EXPLANATORY MEMORANDUM TO

THE MPS', SENEDD AND ASSEMBLY PENSION SCHEMES (TAX) REGULATIONS 2025

2025 No. 52

1. Introduction

1.1 This explanatory memorandum has been prepared by His Majesty's Revenue and Customs (HMRC) on behalf of His Majesty's Treasury and is laid before the House of Commons by Command of His Majesty.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Declaration

2.1 Tulip Siddiq MP, Economic Secretary to the Treasury confirms that this Explanatory Memorandum meets the required standard.

2.2 Gareth Cooper, Deputy Director for Public Service Pensions Remedy, Individuals Policy Directorate at HMRC confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Beverley Davies at HMRC telephone: 03000 512336 or email: policypensions@hmrc.gov.uk can be contacted with any queries regarding the instrument.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument addresses the tax consequences of changes arising from the rectification exercises carried out by the Parliamentary Contributory Pension Fund (PCPF), the Members of the Senedd Pension Scheme (Senedd Scheme) or an Assembly Members' Pension Scheme (Northern Ireland).

4.2 The rectification exercises aim to remedy the age discrimination that occurred when those pension schemes reformed their benefit structure. These exercises would have adverse tax consequences and this instrument will broadly put individuals back in the tax position they would have been in if the discrimination had not occurred.

Where does the legislation extend to, and apply?

4.3 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the United Kingdom.

4.4 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the United Kingdom.

5. Policy Context

What is being done and why?

5.1 The Government provides tax relief for pension saving under Part 4 of the Finance Act 2004 (FA 2004). An individual can have relief on their contributions to registered pension schemes and there are no limits on the amount of pension saving that an individual can have. However, to limit the amount of tax relief available, an individual will be subject to a tax charge if their pension saving in a tax year is more than their annual allowance and, before 6 April 2023, a further charge arose if an individual's pension saving over their lifetime exceeded their lifetime allowance.

5.2 Tax charges also apply if payments made out of tax-relieved pension saving do not meet the conditions set out in Part 4 of FA 2004.

5.3 In 2015, the Coalition Government introduced reforms to public service pensions. In 2018, transitional protections for older workers were found by the Court of Appeal to be discriminatory, and so the Government committed to rectifying this.

5.4 The PCPF, Senedd Scheme and Assembly Members Pension Scheme (Northern Ireland) were similarly reformed between 2015 and 2016 but the court judgment did not apply to them. To ensure fairness for members of these schemes, the schemes are voluntarily undertaking rectification exercises in line with the broader remedies for public service pensions and making the necessary changes in their scheme rules in order to rectify the discrimination.

5.5 Currently, pension tax relief and charges consider the value of the tax relief and benefits which a member has received in each and every tax year. As a result, significant changes to a member's benefits as is envisaged under the rectification exercises, could lead to unintended tax charges or unexpected tax windfalls, which this instrument addresses.

5.6 The rectification exercises being carried out by the PCPF and Senedd Scheme, and in due course the Assembly Members Pension Scheme (Northern Ireland), are not retrospective for tax purposes. This means that in some instances benefits payable as a result of a rectification exercise (rectification payments) could be taxable as unauthorised payments. It also means previous tax charges paid by, or in respect of, scheme members remain correct and due. Individuals will be paid tax redress payments where they have paid tax that would not have been due if the rectification exercise had been retrospective. This instrument addresses adverse tax consequences that arise in respect of rectification payments and tax redress payments.

5.7 From 6 April 2023, the Government made changes to the way pensions tax relief was limited by increasing the amount of the annual allowance and abolishing the lifetime allowance charge. As the rectification exercises are not retrospective for tax purposes, the increase in the annual allowance and abolition of the lifetime allowance would have unduly enriched some impacted members as they would not have had to pay tax that would have been due if the rectification exercise was retrospective.

