

Sent by Email only

12 November 2021

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Dear Sirs

**R (British Medical Association) v Her Majesty's Treasury & Secretary of State for Health and Social Care & – pre-action protocol letter**

**1. Proposed claim for judicial review**

This letter is a formal letter before claim in accordance with the pre-action protocol for judicial review under the Civil Procedure Rules.

**2. Proposed claimant**

We represent the proposed Claimant, the British Medical Association (BMA). The BMA's address is BMA House, Tavistock Square, London WC1H 9JP.

The BMA is a trade union and professional body for doctors in the UK. The vast majority of its members are members of the NHS Pension Schemes. Those who joined the NHS after 1 April 2012 are members of the 2015 NHS Pension Scheme.

**3. Proposed Claimant's legal advisers**

Capital Law Limited  
Capital Building  
Tyndall Street  
Cardiff CF10 4AZ

**4. Proposed defendants**

- (1) Her Majesty's Treasury  
1 Horse Guards Road  
London, SW1A 2HQ

(2) Secretary of State for Health and Social Care  
39 Victoria Street  
London, SW1H 0EU

The proposed First Defendant, HM Treasury, is responsible for making directions that specify how the pension schemes established by the Public Service Pensions Act 2013 must be valued and, in particular, specifying how the cost control mechanism operates.

The proposed Second Defendant, the Secretary of State for Health and Social Security, is the responsible authority for the management and administration of the 2015 NHS Pension Scheme. This includes making scheme regulations in relation to health service workers in England and Wales pursuant to section 2 and Schedule 2 (paragraph 5) of the Public Service Pensions Act 2013.

## 5. Details of any interested parties

Government Actuary  
Finlaison House  
15-17 Furnival Street  
London EC4A 1AB

## 6. Background to the matter being challenged

The Government legislated in the Public Service Pensions Act 2013 for a framework for new public service pension schemes to be introduced from April 2015. This gave effect to recommendations of the Independent Public Service Pensions Commission chaired by Lord Hutton. The reforms to public service pension schemes were designed to manage some of the associated costs and risks to the taxpayer and public sector staff from significant changes in pension costs. This included basing benefits on career average earnings rather than final salary and linking the normal pension age to the State Pension age. It also included provision of a “*cost control mechanism*” that would operate symmetrically so that if actuarial valuations showed that the costs of a scheme had risen or fallen outside of a target rate, steps would be taken to bring them back to target, including the increase or decrease of member benefits or contributions. The cost control mechanism works by measuring the notional past and future service of the ‘cost cap fund’ and comparing it to the “*target cost*” specified in the relevant Scheme Regulations.

### *The legislative framework*

Sections 11 and 12 of the Public Service Pensions Act 2013 govern cost control. By section 11 actuarial valuations are required to be made of the 2015 scheme (and any connected predecessor scheme) and must be carried out in accordance with Treasury directions. The directions may specify (amongst other things) how and when the valuation is to be carried out, the data, methodology and assumption to be used, and the matters to be covered by a valuation. Treasury directions, variations and revocations, may only be made after consultation with the Government Actuary.

The rate, expressed as a percentage of pensionable earnings of members of the scheme, which is to be used for the purposes of measuring changes in the cost of the scheme, referred to as the “*employer cost cap*” or target rate, is also to be set in accordance with Treasury directions made under section 12.

Treasury directions may specify: how the first actuarial valuation under section 11 is to be taken into account in setting the cap; the costs or change in costs that are to be taken into account on subsequent valuation of a scheme for the purposes of measuring changes in the costs of the scheme against the cap; and the extent to which costs of changes in the costs of any connected statutory pension scheme (i.e. a ‘legacy’ public service scheme connected with a ‘reformed’ 2015 public service scheme) are to be taken into account for the purposes of setting the employer cost cap or target rate.

Treasury *regulations* made under section 12(5) are required to make provision for the cost of a reformed scheme (and any connected scheme) to remain within specified margins either side of the employer cost cap or target rate and to specify a “*target cost*” within those margins in circumstances where the cost of a scheme would otherwise exceed them. Section 12 also makes provision for scheme regulations to specify a procedure for agreement to be reached between the responsible authority for the scheme, employers and members (or representatives of employers and members) as to the steps required to achieve the target cost for the scheme, and the steps to be taken if agreement is not reached under that procedure. The steps to be taken to achieve the target cost (sometimes referred to as rectification) may include the increase or decrease of member benefits or contributions.

