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Addendum - BMA letter to the Chancellor – 21 September 2022

BMA overview: Pension taxation crisis

The BMA has been highlighting the absurdity of the current punitive pension taxation rules for many years. This view is shared by many independent experts and the Health and Social Care Select Committee described the fact that pension taxation was driving doctors away from the NHS right at the very time they are needed the most, as a "national scandal". The spiralling rate of inflation has simply added petrol to the fire and unless urgent action is taken, there will be an unprecedented loss of senior staff across the NHS this financial year. Already, rates of retirement reported for 2022-23 have increased by more than 50% and without urgent action, this not only makes NHS recovery impossible, but potentially threatens its long-term survival.

The BMA is not calling for tax breaks or preferential treatment for doctors but instead a fair and progressive system of taxation that does not penalise doctors for working more or delaying retirement. We have outlined the actions required to solve this problem once and for all. Rather than being expensive solutions, these solutions are likely to have minimum adverse impact on government finances and are likely to deliver financial benefits to government through delaying retirements (thereby deferring pension payments) and reducing costs on locum and agency spend within the NHS. This is before the wider economic benefits of improving the health of the nation and reducing waiting times are considered. **The BMA Pensions Committee have outlined the following solutions that must be implemented to avert a workforce crisis:**

Long term solution - tax unregistered scheme

We are clear that the long-term solution to the pension taxation crisis is a tax unregistered scheme for those impacted by pension taxation in the NHS. When faced with similar recruitment and retention problems with the judiciary because of these taxes, the UK government introduced a tax unregistered scheme. This immediately addressed the issue and resulted in more judges being appointed. This is a fundamentally fair system, it ensures that the correct amount of tax is paid on pension growth, and as no tax relief is provided on employee pension contributions, there is no requirement to subject scheme members to either the Annual Allowance (AA) or Lifetime Allowance (LTA). We recognise that the contribution rates in the judicial scheme are significantly lower than for higher earners in the NHS and that accrued benefits are greater. We also recognise that there is much greater variability in the NHS in terms of earnings. Therefore, we are not suggesting that a tax unregistered scheme would look identical to the one implemented in the judiciary. However, we believe there are significant benefits in such an arrangement (on an opt-in basis) for those impacted by pensions taxation in the NHS. Initial discussions in the NHS Scheme Advisory Board on such a scheme with other unions have been positive and we would welcome the opportunity to discuss this in more detail.

As NHS higher earners do not currently benefit from tax relief in the first place because of the contribution structure, extending such arrangements to the NHS would be particularly effective. The benefit of such a scheme is that it would break the link between how much work doctors do and receiving large punitive tax bills, which in many cases result from pension 'growth' that is never received. However, it would also ensure that the doctors pay the correct amount of tax on their pension savings and is fair to the taxpayer.

Initial modelling from the BMA and our actuarial partners suggests that introducing a tax unregistered scheme for doctors would also have an overall positive impact on Treasury Finances, through a combination of delaying retirement (therefore deferring payment of lump sums and pension) and reducing the costs to the NHS of replacing lost capacity through locum and agency fees.

However, we recognise that introducing a tax unregistered scheme will take time and in particular with spiralling inflation, there is a real urgency to take action now to prevent an exodus of senior staff. Therefore, the following actions are required:

Urgently Amend the Finance Act Section 235 & 234

CPI disconnect

The AA is only supposed to apply to pension growth above inflation. However, in this rapidly moving inflation environment, anomalies within the Finance Act (Section 235) mean that this is not the case as two different values of CPI inflation are applied. The issue arises that the pension opening value is calculated based on CPI from September of the preceding year, whereas revaluation of pensions is based on CPI from September of the current tax year. Simply amending Section 235 to ensure that the pension opening value is aligned with to the same tax year as the accrual change (not CPI from September last year), will solve this problem and ensure that he inflationary uplift of benefits is aligned with inflation in the same year. This will ensure that only “growth" above inflation would be subject to testing againstthe AA as was clearly originally intended.

Negative Growth

Although workers in the NHS will only receive one NHS pension, following the Public Sector Pension Reforms, many NHS staff are in both the 1995/2008 and 2015 pension schemes. Under the Finance Act, including section 234 and related regulations, these schemes are considered separately, and negative growth is unjustly ignored. Therefore, even though one or both schemes may have negative growth, this negative growth is not offset against positive growth in the other schemes. For example, if a member had £20,000 negative growth in the 1995/2008 scheme and £60,000 positive growth in the 2015 scheme, even though their combined pension growth was £40,000 and within the standard annual allowance, the 1995/2008 negative growth is considered to be “zero” and instead the member is taxed on the £20,000 excess in the 2015 scheme.