5.8 This instrument provides for a one-off lifetime allowance windfall charge and a revised method for calculating the amount of annual allowance used (pension input amount) in the year members make their choice. The Government aims for members of the PCPF, Senedd Pension Scheme and the Assembly Members Pension Scheme (Northern Ireland) to receive tax treatment equivalent to that given to members under the public service pensions remedy. So this instrument also ensures that they do not

directly benefit from changes to the tax treatment of pensions which only took place after the discrimination occurred.

5.9 This instrument does not affect the Scottish Parliament Members' Pension Scheme, as no reforms took place in respect of their pension scheme.

What was the previous policy, how is this different?

5.10 As a result of the rectification exercises being implemented within the pension scheme rules for MPs and Members of the Senedd and Northern Ireland assembly, the existing tax treatment would result in some adverse tax outcomes for impacted members.

5.11 This policy looks to, as far as possible, put impacted members back in the tax position they would have been in if the discrimination had not occurred.

6. Legislative and Legal Context

How has the law changed?

6.1 The Finance Act 2024 provides the power to make provisions in relation to rectification payments or tax redress payments from a relevant pension scheme, along with increases, decreases and tax windfalls as a result of a relevant rectification exercise.

6.2 This instrument provides that where, as a result of a rectification exercise, a refund of contributions is payable, that payment is treated as an authorised payment that is not subject to income tax.

6.3 Where, as a result of a rectification exercise, pension arrears are paid, this instrument provides that the payment is treated as an authorised payment and taxed as pension income in the tax year in which the payment is made.

6.4 Where, as a result of a rectification exercise, a further defined benefits lump sum death benefit is paid, this instrument provides that this further lump sum payment receives the same tax treatment as the original lump sum death benefit payment.

6.5 This instrument provides that where an additional lump sum is paid as a result of the rectification exercise to the personal representatives of a deceased member that the payment benefits from the same tax-free status that it would have had were the member alive and the discrimination had not occurred.

6.6 This instrument provides that a tax redress payment is not subject to income tax and where paid from a registered pension scheme is treated as an authorised payment. Tax redress payments may be made to an individual where income tax has been paid in respect of the pension rights accrued under a relevant pension scheme or payments from the scheme which would not have arisen if the rectification exercise had been retrospective. A tax redress payment may also be made where an individual is required to pay a contribution to the scheme and the effective amount of relief they receive in respect of that contribution is less than the relief that would have been given if the rectification exercise had been retrospective.

6.7 This instrument provides for a tax charge known as the lifetime allowance windfall charge. Where a member started to take their benefits before 6 April 2023 and those benefits increase as a result of a rectification exercise, the lifetime allowance windfall charge may apply. If the extra benefits mean that the individual would have been subject to a lifetime allowance charge had the rectification exercise been retrospective, then the charge will apply. This provides for fair treatment compared to other scheme members and those subject to the public service pensions remedy. To

reduce complexity this instrument provides that the scheme administrator is solely liable to the charge which they should deduct from the member's benefits before they are paid, and then report and pay the tax to HMRC using the Accounting for Tax return process.

6.8 This instrument modifies how a member's pension input amount is calculated for the tax year that the rectification exercise takes place and requires the scheme administrator to give the member information about their scheme pension input amount on this modified basis. These rules also take account of a difference in the operation of the PCPF, where benefits are changing between two arrangements, and the other schemes which operate a single arrangement. It also restricts how carry forward is used to reduce an annual allowance charge; carry forward may be used only for a year in which the individual was an active member of any registered pension scheme. This is to ensure that pensioner and deferred members of the scheme, who would not have used their annual allowance in previous years, do not receive an unfair advantage.

6.9 This instrument also provides that for the three tax years following the tax year in which the rectification exercise took place the amount of carry forward available to reduce an annual allowance charge is based on the total pension input amounts that would have arisen if the rectification exercise had been retrospective.

6.10 A member's benefits may have been reduced because the scheme administrator paid an annual allowance or lifetime allowance charge on behalf of the member and that tax charge would not have arisen if the rectification exercise had been retrospective. In these circumstances the member's benefits may be adjusted to remove the benefit reduction that would not have occurred if the rectification exercise had been retrospective. This instrument ensures that this benefit adjustment is disregarded when calculating the pension input amount in the tax year that the adjustment is made.