The Public Service Pensions (Employer Cost Cap) Regulations 2014 stipulate that “*the cost of the relevant scheme must remain within the following margins – (a) an upper margin, being a rate of 2 percentage points above the employer cost cap of the scheme; and (b) a lower margin, being a rate of 2 percentage points below the employer cost cap of the scheme*” (Regulation 3). Where the cost of a scheme goes beyond the upper and lower margins in regulation 3 “*the target cost will be the same as the employer cost cap of the scheme*” (Regulation 4).

The National Health Service Pension Schemes Regulations 2015 set the employer cost cap for the 2015 NHS Pension Scheme at 11.6% of members pensionable earnings (Regulation 8). In circumstances where the scheme actuary’s valuation shows that the costs of the scheme would be outside the margins specified in Treasury regulations made under section 12(5) s/he is required to notify the Secretary of State for Health and Social Care (being responsible for the management and administration of the scheme) (Regulation 9). On receipt the Secretary of State must request that the Scheme Advisory Board consider the matter and give advice to the Secretary of State as to the means by which the target cost is to be achieved. The Secretary of State must consider the advice and seek to reach agreement with the Scheme Advisory Board as to how the target cost is to be achieved (Regulation 10). Where no agreement is reached the Secretary of State must adjust the fraction specified in paragraph 13(3) of Schedule 9 of the Regulations (i.e. adjusting the rate at which pension benefits accrue) so as to achieve the target cost (Regulation 11).

### *The 2016 valuation*

A valuation report showing the “preliminary” value of the 2015 NHS Pension Scheme “as at” 31 March 2012 was published on 9 June 2014. Provisional results of the “first valuation” of the 2015 NHS Pension Scheme “as at” 31 March 2016 revealed that the cost cap was breached. The Scheme Advisory Board was formally commissioned in September 2018 to advise the Secretary of State on the measures that should be adopted to rectify the cost cap breach.

Also in September 2018, the Government announced that the initial results of the 2016 valuations of the reformed schemes (including the 2015 NHS scheme) indicated that members would get “*improved pension benefits for employment over the period April 2019 to March 2023.*”. There would be consultation on what this would mean for each individual scheme with changes to be implemented from April 2019. It also asked the Government Actuary to “*undertake a review of the [cost control] mechanism to check whether it was working as intended and delivering on the Government’s objective to protect taxpayers and workers from unforeseen changes in pension costs*”<sup>1</sup>.

The NHS Scheme Advisory Board put forward its preferred rectification changes to both member benefits and contributions for consideration and sought agreement with the Secretary of State in November 2018. These would have operated in favour of scheme members.

On 30 January 2019 the cost cap rectification process was underway, with discussions ongoing between the Department for Health and Social Care and the NHS Scheme Advisory Board, when the Government announced its decision to suspend or ‘pause’ the cost control mechanism<sup>2</sup>. The Government said that its decision to do this was in response to uncertainty about the impact for the valuation of schemes of the Court of Appeal’s judgment in *McCloud v Ministry of Justice* [2018] EWCA Civ 2844 handed down in December 2018. The Court of Appeal held that the “*transitional protection*” offered to some members as part of the 2013 Act reforms amounted to unlawful discrimination.

In February 2019 the NHS Pension Schemes valuation report “as at” 31 March 2016 was published. The report set out the results of the actuarial valuation of the combination of the NHS Pension Scheme and the 2015 NHS Pension Scheme. It was carried out in accordance with The Public Service Pensions (Valuations and Employer Cost Cap) (Amendment and Savings) Directions 2019, which gave effect to the pause of the cost control mechanism. As such it was prepared without including the cost cap costs of the 2015 Scheme and by reference to the “*corrected employer contribution rate*” (20.6%) and the “*uncorrected employer contribution rate*” (17.9%). (The “corrected employer contribution rate” being calculated in the same way as the “uncorrected employer contribution rate”, except that the accrual rate of the 2015 Scheme was assumed to be improved from 1 April 2019 to the extent

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<sup>1</sup> <https://hansard.parliament.uk/commons/2018-09-06/debates/18090633000015/PublicServicePensionSchemesQuadrennialValuations>

<sup>2</sup> <https://questions-statements.parliament.uk/written-statements/detail/2019-01-30/HCWS1286>

necessary that the employer contribution correction cost equalled the target cost of the scheme.) The 2016 valuation measured a 3.2% difference between the “employer contribution correction cost” and the target cost of the scheme.

