



**Armed Forces' Pensions
and Compensation:
Ministry of Defence Response
to the House of Commons
Defence Committee's
First Report
of Session 2003–04**



**Armed Forces' Pensions
and Compensation:
Ministry of Defence Response
to the House of Commons
Defence Committee's
First Report
of Session 2003–04**

Presented to Parliament by the
Secretary of State for Defence
by Command of Her Majesty
January 2004

© Crown Copyright 2004

The text in this document (excluding the Royal Arms and departmental logos) may be reproduced free of charge in any format or medium providing that it is reproduced accurately and not used in a misleading context. The material must be acknowledged as Crown copyright and the title of the document specified.

Any enquiries relating to the copyright in this document should be addressed to The Licensing Division, HMSO, St Clements House, 2-16 Colegate, Norwich NR3 1BQ. Fax: 01603 723000 or e-mail: licensing@cabinet-office.x.gsi.gov.uk

ARMED FORCES' PENSIONS AND COMPENSATION: MINISTRY OF DEFENCE RESPONSE TO THE HOUSE OF COMMONS DEFENCE COMMITTEE'S FIRST REPORT OF SESSION 2003–04

Presented to Parliament by the Secretary of State for Defence and Under Secretary of State and Minister for Veterans Affairs by Command of Her Majesty

Introduction

1. The Government is pleased to present its response to the House of Commons Defence Committee's First Report of Session 2003–2004 on Armed Forces' Pensions and Compensation. It is published before the second reading of the Armed Forces (Pensions and Compensation) Bill in the House of Commons and the Government hopes that this will assist the debate as the legislation progresses.

Lack of progress

It seems from the evidence we have received that several crucial elements of the schemes have still not been finalised despite an unusually long period of review and consultation. It is vital that these elements are clarified by the time primary legislation is brought before Parliament, so that an informed debate is possible on the issues at stake. It would be wholly unacceptable if Parliament were asked to approve enabling legislation without a clear understanding of its implications for Armed Forces personnel and their dependants. (Paragraph 11)

2. It has taken longer than originally expected to finalise the new Armed Forces Pension Scheme (AFPS) and Armed Forces Compensation Scheme (AFCS). This largely reflected the need to undertake additional work to resolve the substantial issues raised in public consultation and the new issues raised by the Government's December 2002 Green Papers¹ on wider pensions policy. The latter in particular required a totally new approach to the benefits paid to those leaving before the age of 55 who are currently entitled to an Immediate Pension (IP).

3. It is normal at this stage of introduction of new schemes for a certain amount of detail to be unresolved; but in general the design of the scheme and its working arrangements have been set out in substantial detail in two framework documents which were placed in the libraries of both Houses of Parliament (and provided to the Select Committee) to coincide with the first reading of the Armed Forces (Pensions and Compensation) Bill 2003.

4. The Government considers that the level of detail provided is sufficient to allow a clear understanding of the implications of the new schemes. The exception to this is the Early Departure Payment (EDP) scheme which has been under development over the last year to respond to the changes put forward in the Government's Green Paper on Pensions Tax Simplification. The position on this is set out in paragraphs 10-12.

¹ Simplifying the taxation of pensions: increasing choice for all. (December 2002) and Simplicity, Security and Choice: working and saving for retirement. (December 2002).

Cost Basis for schemes

The Government intends to use savings that it is making within the pension scheme not only to improve other benefits to personnel, but also to cover the estimated cost of personnel and their dependants living longer. (Paragraph 16)

The Government is proposing to reduce benefits to Armed Forces personnel on the basis that they will live for longer, without also giving them a real opportunity to work for longer within the public service. This is not reasonable. (Paragraph 19)