6.11 This instrument also ensures that where the annual rate of a scheme pension reduces as a result of the rectification exercise, the ongoing reduced pension payments continue to be authorised payments.

6.12 This instrument will have effect for the 2024-25 tax year and subsequent tax years.

Why was this approach taken to change the law?

6.13 As the rectification exercise is not retrospective for tax purposes, this is the only possible approach to make the necessary changes in order to allow the pensions tax regime to operate as intended by Parliament from 6 April 2024, when members make their choice. This instrument is made under the power provided in the Finance Act 2024 to make the necessary changes.

7. Consultation

Summary of consultation outcome and methodology

7.1 A formal consultation was not considered necessary as the small number of scheme administrators and individuals potentially affected limits the benefit of such an approach. However, drafts of the regulations were provided and discussed with the scheme administrators in relation to MPs and Members of the Senedd and their pension schemes for their technical feedback to ensure they would operate in conjunction with the changes to their scheme rules. Where necessary a similar informal consultation will be carried out with officials of the Northern Ireland Assembly when they finalise their approach.

8. Applicable Guidance

8.1 Guidance has been published on the gov.uk website for individuals explaining how changes in this instrument that they need to report will work[1].

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A Tax Information and Impact Note covering this instrument was published on 22 November 2023 alongside the Autumn Statement and is available on the gov.uk website[2]. It remains an accurate summary of the impacts that apply to this instrument.

Impact on businesses, charities and voluntary bodies

9.2 There is no, or no significant, impact on business, charities or voluntary bodies because this issue arises within the relevant public service scheme.

9.3 The legislation does not impact small or micro businesses.

9.4 The impact on the public sector is only in relation to the scheme administrators of the PCPF, the Senedd scheme or Assembly Members Pension Scheme (Northern Ireland). They will be required to calculate the member's pension input amount to account for the change in benefits and provide a relevant pension savings statement. They will have to tell HMRC using the Event Report and pay the tax charges on the Accounting for Tax return.

9.5 They will also be required to establish whether the member would have been liable to the lifetime allowance charge, had their rectification exercise been retrospective, and where applicable they will become liable for a charge and must report and pay the tax charge on the Accounting for Tax return.

9.6 To identify the amount of tax redress payment that will not be subject to tax, schemes will need to identify the amount of annual allowance charge or lifetime allowance charge that would have been due if the rectification exercise had been retrospective.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring of this legislation is that it will be monitored through communications with the relevant pension schemes and taxpayer groups.

10.2 The instrument does not include a statutory review clause as it falls within section 28(3)(a) of the Small Business, Enterprise and Employment Act 2015.

[1] Guidance for tax treatment of pensions remedies: https://www.gov.uk/government/publications/pensions-schemes-newsletter-158-april-2024/newsletter-158-april-2024#pension-remedies-for-mps-mss-and-members-of-the-northern-ireland-legislative-assembly--tax-treatment-of-annual-allowance-and-lifetime-allowance

[2] Tax Information and Impact Note: https://www.gov.uk/government/publications/taxation-of-members-of-parliament-members-of-the-senedd-and-members-of-the-legislative-assembly-of-northern-ireland-pension-reform-remedies/taxation-of-the-pension-remedies-for-members-of-parliament-members-of-the-senedd-and-members-of-the-legislative-assembly

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 This instrument contains the first use of the powers in section 15 of the Finance Act 2024. Section 15(8)(a) provides that regulations made before 6 April 2025 may have effect in relation to the tax year 2024-25.

12. European Convention on Human Rights

12.1 The Economic Secretary to the Treasury has made the following statement regarding Human Rights:

"In my view the provisions of the MPs', Senedd and Assembly Pension Schemes (Tax) Regulations 2025 are compatible with the Convention rights."

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").