The Government subsequently lifted the pause of the cost control mechanism on 16 July 2020<sup>3</sup>. It purported to do so on the basis that progress with determining the cost of putting right the discrimination identified in *McCloud* (the “McCloud remedy”) meant that the valuation of public service scheme costs was now more certain. The announcement accompanied proposals, which were subject to consultation, to address the unlawful discrimination arising from the transitional arrangements introduced when public service schemes were reformed in 2015, and a decision that from 1 April 2022 all members not already in the reformed schemes and still accruing benefits in legacy schemes would be placed into the 2015 reformed pension schemes. The Government said that:

*“When the mechanism was established, it was agreed that it would consider ‘member costs’: i.e. costs that affect the value of schemes to members. As the proposals in the consultation published today will increase the value of schemes to members, this falls into the ‘member cost’ category. As a ‘member cost’, this will be considered as part of the completion of the cost control element of the 2016 valuations process. Current employer contribution rates will not be affected.”*

In February 2021, the Government announced<sup>4</sup> (following consultation) that it would “give eligible scheme members a choice at the point their pension becomes payable, whether they wish to receive benefits from their legacy scheme or benefits equivalent to those that would have been available under their reformed schemes in relation to service between 1 April 2015 and 31 March 2022 [“the deferred choice underpin”]. In the meantime, eligible members will be deemed to have been members of their legacy schemes for any period of service between those dates.” It also confirmed that benefits accrued in the legacy schemes, which would close on 31 March 2022, would be protected.

The announcement also included an update on the cost control mechanism. The Government said that:

*“the increased value of schemes to members as a result of the McCloud remedy will be taken into account in the completion of the 2016 valuations. Given that this will lead to higher costs than would otherwise have been expected, early estimates indicate that some schemes could breach the ceiling. If normal statutory procedure were followed, any ceiling breaches would lead to a reduction in member benefits in order to bring costs back to target. The [Government Actuary] review is ongoing, and I have decided that it would be inappropriate to reduce member benefits based on a mechanism that may not be working as intended.*

*This means any ceiling breaches that do occur during the completion of the 2016 valuations will therefore not be implemented, and benefit levels will not be reduced. However, I have also decided that should any floor breaches occur, they will be honoured, and member benefits increased in order to bring costs back to target. These decisions apply only to the cost control element of the 2016 valuations. Future cost control policy for future valuations will be set out once the [Government Actuary]’s review of the mechanism has concluded and any recommendations have been fully considered by the government.”*

By introducing Clause 80(3) of the Public Service Pensions and Judicial Office Bill the Government seeks to give legislative effect to its decision to waive the requirement to rectify a ceiling breach at the 2016 valuation so that no benefit reductions take place following the conclusion of the 2016 valuations. The Bill is currently at Report stage in the House of Lords.

On 7 October 2021 the Government published amending directions (The Public Service Pensions (Valuations and Employer Cost Cap) (Amendment) Directions 2021) governing completion of the 2016 valuations. A letter from the Government Actuary confirmed his opinion that these reflected the Government’s policy intention that the entire impact of the “McCloud remedy” be taken into account at this set of valuations<sup>5</sup>.

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<sup>3</sup> <https://questions-statements.parliament.uk/written-statements/detail/2020-07-16/HCWS380>

<sup>4</sup> <https://questions-statements.parliament.uk/written-statements/detail/2021-02-04/HCWS757>

<sup>5</sup> <https://www.gov.uk/government/publications/public-service-pensions-completion-of-2016-valuations>

The Fire Brigades Union (FBU) and Joshua Dunn issued an application for Judicial Review challenging the failure of HM Treasury and the Secretary of State for the Home Department to lift the “pause” on the operation of the cost control mechanism set out in the Firefighters Pension Scheme 2015 which had been introduced by The Public Service Pensions (Valuations and Employer Cost Cap) (Amendment and Savings) Directions 2019. Organisations representing members of the public service pension schemes, including the BMA, were named as interested parties. The BMA filed Summary Grounds that adopted and supported the FBU’s grounds of challenge on the basis that these were of equal application to the 2015 NHS Pension Scheme. The BMA advanced a further ground of challenge that the 2019 Directions unlawfully frustrate the policy and objects of the relevant legislation.