5. The Government does not consider that the use of savings to cover longevity costs represents a reduction in benefits. Payment of pensions for an extended period in retirement to reflect longevity improvements is a benefit improvement that would commonly be covered in the wider economy by increased member contributions or by reductions in benefits elsewhere. The costs of longer payment of pensions will generally be covered elsewhere in the public services by introduction of a later normal pension age and the proposed response to this pressure for the Armed Forces does not therefore disadvantage Service personnel in this respect. The Government considers it appropriate that they should similarly contribute to this benefit. The change has not, however, reduced the value of benefits paid at the normal pension age for the scheme (55), and the benefits paid to members of the Armed Forces leaving at mid-career remain uniquely generous, even though reduced in value. The benefits paid at normal retirement age have been enhanced, notably through the major improvement in the value of widows' pensions. The preserved pension age has been deferred in line with the Government's broader policy on longer working lives, but the benefits paid to members at that point have not been reduced and, for the new scheme, opportunities have been offered to accrue additional qualifying years for a pension, for example through allowing qualifying service from an earlier age than at present.

6. The majority of Service personnel do not wish to serve a full career in the Armed Forces; many leave well before the full career point, having enjoyed the opportunity offered by a career in the Armed Forces of an exciting and challenging job and having acquired substantial transferable skills to allow a successful second career. For the rest, the Armed Forces can only retain a limited number through to a full career at age 55 because of their fitness requirements. This has long been recognised and is compensated for in the new scheme by an early leavers' package for those leaving from age 40 and by a full career pension that comes into payment at the unusually early age of 55. The Government continues to regard this as a very fair package given the opportunities for a second career arising from the skills acquired by Armed Forces personnel. Future career structures may change, reflecting both technological developments and the changing nature of future warfare, and the new AFPS provides the flexibility to allow longer careers where needed (with continued pension accrual up to 40 years of service).

The Government is basing its decision to reduce the cost of the pension scheme on the expectation that each individual member of the pension scheme will cost the MoD more in future because of increased longevity. However, because of the reduction in Service numbers over the last two decades, we would expect the MoD's *total* pensions bill to decrease just as the financial effects of increased life expectancy kick in. In terms of the total cost to the public purse, there is no need to adjust the pension scheme to reflect increased longevity in order to achieve 'cost neutrality'. It is only fair to point out that any cost increases as a result of pensioners living for longer are likely to be more than compensated for by the reduction in the total number of pensioners. (Paragraph 22)

7. It would not be appropriate to increase pensions because the size of the Armed Forces was reducing, any more than the reverse would be appropriate. The reducing size of the pensioner population, does not, in any event provide savings to the Ministry of Defence (MOD). The cost of pensions to the MOD's budget for managing the Armed Forces is met through employer contributions determined by the annually accruing pensions liability for those currently serving. As in other employments, the value of Armed Forces pay and pension benefits reflects the remuneration package required to recruit and retain personnel of the right quality and the special demands of that occupation. The decision that no increase in pensions expenditure was justified in recruitment and retention terms means broadly that the MOD's annual pensions cost will remain unchanged unless Armed Forces numbers were to increase or decrease, or there were a further change in actuarial assumptions.

With the introduction of the new pension scheme, the MoD has changed its definition of 'cost neutrality' to seek to ensure that the future cost of an average member of the new scheme should not exceed the current cost of an average member of the existing scheme. (Paragraph 25)

Personnel transferring to the new pension scheme will receive benefits of a lesser overall value than those remaining on the existing scheme. This would in many circumstances seem to be a fairly obvious disincentive to transfer. (Paragraph 26)

We have always been unhappy that the Government in its review of Armed Forces pensions has imposed on itself the constraint of how much current benefits cost, rather than looking more generally at what Armed Forces personnel deserve. We are even less happy now that it emerges that the Government proposes to reduce the overall value of benefits under the new scheme, compared with the existing scheme. The goalpost of 'cost neutrality' have been shifted — to the disadvantage of future personnel. (Paragraph 27)

8. The recosting of the current and new pension schemes is based on actuarial assumptions relating to a new entrant. This is more applicable to the new scheme which in the longer term will be made up predominantly of new entrants, than for the current scheme which includes significant numbers of more mature personnel. On this basis, the Government considers that those joining the Armed Forces under the new scheme will benefit more from longevity improvements than those on the current scheme and should therefore bear a greater share of the cost of longevity. It is also expected that those joining the Armed Forces under the new scheme will not require the same level as at present of early compensation when leaving service from around the age of 40. The current trend of improved transferable skills is expected to continue, reducing further the financial risk that has in the past attached to second careers. The apportioning of the cost of longevity and the measures taken to implement this are therefore considered to be justified and fair in objective terms, notwithstanding any considerations of cost-neutrality. The result is a pension scheme which, as demonstrated by the independent assessment of the new scheme proposals commissioned by the MOD², is good and expected to become increasingly generous as other schemes adapt to the same actuarial pressures that have been addressed. Such a high quality scheme is fully in line with what the Armed Forces deserve.

