EXPLANATORY MEMORANDUM TO

THE SOCIAL SECURITY (CONTRIBUTIONS) (AMENDMENT NO. 3) REGULATIONS 2025

2025 No. 325

1. Introduction

1.1 This explanatory memorandum has been prepared by His Majesty's Revenue and Customs (HMRC) and is laid before Parliament by Command of His Majesty.

2. Declaration

2.1 Torsten Bell, Minister for Pensions at the Department for Work and Pensions and HM 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 Ativie Edebiri at HMRC Telephone: 0300 584748 or email: ativie.edebiri@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 National Insurance contributions (NICs) consequences 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. The adverse tax consequences of the rectification were addressed through the MPs', Senedd and Assembly Pension Schemes (Tax) Regulations 2025 (S.I. 2025/52). Those regulations exempted compensation, known as tax redress, from a tax liability which would not have occurred if the rectification exercise had been retrospective.

4.3 The tax redress paid as a result of the rectification exercises would also have adverse NICs consequences. This instrument will broadly put individuals back in the NICs positions they would have been if the discrimination had not occurred. They do this by disregarding the tax redress payment made from qualifying earnings.

Where does the legislation extend to, and apply?

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

4.5 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 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.

5.2 The PCPF, Senedd Scheme and Assembly Members' Pension Scheme (Northern Ireland) were similarly reformed between 2015 and 2016 but the court judgement did not apply to them. To ensure fairness to 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.

5.3 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 or NICs charges.

5.4 The rectification exercises being carried out by the PCPF and the 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 exercises had been retrospective.

5.5 The MPs', Senedd and Assembly Pension Schemes (Tax) Regulations 2025 S.I. (2025/52) address the adverse tax consequences that arise in respect of tax redress payments by exempting the qualifying amount of a tax redress payment from income tax and specifying how the qualifying amount is to be calculated. This instrument amends the Social Security (Contributions) Regulations 2001 to provide that the qualifying amount of a tax redress payment will be disregarded in the calculation of earnings for the purpose of establishing liability to Class 1 NICs.

5.6 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?

5.7 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 and NICs treatment would result in some adverse tax and NICs outcomes for impacted members.

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

6. Legislative and Legal Context

How has the law changed?

6.1 Section 3(2) and (3) of the Social Security Contributions and Benefits Act 1992, and section 3(2) and (3) of the Social Security Contributions and Benefits (Northern Ireland) Act 1992 contain a regulation-making power to establish the basis on which the amount of earnings shall be calculated, and that payments of a particular class or description can be disregarded from that calculation. In accordance with those sections, this instrument is made with the concurrence of the Secretary of State and the Department for Communities (Northern Ireland).

6.2 Part 6 of Schedule 3 to the Social Security (Contributions) Regulations 2001 (payments to be disregarded in the calculation of earnings for the purposes of earnings-related contributions) specifies the pension payments and pension contributions to be disregarded for the purposes of establishing liability to pay Class 1 NICs.

6.3 This instrument amends Part 6 of Schedule 3 to the Social Security (Contributions) Regulations 2001 to provide that the qualifying amount of a tax redress payment, as defined in section 15(4) of the Finance Act 2024, will be disregarded in the calculation of earnings for the purpose of establishing liability to Class 1 NICs.

Why was this approach taken to change the law?

6.4 This is the only possible approach to make the necessary changes.

7. Consultation

Summary of consultation outcome and methodology

7.1 No formal consultation exercise has been held as these are minor changes which are wholly relieving to the taxpayer.

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.

[1] Guidance for tax treatment of pension 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

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 and Assembly Members' Pension Scheme (Northern Ireland). This instrument will apply to these scheme administrators in the small number of cases where tax redress payments are greater than the qualifying amount. In those cases, the excess will not be subject to NICs.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring 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.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None.

12. European Convention on Human Rights

12.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation no statement is requires.

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").