Department
of Health &
Social Care

Stephen Hammond MP
Minister of State for Health

39 Victoria Street
London
SW1H 0EU

020 7210 4850

Your Ref: JS7278

PO-1174774

Jo Swinson CBE MP
By email to: jo.swinson.mp@parliament.uk

08 MAY 2019

Dear Jo,

Thank you for your correspondence of 29 April to Matt Hancock on behalf of a number of your constituents about changes to NHS consultants' pensions.

I appreciate your constituents' concerns and I would like to thank them for raising them with you.

We want to encourage pension saving to help ensure that people have an income, or funds on which they can draw, throughout retirement. This is why, for the majority of savers, pension contributions are tax-free. This makes pension tax relief one of the most expensive reliefs in the personal tax system. In 2015/16, income tax and employer National Insurance contributions relief cost around £50billion, with around two-thirds going to higher-rate taxpayers.

In this context, the Government keeps its lifetime and annual allowance tax policies under review. The 2018 Autumn Budget confirmed that the lifetime allowance would rise from £1,030,000 to £1,055,000 in April 2019, in line with the Consumer Price Index, to ensure the benefit is not eroded. The annual allowance remains at £40,000, although it may taper down to no less than £10,000 for higher earners. This allows savers to continue to make significant amounts of pension savings tax-free, whilst ensuring incentives to save are targeted across society.

The reforms to the lifetime and annual allowance made in the previous two Parliaments are expected to save over £6billion per year, and are necessary to deliver a fair system and protect public finances. The measures affect the wealthiest pension savers. Of those currently approaching retirement, 95 per cent have a pension pot worth less than the lifetime allowance, while the median pension pot for people approaching retirement is around £150,000.

The annual and lifetime allowances are important fiscal measures to ensure income tax relief on pension contributions is fair and sustainable. In the 1995 final salary section of the NHS Pension Scheme, clinicians who use up the full £40,000 annual allowance would see their annual pension increase by around £2,500. Clinicians who accumulate benefits worth the current lifetime allowance of £1,055,000 can expect an annual pension of around £46,000 a year, plus a tax-free lump sum of £138,000 on retirement. Pensions of this size provide very substantial financial security in retirement, and it is right that the Government takes steps to limit the tax incentive to save further.

The Government recognises that pension tax considerations may contribute to decisions by some senior clinicians to retire early or reduce their NHS commitments. For those who wish to remain in the NHS Pension Scheme, the annual allowance provides a disincentive to take on additional work and responsibilities, because the extra income increases the impact of the tapered annual allowance. The Government is listening carefully to concerns raised by senior doctors and NHS employers about the impact of the tapered annual allowance.

As an immediate step, the Department has sought to make available to NHS Pension Scheme members maximum flexibility within HM Revenue and Customs (HMRC) legislation and the current fiscal framework for public sector pension schemes. We have extended the scope of the 'Scheme Pays' facility implemented by the NHS Pension Scheme, and it now covers the payment of tax charges of any amount and those arising from breaches of the tapered annual allowance. This means that from the tax year 2017/18 a member has been able to elect for the scheme to pay 100 per cent of their annual allowance charge to HMRC on their behalf.

Scheme Pays allows individuals to settle their tax charge without needing to find funds upfront. However, HMRC requires that if a defined benefit pension scheme pays an annual allowance charge there must be an adjustment to the benefits members have accrued. This adjustment must be just and reasonable, having regard to normal actuarial practice. Accordingly, the NHS Pension Scheme applies an interest rate to the charge paid on the member's behalf. This is deducted from the capitalised value of the pension at retirement, with the interest rate set at the scheme discount rate. We recognise that, for some younger clinicians with many years before retirement, the compounding effect may influence the attractiveness of Scheme Pays.

In terms of potential further measures, the Government keeps the impact of public sector pay and pensions policies under constant review, taking account of total reward and fiscal considerations. The fiscal framework within which the NHS Pension Scheme operates is an important consideration. Like most public service pension schemes, the NHS Pension Scheme does not manage a fund of assets out of which pensions are paid. It is instead financed on a 'pay as you go' basis, similar to the State Pension, with contribution income defraying the cost of pensions in payment. Any change to scheme rules that provides flexibility could therefore have a significant effect on contribution income, which would have an immediate fiscal impact on the Exchequer.

The Government must balance fiscal risks against the benefits of providing additional flexibility. Any further proposed pension flexibility would require approval from the Chancellor.

I hope this reply is helpful.

Best wishes

STEPHEN HAMMOND