² Report on Armed Forces Pension Scheme. Addendum to the report on the proposals for a new Armed Forces Pension Scheme by Watson Wyatt LLP (Actuaries and Consultants) dated 12 September 2003.

Welcome improvements

The Government should ensure that any money which would have been paid to pensioners in the existing scheme were it not for the rise in the preserved pension age is used to improve other pension benefits. (Paragraph 31)

We welcome the MoD's decision to improve provision for dependants, particularly where personnel have died in service, given the unique commitment that these personnel make to the service of their country. (Paragraph 33)

It is essential that the schemes should be as clear as possible about when unmarried partners will qualify for benefits, both to avoid bad feeling among non-qualifying partners, and to avoid potentially expensive legal action. We welcome that fact that criteria have been developed against which to assess whether a substantial and exclusive relationship exists between unmarried partners, which would entitle them to benefits. (Paragraph 41)

9. The Government is pleased to note the Committee's support for the substantial improvement to the benefits provided for dependants in the new schemes. The final AFPS package gives due recognition to the particular demands of Service life, in particular the effect on Service dependants, and this was the basis for the increase in death-in-service benefit to four times pay (paid regardless of the cause of death), the 25% improvement in widows' pension and the extension of benefits to Service partners in substantial relationships. The MOD is pleased to note the Committee's acknowledgement that there is a clear set of criteria for establishing entitlement to unmarried partner benefits.

Early Departure Scheme

We are disappointed that details of the new Early Departure scheme are not yet available to inform Parliament in its consideration of the primary legislation now before it. (Paragraph 49)

If the MoD removes too much value from the Immediate Pension, its ability to retain expert personnel will be adversely affected, to the detriment of the Armed Forces as a whole. (Paragraph 52)

Given that the MoD is operating within self-imposed constraint of 'cost neutrality', we agree that the Immediate Pension was the appropriate benefit to cut in order to fund improvements to benefits elsewhere in the pension scheme. (Paragraph 53)

Taking early departure payments out of the pension scheme could be a blessing in disguise for the MoD, by allowing it to use the money more flexibly. The Government, however, needs to ensure that Early Departure payments are targeted not only to help the Armed Forces retain skilled personnel who would otherwise leave, but also to support former personnel who are in most need of such payments. (Paragraph 55)

The Government should be more explicit about its intention not to protect early departure payments from inflation, the savings that they expect to make from this, and the likely effect on payments to personnel. (Paragraph 56)

If not protected from inflation, the real value of a fixed rate early departure payment is likely to decrease substantially over time. (Paragraph 57)

If early departure payments are not protected from inflation, the real value of these payments over time to personnel leaving at different points is likely to differ substantially, as the rate of inflation varies. This may well lead to future grievances. (Paragraph 58)

The proposal would almost certainly result in former service personnel being paid more in real terms at the age of 41 than at the age of 64. This would seem to be in conflict with the likely needs of former personnel at those ages. It would be most unfortunate if those former personnel who rely on Early Departure payments for a basic standard of living were to see the value of those payments decrease in real terms as they grow older and become less able to pursue a second career. (Paragraph 60)

10. The Government notes the Committee's acceptance that the EDP scheme is the most appropriate benefit to reduce in value in order to improve benefits elsewhere in the new AFPS. We agree that further detail on the EDP scheme should be available to inform Parliament during its scrutiny of primary legislation. We regret that this information has not been available earlier but further discussions are needed to agree an acceptable alternative to the early IP, compatible with the Inland Revenue's proposals for Pensions Tax Simplification published in December 2002. As the Committee recognises, divorcing the EDP scheme from the constraints of pension rules allows a more flexible and targeted approach, responsive to manning needs and in particular reflecting the various manning exit points.