Following the Government’s announcement in July 2020 the proceedings were stayed until such time as the Treasury published new directions setting out how the judgment in *McCloud* would be reflected in the costs control element of the valuations process.

Under the terms of the Order granting the stay the Claimants are to file and serve any amendments to their Statement of Facts and Grounds within 28 days of notification by the Defendants of the directions being published by the Treasury, with the Defendants to file and serve their Acknowledgement of Service within 28 days of the Claimants’ amended documents.

The Government Legal Department notified the BMA’s legal representatives of the publication of the directions on 8 October 2021.

## **7. The matter being challenged**

This letter challenges The Public Service Pensions (Valuations and Employer Cost Cap) (Amendment) Directions 2021 made on 7 October 2021 and which give effect to the Government’s decisions (announced on 16 July 2020) to: (1) lift the suspension of the cost control mechanism, and (2) include the full costs of the McCloud remedy for the purposes of resuming the cost control mechanism and completing the 2016 valuation in respect of the 2015 NHS Pension Scheme.

First of all, it is wrong in principle, and contrary to the policy and object of the cost control mechanism which was to provide for unexpected events, that the McCloud remedy costs should be borne by scheme members. Moreover, given the circumstances, it is artificial for the Government to present its solution as increasing the value of the scheme. The true position is simply that the Government is providing restitution for its previously unlawful discrimination. Had it acted lawfully at the outset, the McCloud remedy would not have arisen and cannot properly be said to be an unexpected event of the type which the mechanism was intended to accommodate.

It is convenient for the Government to attribute any increase in scheme funding deriving from the McCloud remedy as being a member cost. But the cost control mechanism was never intended to operate in response to a fluctuation of scheme costs of that sort and such costs should properly be excluded for the purposes of calculating the costs cap. The value of pension schemes to members is irrelevant to the operation of the cost control mechanism, which is intended to share some of the risk of increased costs of scheme funding between employers and members. The mechanism is intended to value the ongoing costs of a scheme but not the costs of implementing protection or transitional protection. The liabilities associated with protection or transitional protection associated with membership of the legacy scheme should properly be excluded from the cost control mechanism (and the costs cap valuation).

Similarly, the cost of rectifying the age discrimination inflicted on members in service before 1 April 2012 should not be imposed on members who joined on or after that date and who might only have been members of the reformed 2015 scheme. Although section 12(4)(b) of the Public Service Pensions Act 2013 empowers Treasury directions to specify “*the costs, or changes in the costs, of any statutory pension scheme which is connected with a scheme under section 1 for the purposes of measuring changes in the cost of the scheme against the cap*” this is necessarily subject to limitation by the purpose of the enabling legislation, and fundamental requirements of procedural fairness.

One consequence of wrongly treating such restitutional costs as member costs has been insufficient consideration of relevant matters and/or consultation upon the issues, in particular the detriments that flow from both the prolonged pause of the cost control mechanism and the wrongful attribution of the McCloud remedy costs to all scheme members irrespective of their circumstances.

Specifically, there has been a failure to consider, consult upon and/or address:

- overpayment of contributions for the duration of the pause by some categories of scheme member,
- loss of value in accrued pension benefits (through displacement of what would otherwise have been calculated as a costs 'floor breach' and the loss of consequential increase in member benefits),
- the imposition of indiscriminate burdens and disadvantages to particular categories of scheme members (for example, new joiners of the 2015 NHS Pension Scheme bear the costs of the McCloud remedy despite not being members at the time of the unlawful treatment), and,
- failure to consider and address the impact upon members and groups of members with protected characteristics.

A consequence of introducing the pause during 2019 has been the interruption of and interference with the cost cap rectification process connected with the 2015 NHS Pension Scheme. This has prevented and delayed achievement of the target cost of the scheme (either by agreement between the Secretary of State and the Scheme Advisory Board and/or the triggering of the default adjustment) that would have followed in the absence of the pause (or have been delayed for a much shorter period). Consequently, the Secretary of State is inhibited from complying with his statutory duty to correct the cost cap breach of the Scheme, to do so promptly and without frustrating or undermining the legislative policy and objectives. The interruption of the rectification process has introduced detriment to pension benefits. By introducing the McCloud remedy costs that detriment has been compounded and, by the amending directions, will become a feature with adverse longer-term implications for the valuation of member benefits. Members have also suffered detriment in consequence of overpayments and being deprived of the adjustment in accrual value which they were entitled to expect through the proper and timely operation of the legislative scheme.

