introduced following the recommendations of the Independent Public Service Pensions Commission (IPSPC) in 2011. Whilst the IPSPC recommended a mechanism to protect the Exchequer from increased costs, the final mechanism negotiated between the Government and member representatives is symmetrical and so also maintains the value of pensions to members when costs fall. The operation of the cost control mechanism is provided for by section 12 of the Public Service Pensions Act 2013.

7.2 For each scheme, the mechanism assesses certain elements of scheme costs and if they have decreased/increased by more than a certain percentage of pensionable pay compared to their base level ("the employer cost cap"), then member benefits that accrue are increased/reduced to bring costs back to that base level (or contribution rates are adjusted). So, there is effectively a corridor either side of a target cost with limits representing the "ceiling" and "floor" – otherwise known as the "upper margin" and "lower margin" respectively. When those margins are breached, member benefits (or contribution rates) must be adjusted to bring costs back to target.

7.3 The Government asked the Government Actuary to review the cost control mechanism in 2018 amidst concerns that the mechanism was too volatile and not operating in line with its objectives. The review commenced in 2020 and his final report was published in June 2021.[1] It contained several recommendations on how to improve the mechanism. The Government consulted on three of those recommendations and published its response in October 2021.[2] It decided to take forward all three proposals. One of those proposals was the widening of the cost corridor from +/-2% to +/-3% of pensionable pay, which these Regulations implement. This will make the mechanism more stable, meaning members can have greater certainty regarding their future contribution rates and projected retirement incomes.

New Judicial Pension Scheme 2015

7.4 With respect to the specification of the New Judicial Pension Scheme 2015 (NJPS 2015) as a restricted scheme, the context of these Regulations is the reformed Judicial Pension Scheme 2022 (JPS 2022) that replaced the NJPS 2015 from 1 April 2022.

7.5 The NJPS 2015 was introduced alongside other reformed public service pension schemes, following recommendations from the IPSPC. The reformed schemes were a significant component of the major reforms to public service pensions implemented between 2011 and 2015. The NJPS 2015 replaced the existing scheme made under the Judicial Pensions and Retirement Act 1993, except for those judges covered by transitional protection arrangements. The NJPS 2015 was established under section 1 of the Public Service Pensions Act 2013 (PSPA 2013) and is therefore required to undergo valuations and operate the cost control mechanism.

7.6 Following issues with the recruitment and retention of judges raised by the Senior Salaries Review Body in its Major Review of the Judicial Salary Structure,[3] published in 2018, a policy decision was taken to close the NJPS 2015 to future accrual and replace it with the JPS 2022 from 1 April 2022. The JPS 2022 was established through The Judicial Pension Regulations 2022 (as made under the Public Service Pensions Act 2013) and came into force on 1 April 2022. Three key differences between the NJPS 2015 and the JPS 2022 are that the latter is tax-unregistered, has a uniform contribution rate, and starts with a higher accrual rate. Nevertheless, the JPS 2022's scheme regulations are subject to the PSPA 2013 statutory framework and are therefore consistent with the modernised pension provisions and governance requirements that were brought into force by the PSPA 2013 for the main public service pension schemes following the IPSPC's recommendations. It is therefore consistent with the NJPS 2015 in that, for example, it is a "career average", rather than "final salary", scheme, and has a normal pension age linked to the state pension age.

7.7 Schemes that are closed to future accrual do not require valuations separate from those of the schemes that will replace them or subjection to the cost control mechanism. This is because the costs associated with closed schemes will be

---

[1] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/993416/Cost_Control_Mechanism_-_GA_Review_-_Final_Report_-_27_May_2021.pdf

[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1022938/CCM_RESPONSE.pdf

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/751903/Supp_to_the_SSRB_Fortieth_Annual_Report_2018_Major_Review_of_the_Judicial_Salary_Structure.pdf

considered as part of the new scheme's valuation and cost control process if, and to the extent that, it is appropriate to do so. These Regulations ensure that now the NJPS 2015 is closed to future accrual, it will not be required to undergo those processes.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 HM Treasury have no plans to consolidate the legislation at this time.

10. Consultation outcome

Cost corridor

10.1 With respect to the wider cost corridor, this policy was consulted on in the Government's "Public service pensions: cost control mechanism consultation".4 A majority of respondents to the consultation agreed with the principle of widening the cost corridor and thought +/-3% was an appropriate size.

New Judicial Pension Scheme 2015

10.2 With regard to the specification of the NJPS 2015 as a restricted scheme, this is a matter of removing the requirement to perform certain actuarial processes when the replacement of that scheme renders them unnecessary. It is a technical change that follows from the policy decision to close the NJPS 2015 to future accrual. Once that decision was taken, this technical change was required to ensure the process of closing the scheme could proceed appropriately. In this context, the Government did not consider it appropriate to consult on whether the actuarial processes should continue.

10.3 The decision to close the NJPS 2015 follows a review that found the scheme was having adverse effects on the recruitment and retention of judges. This was identified by the Senior Salaries Review Body in its Major Review of the Judicial Salary Structure, published in 2018.5 For that reason, the NJPS 2015 has been replaced by the JPS 2022, which came into force on 1 April 2022. The design of the JPS 2022 was the subject of two consultations, in 2020 on the scheme design6 and in 2021 on the scheme regulations.[7] Overall, the responses received were supportive, with many judicial associations, especially those representing senior members of the judiciary, saying that the proposed reforms were a significant step towards resolving the recruitment and retention issues.

10.4 Some concerns were highlighted in the consultations. This included several comments that some features of the JPS 2022 were not as attractive as the pension scheme set out in the Judicial Pensions and Retirement Act 1993 or the Fee-Paid Judicial Pension Scheme 2017, and that the uniform contribution rate would reduce the take home pay for some judges. In response to the latter, the Government introduced the option for

[4] https://www.gov.uk/government/consultations/public-service-pensions-cost-control-mechanism-consultation

[5] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/751903/Supp_to_the_SSRB_Fortieth_Annual_Report_2018_Major_Review_of_the_Judicial_Salary_Structure.pdf

[6] https://www.gov.uk/government/consultations/consultation-on-a-reformed-judicial-pension-scheme

[7] https://www.gov.uk/government/consultations/judicial-pension-scheme-2022-scheme-regulations

members to pay a lower contribution rate (and receive a corresponding lower accrual rate) for three years to help members adjust to the new scheme. The Government responded to concerns in its consultation responses.[8][9]

11. Guidance

11.1 No specific guidance has been produced to accompany this instrument.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 With respect to the widening of the cost corridor, the impact on the public sector is that members of public service pension schemes are less likely to have their benefits or contributions changed via the cost control mechanism. With respect to the specifying of the NJPS 15, there is no significant impact on the public sector.

12.3 A full Impact Assessment has not been prepared for this instrument because no impact on business is foreseen.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 HM Treasury will continue to work with relevant Departments to review the impact and appropriateness of these Regulations. There is no requirement to review these on a fixed basis.

15. Contact

15.1 Sam Couldrick at HM Treasury (email: sam.couldrick@hmtreasury.gov.uk) can answer any queries regarding these Regulations.

15.2 Henry Elks, Deputy Director for Workforce, Pay and Pensions, at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.

15.3 The Rt Hon Simon Clarke MP, Chief Secretary to the Treasury, can confirm that this Explanatory Memorandum meets the required standard.

---

[8] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/964866/reformed-judicial-pension-scheme-consultation-response.pdf

[9] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1041395/jps-2022-consultation-response.pdf