11. With the close involvement of Service pay and manning staffs, current detailed modelling for the new EDP scheme is focused on options which preserve a substantial initial lump sum payment, both to cushion the transition to a second career and to help achieve pull-through to age 40. Subsequent annual payments are expected to increase towards the age of 65 to reflect the higher risk attached to second careers at this stage, providing an appropriate safety net for those whom have served a substantial part of their career in the Armed Forces at the time when the need is likely to be greatest. The total value of the payments will be lower than the value of the current IP by 2% of pensionable pay (around a third of the value of the current IP). It is regretted that information on the MOD's website implying that there was expected to be no indexation of EDP payments was incorrect. No decision has yet been taken on this issue. Further work is in hand to agree the precise value of the proposed lump sums and annual payment. Parliament will be further advised of progress and details during the passage of the Bill to facilitate proper consideration of the legislation.

12. Together with the EDP lump sum payment, the EDP income stream will be set at a level designed both to pull personnel through to provide a reasonable return of service and to provide a fair level of support for those who leave until pension is paid. The Government does not consider it practicable to adjust payments individually to anticipate the significantly different needs of personnel after they have left the Services. We recognise that a small number of those leaving the Armed Forces may later face particular difficulties but these may not develop until long after retirement and are not readily predictable. These issues are appropriate to be considered as part of the Veterans Initiative.

Treatment of officers and other ranks

We welcome the fact that the MoD has taken the opportunity to ensure that all ranks are treated equally under the new schemes. (Paragraph 62)

13. The Government is pleased to note the Committee's support for equal treatment of officers and other ranks with respect to eligibility and qualifying times for pension benefits.

Compensation proposals

We welcome the fact that some of the safeguards within the compensation scheme have been strengthened. But our essential concerns about the structure of the compensation scheme have not been addressed. (Paragraph 65)

14. The Government is pleased to note the Committee's recognition of the new safeguards introduced for the compensation scheme. We consider that, with the addition of the exemptions list for late-onset conditions, the discretion to consider other claims outside the time limit in exceptional circumstances, the exceptional review process for significant deterioration, the internal disputes resolution procedures and the independent appeals process, the scheme will ensure that a Service person with attributable disablement will receive appropriate compensation. The scheme closely reflects wider good practice in modern compensation schemes. With the provision of lump sum compensation for pain and suffering (including in-service awards) as well as an income stream for significant loss of earnings capacity, it is considered a major improvement on the structure of the current arrangements.

Because of the special risks that Armed Forces personnel are required to run, and because they are likely to be involved in situations of great uncertainty, with uncertain effects on their health, we continue to believe that the onus should remain on the Government to prove that service was not responsible for causing or worsening a condition for which a compensation claim is made. (Paragraph 69)

A possible solution might be to apply a double test to compensation cases to ensure that the *burden* of proof does not unfairly discriminate against service personnel. Under such a system, a claim for compensation would only fail where both: (a) the claimant is unable to prove on the balance of probabilities that a condition is due to service, and (b) the MoD is able to prove on the same standard of proof that the condition is *not* due to service. We have not assessed how this proposal would be implemented in practice, but believe that the MoD should seriously consider it in the light of the special circumstances of Armed Forces personnel. (Paragraph 70)

15. The Government considers it is reasonable to adopt the balance of probabilities standard of proof, which is in line with the practice of other occupational pension schemes and the civil courts. This approach was considered as part of the review of the scheme commissioned by the MOD from independent consultants who confirmed that "the proposed standard of proof is reasonable". We accept and understand that the new scheme places the primary onus on the individual claimant and consider this reasonable given that we have no visibility of events in the individual's personal sphere or second career where injury or illness may equally arise.

16. Nonetheless, the MOD also accepts that there are responsibilities relating to proof that will rest with it, rather than the individual. These include the provision of medical and service records and the duty to undertake reasonable investigations into the circumstances of the claim and make the results of such investigations available to the individual or their legally empowered representative. The Government fully recognises the concerns of the Committee and of the ex-Service community that there should be greater assurance for the claimant in this area. The Government considers that the responsibilities on it set out above, incorporated in the scheme regulations and reinforced by an independent appeals tribunal will provide assurance that the claimant will be well placed to demonstrate any reasonable claim.