In addition, negative growth cannot be carried forward or backward in the same scheme to offset previous positive growth in those years. This is particularly problematic in the current inflationary environment because if as is hoped, inflation settles, then the CPI “disconnect” described above means that for many, their accrued pension will fall in real terms with the net result being that not only will have doctors paid large amounts of annual allowance charges on “non-existent Pseudogrowth” but that despite doing so their pension may have in fact fallen in real terms.

Recycling of Employer pension Contributions

The BMA has been calling for mandatory scheme level recycling of employers’ pension contributions forthose NHS workers who need to opt out of the scheme because of pension taxation. This is currently something which individual Trusts can choose to offer, but it is not mandated nationally by NHS Employers, and despite being supported by DHSC, its availability is variable and results in a “postcode lottery” for senior NHS workers. Recycling of employer’s pension contributions is commonplace in other sectors and is largely cost neutral for the employer and fair to those working in the NHS. Most importantly, it could improve the retention of senior NHS staff at a time when they are needed the most. The Health & Social Care Committee recently suggested that Government should “instruct” national bodies to offer this.

Introduction of Partial Retirement with Pensionable Re-employment and Late Retirement Factors

The 1995 pension scheme, which most senior NHS staff are a member of does not have the option for partial retirement, and staff in receipt of their 1995 pension are prevented from re-joining the 2015 scheme. In addition, whilst the value of pension is actuarily reduced if members retire early, in the 1995 scheme the value is not increased if members work beyond normal pension age. This therefore acts as a powerful driver to retire at or before the age of 60, and indeed members can be significantly financially disadvantaged by delaying retirement. Introducing the option of partial retirement with pensionable reemployment, together with introducing late retirement factors will correct this unfair situation. However, this solution alone will not solve the problem and it is essential that it is combined with the changes to the Finance Act and in the longer term a tax unregistered scheme.

Repeat of the 2019/20 Annual Allowance compensation scheme
Given the urgent nature, and significant impact CPI on senior doctors and senior NHS staff, if the above changes cannot be implemented quickly, a repeat of this compensation should be considered. This would stabilise the workforce and reduce the need for this group to consider retiring or reducing work over the next 12 months as it would prevent the penalty associated by being taxed on non-existent pension “pseudogrowth” that arises due to the anomalies within the Finance Act. It has been implemented rapidly in the past and is a fully operational solution that could be introduced immediately. However, it is essential that if this is utilised it covers all four nations across the UK.

Why flexibility suggested by the Secretary of State and NHSEI won’t work
We are disappointed to hear the suggestion from NHS Employers and the Secretary of State to the HSCC that the solution to the outstanding pension taxation problem lies in the use of pension flexibilities. Whilst it may help those on lower incomes to partially contribute towards their pension, we are clear that it is absolutely not a solution to the problem with pension taxation.

The Government has conducted two prior consultations on pension flexibility over the last 4 years. The first “50:50” consultation was pulled and the second “decile flexibility” consultation was rejectedby both members and the government. A third attempt to push flexibility as the solution will not only delay but will not solve the problem, leading to thousands more doctors retiring over the next year.

The option to “flexibly” contribute towards an NHS pension doesn’t work for several reasons. Firstly, it adds another layer of incredible complexity to an already extremely complicated pension scheme and pension tax system. Secondly, scheme members will not know their own pension growth position during a given tax year and once a tax year has ended, there is no ability to retrospectively adjust your pension inputs, so any flexible options are not available. The complexity is such that you cannot predict your pension growth in advance, even with specialist advice and if trying to “guess” the level of accrual, it is very likely that the majority will over or under contribute. The penalties for guessing wrong are so severe and the complexity so high that most members simply won’t be able to use this option. Furthermore, without recycling of the full value of the employers’ contribution (less employers NI) being available, flexibility (i.e., reducing how much youcontribute towards your pension) is simply an overall pay cut and particularly given the successive below inflation pay awards over many years, this will simply result in more doctors planning to leave the NHS.

As an immediate next step, I hope that a meeting between us can take place in the coming days to discuss these solutions in more detail, and to provide any additional information which you may need.

Yours sincerely,

VSharma

Dr Vishal Sharma
BMA pensions committee chair