Summary
- Transfer incentive exercises have proved controversial in the private sector, but should not exist in the public sector, because members of unfunded public-service schemes cannot transfer out of them.
- LGPS members can transfer out of the scheme, but few have done so.
- Some public-sector employers, including private-sector outsourcers delivering public services, may be tempted to encourage staff to opt out of the public service schemes – the employer must tread carefully to avoid legal/regulatory risks.
- It is conceivable that a future government might want to encourage transfers out of the public service schemes, but this would be extremely difficult in practice.

Jumped or pushed?

The controversial issue of employers encouraging staff to opt out of DB schemes shouldn't really exist in the public sector, because members of unfunded public-service schemes are unable to transfer pension benefits out of the scheme. But, as David Adams explains, some public-sector workers can use such transfers; and public-sector employers could find themselves in legal and regulatory hot water if they encourage staff either to transfer out or to opt out of their public-service pension rights altogether

One controversial consequence of the freedom and choice reforms has been the development by some private-sector employers of incentive programmes designed to promote the option to members of DB schemes to transfer out of the scheme into a DC scheme – which may not always be in the member's long-term financial interests.

This issue has barely existed in relation to the public-service pension schemes, because most public-sector schemes are unfunded, so it is unlikely to be able to provide a transfer value in cash – and in any case members of these schemes have not been given the right to transfer out of them. But members of the Local Government Pension Scheme (LGPS), which is funded, do have the right to request a transfer. In addition, some public-sector employers may be tempted to encourage their employees to opt out of a public-service scheme, although any employer deemed to be offering an incentive to transfer or opt out of a public-service scheme risks breaching The Pensions Regulator's (TPR) guidelines; and may be subject to legal challenge, in the near or long term. Bevan Brittan employment, pensions and immigration senior associate, Philip Woolham, says his firm has advised employers in this position.

Members of the LGPS who want to transfer out of the scheme must do so at least a year before retirement age; and are required to take independent financial advice if the value of their accrued pension benefits is greater than £30,000. Research completed by the Local Government Pensions Committee suggests very few are doing so: no more than a handful of the 2.2 million or so active and 2.3 million deferred LGPS and LGPS Scotland members. "It's not a big issue for us at this point," says LGPS Advisory Board secretary, Jeff Houston.

But Houston also says some employers are getting quite close to encouraging employees to opt out of the scheme. "It will be employers skirting very close to the edge: 'If you opt out, I'll pay you a bit more,'" he says. "That's either trying to reduce the number of people in the scheme, or they are seeking to repackage benefits in a way that applies to the individual who might already be up to the lifetime allowance."

The issue of the tapered lifetime allowance has caused some major problems in the NHS during the past two years, with some staff reducing their hours in order to avoid breaching annual or lifetime allowances, or leaving the NHS scheme altogether. Woolham says Bevan Brittan has seen cases where individuals working for local authorities have found themselves in the same position.

"We're being asked to advise on what would be classed as an incentivisation package an employer could offer those employees," he says. "You can incentivise someone to move from one qualifying scheme to another, but you can't incentivise someone to opt out. We've seen situations where someone's pay has increased after they've opted out, although you don't have proof that the offer of the latter has encouraged the former."

Temptation

Pensions and Lifetime Savings Association (PLSA) policy lead on master trusts, Craig Rimmer, says his organisation has seen no evidence of employers deliberately incentivising people to leave the public service schemes. Nor has Unison head of pensions, Glyn Jenkins – but he says the union has seen employers failing to put new employees into the scheme, or suggesting to members they should opt out.

Public-sector employers that might be tempted to encourage employees to transfer or opt out of public-service schemes include outsourcing providers from the private sector or the third sector delivering public services. Woolham has seen cases where an outsourcer has wanted to find a way of avoiding the obligation to maintain access to the public-service schemes for staff moving over to the outsourcer via Tupe. "We'd expect to see more of this, because the exposure to those risks can be very off-putting to the new employer," he says.

The key question, of course, is the level of awareness among the employees about their pension rights and their options. A similar question needs to be considered in relation to public-sector employees who opt out of the public-service schemes. More than 200,000 NHS workers have opted out of the NHS Pension Scheme since March 2014, according to figures released in answer to a written parliamentary question asked by Chris Skidmore MP in 2019; 43,309 did so in 2018/2019.

These figures include people who have opted out because of the tapered annual allowance issue – a 2019 survey from GP Online showed that 19 per cent of GPs had left the NHS pension scheme (12 per cent for good, 7 per cent temporarily) to avoid tax penalties. But Woolham says that in some cases, in his experience, around 20 per cent of new NHS employees aged 30 or under are opting out of the NHS pension scheme. People are more likely to opt out if the cost of living is particularly high where they live, or if they are not from the UK and not planning to work here in the longer term.

Pinsent Masons partner, Nick Stones, says similar trends are also visible in some parts of the education sector. "Contributions are getting higher and they don't see the long-term value in the pension," he says. "That's not due to the actions of an insidious employers, it's more a reflection of priority and lifestyle; and a lack of education about the importance of pension saving."

Trouble ahead

But awareness of pension rights is reasonably widespread in many parts of the public sector, in part because the past decade has seen an intermittent attack on public-sector pensions by some policymakers and commentators as being 'gold-plated', in comparison to much private-sector pension provision (although in reality the vast majority of public sector pensions are modest), and 'unaffordable' to the taxpayer. Unions have organised robust opposition to changes made to the schemes since 2010.

Although the government now predicts that the long-term effects of those changes will help to reduce spending on the unfunded public service pensions as a share of GDP, from about 2 per cent today to 1.5 per cent by 2070, there is plenty of scope for future conflict. We may see further legal challenges to the 2015 reforms following a Court of Appeal ruling that changes made to the firefighter's and judge's pension schemes discriminated against younger scheme members. The judgment may eventually cost the government £4 billion, as other public-sector workers consider launching further legal action.

So might a future government see encouraging public sector employees to transfer out of the scheme as a means of reducing costs to the public purse? Any government seeking to do so would face very serious financial challenges. "You just keep hitting the cashflow issue," says Houston. "If the Treasury thought this was a good idea they would have allowed the unfunded schemes to go down that route. The fact they have stopped them from doing so shows that it doesn't matter how much tax you get in, your short-term cash problem is unfundable."

Instead, the government, public sector employers and scheme members should be focused on the tapered allowance issue, says Woolham. "We're running into a position where it's not just the highest-paid staff that are falling foul of annual and lifetime allowances," he says. "If you've been in a public-service scheme for 30 or 40 years you could be getting to the point where you're not able to save any more into your pension in a tax-efficient manner."

Public-sector employers seeking to resolve this issue will need to tread very carefully, he suggests. "TPR states you should start from the position that the best option for the employee is that they should remain in their valuable pension scheme," he says. "So you should always ensure that the offer you're making is in the best interests of the individual. Because these things can come back to bite you in 20 or 30 years in some cases, not just two or three."

Written by David Adams, a freelance journalist