The Government should ensure that the compensation scheme rules set out clearly how a claim will be handled where medical records are inadequate or incomplete. It would be unfair, as the Government has acknowledged, if claimants were unable to make a successful claim because of the inadequacy of the records held by their employer. (Paragraph 72)

17. The Under Secretary of State made clear during the oral evidence session that, where there was a demonstrable failure of the Service record-keeping system affecting a claim, account would be taken of the individual's own testimony and any other evidence related to the claim and, if otherwise it appeared likely that a claim was reasonable, then an award would be made. This remains the Government's position and will be reflected in the legislation setting out the scheme rules.

We welcome the focus of the compensating scheme on the severely disabled, and the new lump-sum payments for pain and suffering. These basic aims seem both sensible and just. (Paragraph 73)

As they are currently drawn, the boundaries in the new compensation scheme between injuries leading to compensation for loss of earnings, and injuries leading to no such compensation, seem illogical. (Paragraph 80)

The system of tariffs as proposed fails to take account of the fact that similar injuries will affect the employment prospects of different personnel in different ways (and indeed, may cause radically different levels of pain and suffering to different people). This will continue to be the case, no matter how tariff boundaries are drawn and redrawn. (Paragraph 82)

Guaranteed Income Stream payments should be based on a proper assessment of earning capacity in civilian life for each individual, on the same lines as ill-health benefits under the pension scheme, rather than on the basis of tariffs for types of injury which may affect different individuals' earning capacity in very different ways. The Government should also reconsider whether it is appropriate to have two such similar benefits administered by different organisations under different schemes. (Paragraph 85)

18. The Government is pleased to note the Committee's support for the better focus of benefits on the more severely disabled and for the new principle of providing one-off lump sum compensation payments for pain and suffering.

19. The Armed Forces are a young fit population. The longstanding experience of the War Pension Scheme (WPS) and modelling for the new compensation scheme confirms that the majority of injuries will lie at the lower end of the tariff. Most of these disorders will be compatible with paid civilian work. The MOD considers it reasonable to provide only a pain and suffering lump sum payment where such conditions do not affect capacity to work. However, we note the Committee's views on possible anomalies with respect to the position of particular conditions within the table of tariff levels. While the broad positioning of conditions is considered sound, the Committee is aware that it is not final and will be subject to further review to ensure that the range of disorders, their relative positions, and average progress are appropriate. This work will be informed and validated by independent expert advice by the relevant UK medical authorities and will take the Committee's points into account.

20. The Government understands that the same condition can have very different effects on individuals in respect of how they might adapt to their changed circumstances and the possible effects on their subsequent employment. The arrangements put forward for the new scheme are in a significant respect an improvement over the WPS, as they take account not just of the level of disability, but also, at the higher tariff levels, of the individual's earning capacity which provides security for those most seriously disabled. In addition, the scheme's approach reflects the fact that most people with disabilities want to be in paid employment. This is in line with disability discrimination law and the substantial evidence that work is good for health. The approach advocated by the Committee is consistent with that taken by the civil courts for negligence claims, but it is not appropriate to a no-fault scheme where the aim is to deliver consistent, fair and reasonable outcomes, within a reasonable timescale and cost-effectively, and which can be easily understood and administered. Nor is it a feature of the current schemes.

21. The Government plans for the future that pensions and compensation benefits should be delivered as an integrated service from a single point of contact so that the claimant does not have to deal with multiple agencies. The MOD is also looking at the scope for rationalising administrative arrangements to remove duplication and reduce processing time. It may not be possible to deliver these changes for the introduction of the new schemes but we will provide the Committee with further advice on when these changes can be expected.

