EXPLANATORY MEMORANDUM TO

THE SOCIAL SECURITY (CONTRIBUTIONS) (AMENDMENT NO. 4) REGULATIONS 2026

2026 No. 684

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 MP, Minister for Pensions at the Department for Work and Pensions and HM Treasury confirms that this Explanatory Memorandum meets the required standard.

2.2 Charlotte Axson, Deputy Director for National Insurance Policy, at HMRC confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Ativie Edebiri at HMRC can be contacted by email at the following address with any queries regarding the instrument: nics.policy@hmrc.gov.uk.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument makes changes to the National Insurance contributions (NICs) rules to ensure that the remedy to age discrimination that arose from the 2015 public service pension reforms do not give rise to unintended NICs charges for certain members of the Armed Forces Pension Scheme.

4.2 The instrument ensures that where, following a choice made as part of the remedy, members of the Armed Forces Pension Scheme 1975 receive payments that are equivalent to early departure payments under the Armed Forces Pension Scheme 2015, those payments are treated consistently for NICs purposes. The instrument does this by providing that such payments are disregarded when calculating earnings for Class 1 NICs, so that affected individuals are not placed in a different position purely because of how the benefits are paid.

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 This instrument supports the Government's approach to addressing the age discrimination that arose from the 2015 public service pension reforms, commonly

referred to as the "McCloud remedy". The overall aim of the remedy is to put those affected in the financial position they would have been in if the discrimination had not occurred, so far as is possible.

5.2 In the Armed Forces pension schemes, certain individuals can, following choices made as part of the remedy, become entitled to benefits that are comparable to early departure payments under the reformed scheme. These payments would normally be made under the Early Departure Payments Scheme 2015 and would not give rise to a NICs charge.

5.3 However, in some cases those equivalent payments are instead made from the Armed Forces Pension Scheme 1975. Without legislation, this difference in how the payments are made could lead to a different NICs outcome, even though the nature of the benefits is effectively the same.

5.4 This instrument ensures that these payments are treated consistently for NICs purposes by providing that they are disregarded when calculating earnings for Class 1 NICs. This avoids individuals being disadvantaged as a result of the way the remedy operates and ensures that the policy intention of the remedy is achieved.

What was the previous policy, how is this different?

5.5 Under existing NICs rules, early departure payments made under the Armed Forces Pension Scheme 2015 are already disregarded from Class 1 NICs. This reflects the established policy that such payments should not give rise to NICs liabilities.

5.6 Prior to this instrument, the rules did not cover situations where similar payments arise under the Armed Forces Pension Scheme 1975 as part of the remedy. This meant that individuals could face different NICs treatment depending on how their benefits were delivered.

5.7 This instrument changes that position by extending the existing disregard to cover these cases. As a result, individuals receiving equivalent payments will be treated consistently for NICs purposes, regardless of which scheme pays the benefits.

6. Legislative and Legal Context

How has the law changed?

6.1 Sections 3(2) and (3) of the Social Security Contributions and Benefits Act 1992, and Sections 3(2) and (3) and of the Social Security Contributions and Benefits (Northern Ireland) Act 1992 contain 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.

6.2 Section 175(3) of the Social Security Contributions and Benefits Act 1992 and Section 171(3) of the Social Security Contributions and Benefits (Northern Ireland) Act 1992 contain general regulation-making powers in relation to the NICs regime.

6.3 Part 6 of Schedule 3 to the Social Security (Contributions) Regulations 2001(S.I. 2001/1004) (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.

6.4 Prior to this instrument, that Schedule includes a provision to disregard early departure payments made under the Armed Forces Pension Scheme 2015 but does not extend to equivalent payments arising under the Armed Forces Pension Scheme 1975

as a result of a Section 6 or Section 10 election under the Public Service Pensions and Judicial Offices Act 2022.

6.5 This instrument amends Part 6 of Schedule 3 to the Social Security (Contributions) Regulations 2001 by inserting an additional category of payments to be disregarded. It provides that where an individual makes a section 6 or section 10 election in relation to remediable service under the Armed Forces Pension Scheme 1975, and this results in the payment of benefits equivalent to those provided under the Early Departure Payments Scheme 2015, those payments will be disregarded in calculating earnings for Class 1 NICs purposes.

Why was this approach taken to change the law?

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

7. Consultation

Summary of consultation outcome and methodology

7.1 Informal technical consultations with public service pension scheme stakeholders were held to review draft regulations and guidance. Schemes generally supported the approach, mainly requesting clarification on process implications, deadlines and timescales which will be addressed through published guidance.

7.2 A more formal technical consultation was not considered necessary as the policy and approach was developed in conjunction with public service pension scheme stakeholders, and some provisions only impact a limited number of public service pension schemes.

8. Applicable Guidance

8.1 We currently anticipate full guidance to be released through the McCloud pension scheme newsletters in June 2026, as has been the case with previous McCloud regulations.

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 27 October 2021, alongside the Finance Bill, and is available on the gov.uk website[1]. 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 the issues in this instrument arise within the relevant public service pension schemes.

9.3 The legislation does not impact small or micro businesses.

9.4 There is no, or no significant, impact on the public sector because this instrument makes amendments to support the administration of the existing public service pension schemes remedy and to ensure that unintended NICs consequences do not arise from its implementation. Any impacts on public service pension schemes and

[1] Tax Information and Impact Note: https://www.gov.uk/government/publications/taxation-of-public-service-pension-reform-remedy/taxation-of-public-service-pension-reform-remedy

HMRC are expected to be limited to minor administrative adjustments associated with delivering the remedy more effectively.

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 procedure and does not amend primary legislation no statement is required.

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").