The imposition of the McCloud remedy costs upon scheme members has the effect of discounting what would have been a costs 'floor breach' at the 2016 valuation and a corresponding increase in accrued member benefits. It is no answer to say that any costs 'ceiling breach' relating to the 2016 valuation is to be waived.

Concern about the effectiveness of the cost control mechanism and the Government Actuary's review and recommendations is noted but these and the resulting Government proposals (which have been the subject of public consultation this year) concerning prospective changes to the cost control mechanism are irrelevant to the current set of valuations and have failed to engage with the issue of the introduction and continuation of the pause and the inclusion of the McCloud remedy costs in the 2016 valuation of the costs cap. Those issues are so significant to the scheme and their members that they ought to have been addressed by consultation, and no decisions about them should have been made without regard to the requirements of the Public Sector Equality Duty.

The 2021 Directions are unlawful in that their instructions for the purposes of the actuarial calculation and completion of the 2016 valuation of the cost cap cost of the 2015 NHS Pension Scheme will involve or result in:

- (1) frustration of the policy and objectives of the relevant legislation (the Public Service Pensions Act 2013 and the NHS Scheme Regulations) rendering them *ultra vires*;
- (2) a breach of legitimate expectation concerning the operation of the cost control mechanism and deviation from the proper and expected calculation and accrual of pension benefits;
- (3) indirect age discrimination by burdening the costs, tax and administrative liabilities associated with the McCloud remedy on members of the Scheme as a whole (with/without having the benefit of that remedy individually); and, relatedly,
- (4) breach of the non-discrimination rule implied by section 61 of the Equality Act 2010; and
- (5) unlawful interference with the value of pension benefits contrary to Article 1 Protocol 1 rights under the ECHR.

Furthermore, the BMA is concerned that in making and implementing the 2021 Directions there has been material failure:

- (6) to carry out any or any adequate consultation with the NHS Scheme Advisory Board and/or with scheme members and representative bodies (including the BMA);
- (7) to carry out any or any adequate equality impact assessment as required by section 149 of the Equality Act 2010; and,
- (8) through administrative inaction without justification, to lift the suspension of the cost control mechanism promptly in order to promote the relevant legislative policy and objectives.

The pause of the cost control mechanism has resulted in loss of member benefits and/or the overpayment of member contributions throughout the period of its suspension. It has frustrated the rectification process that the cost control mechanism was intended to facilitate, which was already underway and would have resulted in a significant increased change to the rate of accrual.

The impact of the changes brought about by the 2021 Directions is for NHS pension scheme members to suffer loss and hardship generated by the delay to the proper working of the cost cap mechanism in a variety of ways, including:

- loss of value in pension benefits
- increased tax liability
- administrative costs and uncertainty relating to career choices and financial planning.

Those adverse consequences may be compounded further by the disproportionate impact upon those with a protected characteristic(s).

The BMA maintains that the facts and circumstances giving rise to the suspension of the cost control mechanism, and its protracted continuation, are unjustifiable.

#### **8. Action that the defendants are expected to take**

HM Treasury is expected to urgently acknowledge the defects of the 2021 Directions set out above and amend/revoke them so that the costs of the McCloud remedy are excluded from the cost cap cost valuation of the NHS 2015 Scheme (and other public service pension schemes also subject to their provisions). The Secretary of State is then expected to resume and conclude the **cost cap rectification process**.

#### **9. Details of information/documents sought**

Please provide us with information, documents and correspondence evidencing any consultation relating specifically to the decision to include McCloud remedy costs as a member cost for the purpose of resuming the cost control valuation for the 2016 valuation of the NHS 2015 Scheme.

Please provide us with information and documentation material to any equality impact assessment carried out in relation to the decision to include McCloud remedy costs in the 2016 valuation of the NHS 2015 Scheme.

#### **10. Address for reply and service of court documents**

The address given at the head of this letter should be used.

#### **11. Proposed reply date**

A response to this pre-action protocol letter is required no later than Friday 3 December 2021.

Yours faithfully



**Capital Law Limited**

cc. Her Majesty's Treasury, Secretary of State for Health and Social Care, Government Actuary