We would welcome an undertaking that, whatever the cost to the Government of extending backdated ill-health and death benefits under the pension scheme to those in receipt of equivalent benefits under the War Pension Scheme, it will not have a negative effect on the future entitlement of Service personnel to benefits under the pension and compensation schemes. (Paragraph 87)

22. The costs associated with compensating former Service personnel who did not receive the AFPS invaliding benefits to which they were entitled or whose benefits were wrongly taxed will have no effect on the benefits available under the new AFPS and new compensation scheme.

Communications with personnel

The MoD should identify lessons from the shortcomings of the consultation process to ensure that information about the new schemes reaches all levels of all units. (Paragraph 91)

23. The Government accepts this important point. The lessons are being addressed for future communications exercises and in particular for the major exercise required to allow those serving after 2005 who will be eligible to transfer to decide whether to transfer to the new scheme or remain with the current one. We also recognise that, in the past, Service personnel have not been well informed about their pension entitlements. Last year a new, more comprehensible booklet on the current AFPS was issued and this has been followed up with a number of supporting booklets on specific pension and compensation issues.

There have been various failures in information provision to service personnel on pensions and compensation, including in the very recent past. It is crucial that the MoD learns from these experiences in designing and implementing its communication strategy on the new pension and compensation schemes, if the transition to these schemes is to be a success. (Paragraph 92)

The new schemes are scheduled for implementation in less than 18 months' time. The MoD needs to ensure that its communications with personnel are well underway as soon as possible. (Paragraph 96)

It is essential that communication with personnel on those aspects of the new schemes which are yet to be finalised (such as early departure payments) are both complete and timely enough to allow for the information to be properly considered before any choice is made. The MoD should issue information to all serving personnel to enable them to make an informed choice, including pensions forecasts for both the existing and the new schemes tailored to individual personnel. (Paragraph 97)

24. There is no doubt of the crucial importance of effective communication for implementation of the new schemes. We intend to introduce the new AFPS for new entrants from 6 April 2005. The Committee have been advised that those personnel serving after 2005 who will be eligible to transfer to the new AFPS are unlikely to be able to do so at the same time, but will by 6 April 2007 at the latest. This is because of the requirement to produce individual benefit statements to Service personnel. The Armed Forces Personnel Administration Agency is not able to deliver such statements using the present computer systems and work is being undertaken to provide this capability through an alternative route. The MOD expects to know by the Spring the timescale for being able to produce such statements and this will determine the timetable for offering the transfer option and for the associated release of a multi-media package of information to assist current serving personnel in making their decision. The MOD is keeping in close contact with the Principal Civil Service Pension Scheme to capitalise on the work they undertook to implement their new scheme decision-process, including their communications exercise. On this basis, to achieve a timely impact, our aim would be to start the main part of the transfer option communications process around 12 months before the new scheme is available to currently serving members.

25. The Government is aware that targeting individual Service personnel may be more challenging than the equivalent exercise undertaken within the civil service. The level of Service responses to the consultation was low. The Services are currently considering how they can best ensure all their personnel are reached. Experience has shown that, wherever Service personnel are, they receive and read their pay slips and this may be an important mechanism for alerting people to the transfer option exercise and allowing them to alert those responsible if they have not received their transfer offers. We recognise the scale of the problem. Even with a relatively static population, the response rate from the civil service exercise was only 40% within the prescribed timescale. Follow up measures will therefore be an essential part of our planning.

The MOD needs to ensure that the impact of the new compensation arrangements on existing personnel is clearly communicated. (Paragraph 99)

It is vital that the rules for determining whether injuries and illnesses should be treated under the old or the new compensation scheme are not only clearly defined, but also clearly communicated. (Paragraph 100)

26. We will be issuing information to personnel before the introduction of the new compensation scheme for death, injury and ill-health due to service to make clear the provisions of the new scheme. This will include explaining the ways in which there are differences from current arrangements which the individual may need to take into account, particularly time limits to claim. We have been and will continue to be careful to draw a distinction between the new AFPS and the new compensation scheme, given that there is choice as to whether to join the former but not the latter. Advice on the provisions of the new compensation scheme will be reinforced on the point of departure (whether at the end of service or on medical invaliding). This material will make clear whether a condition would be considered under the current or new arrangements. It has already been agreed that, where the Veterans Agency receives a claim under the incorrect scheme, they will provide advice on how to make an appropriate claim; no such incorrect claim will be rejected without making clear the correct claim route. For most cases, the origin of a condition will be a specific event and it should be clear under which scheme it should be compensated. For more complex cases, work is underway to ensure that there is appropriate guidance and adjudication.

Consultation with Armed Forces personnel on raising the preserved pension age to 65 is particularly important, because this change will affect the Armed Forces very differently from the rest of the public sector. A majority of Armed Forces personnel will be financially disadvantaged by this change. Moreover, even of those personnel who do serve to the retirement age of 55, very few are likely to be able to take advantage of any enhancement to benefits which the opportunity to serve to age 65 might bring (Paragraph 104)

Further details need to be published clarifying how an increase in the preserved pension age for existing personnel will impact on the benefits they receive and when they receive them (Paragraph 105)

The MOD has failed to consult with serving personnel on the timescale for changing the preserved pension age, and it has already begun to define how the change to the preserved pension age will be introduced for serving personnel, again without consultation. This is unacceptable, given the Government's public undertaking to "consult on how and to what timescale the higher pension age and any associated enhancement to benefits could be extended to existing employees, while protecting rights already accrued". Proper consultation, as promised, should be carried out as soon as possible, to establish what measures might be appropriate to mitigate the special impact of the higher preserved pension age on Armed Forces personnel, both those who serve to the early departure point and those (the majority) who do not. (Paragraph 106)

27. The change to the age for the payment of preserved pension reflects a wider change to Government policy for the public services on which there has already been public consultation.³ It would not therefore be appropriate to consult Service personnel on the

³ Simplicity, Security and Choice: working and saving for retirement (December 2002).

general principle of the change which is agreed Government policy. Currently serving personnel have been advised about the broad implications of this policy change, in terms of the effects on both the new and current pension schemes. This will be reinforced, notably as the date for the change approaches but also in information on the new pension scheme; this will include information to enable individuals to assess how their personal pension benefits will be affected. Pension benefits based on service before the date of any change will be payable as before. A final decision has not yet been made about when this change will be introduced, but once the position is clear, individuals will be given reasonable notice of the change and at this time the MOD will invite any comments on the different options for paying preserved pensions under a combination of existing and new rules.

Timescale to implementation

We are concerned by how much work still needs to be done in relatively little time, both in terms of finalising the schemes, and in terms of communicating to Personnel what they mean (Paragraph 107)

28. The MOD has kept current Service personnel in regular contact with developments on the reviews through internal communications messages. Paragraph 10 notes that the key area for resolution is the EDP scheme. The results of the further work will be communicated to personnel as appropriate. Where there is a need or a clear concern on the part of personnel to have an early understanding of provisions as they are finalised, this will be provided as a matter of priority. We recognise, however, that there are risks attached to piecemeal communication, both that elements will not be seen in context and that there will be confusion about the overall arrangements for the schemes and their implementation. The strategy for keeping personnel informed will reflect these considerations and the concerns of the Committee.

Legislation

Because of inadequate consultation, because of the evidence we have heard that the elements of the schemes will not be fleshed out until consideration of primary legislation is already under way, and because Armed Forces personnel have no body representing their interests as employees, it is essential that the Government should seek explicit parliamentary approval for the schemes themselves, as well as for primary legislation (Paragraph 114)

Any amendments to the schemes which could negatively affect the benefits of personnel and their dependants under the schemes should also be approved by Parliament. (Paragraph 116)

We also believe that there is a strong case for setting the basic principles of the schemes in primary legislation, for example as a schedule to the bill (Paragraph 117)

In order to ensure that future major changes to the schemes involve proper consultation, and to ensure that Parliament is able to suggest changes to the schemes themselves, we recommend that major changes to the schemes in the future should be by statutory instrument subject to super-affirmative procedure, allowing for consultation both with interested groups and with Parliament, before final secondary legislation is presented to Parliament for approval. (Paragraph 118)

We regard it as essential that a framework document for the new Armed Forces Early Departure Scheme should be available to Members before second reading of the bill, as well as the framework documents already provided to us. (Paragraph 119)

If the details of the scheme rules is not available before second reading of the bill, this makes it all the more important that Parliament should have the chance to examine and question Ministers on the detail of these rules when secondary legislation is made. (Paragraph 120)

29. The Government accepts that Parliament has a proper interest in the Armed Forces pension and compensation arrangements, but does not accept that there has been inadequate consultation. The Bill is drafted as enabling legislation with the detail to be set out in secondary legislation by way of Statutory Instruments. To include details of the schemes in the Bill itself could mean an amendment to primary legislation would be needed in future every time that a change to the scheme rules was required; such changes are frequently necessary, for reasons of good administration, the need for uprating, and changes in external fields such as pension law, taxation and social security. To ensure understanding of the implications of the Bill, we have provided two detailed documents setting out the scheme structures both to the Committee and to the libraries of both Houses.

30. Current AFPS scheme rules are made under prerogative powers and are laid, after they are made, before both Houses for information purposes. However, the Government is proposing that the detailed regulations for the new scheme should be made in the form of Statutory Instruments (SIs), subject to annulment. We consider that this improved opportunity for scrutiny will provide Parliament with the proper opportunity to scrutinise policy change. This approach brings the new AFPS into line with the normal Parliamentary process for public service and parliamentary pension schemes.

31. The consultation exercise received significant publicity in the national media and was augmented by focus groups covering a representative cross-section of Service personnel to address the particular issue of benefits for unmarried partners, raised as an issue by Service personnel. It has been long-established practice that the interests of Service personnel are represented through their chain of command, and in particular through the Personnel Staffs who have had a direct input to the process of policy formulation for the new schemes, independent of the team conducting the reviews. We believe that this arrangement has worked effectively, identifying and representing the particular concerns of Service personnel with regard to the reviews. This has been augmented by the close consultation with the ex-Service organisations who have also strongly represented their concerns about the extent to which the proposals addressed the needs of the Service community. Finally, in view of concerns about the independence of the review process, we commissioned independent reviews of the proposals from one of the leading firms of independent consultants well placed to compare the consultation proposals, and their subsequent evolution to reflect views expressed in consultation, with broader good practice among employers. The final reports from these independent consultants have been released to the Committee as well as to those groups in the ex-Service community who were consulted during this work. Copies are being placed in the libraries of both Houses. The Government welcomes the Committee's contribution to the development of the schemes and looks forward to its continued involvement as they move forward to implementation. It also remains committed to ensuring that Parliament has visibility of any substantial changes to the Armed Forces pensions arrangements that might be of concern, to allow members of either House to pursue these if they wish.

Legacy issues

The MOD should look carefully and with a fresh eye at the suggestions put forward by the Forces' Pension Society as possible solutions to a number of 'legacy issues', and should establish whether any of them can be implemented, and at what cost. Former Armed Forces personnel and their dependants deserve no less. The Government risks giving the impression that it has forgotten or is ignoring these people, and that it fails to appreciate the fundamental validity of many of their concerns. (Paragraph 127)

32. The Government is well aware of the concerns of Armed Forces pensioners, widows and widowers who have not benefited from improvements to the pension scheme made after the retirement of the scheme member. We have been in discussion with those ex-Service organisations concerned — notably the Forces Pension Society, the Royal British Legion and the War Widows Association — to consider whether there are practicable solutions to these issues. We welcome the Committee's recognition that "it would hardly be reasonable of the Government to avoid making better provisions for future pensioners so that previous pensioners do not feel aggrieved". The issues raised by the Forces Pension Society are common across the public sector and, in this context, successive Governments have taken the view that pension improvements should not be made retrospective to the benefit of those who have already retired on the basis that the improvements would otherwise be unaffordable. It has also been the case for some time that the level of pension benefits has been reflected in an abatement of comparator pay which could not be applied to those who have already retired. The MOD has no plans therefore to change the policy, but is willing to consider other innovative ideas to resolve such concerns and work is underway at the moment on an idea put to the Government by the Forces Pension Society.

33. The provisions that widows and widowers should lose their pension on remarriage or cohabitation was originally common to all public service pension schemes, and was felt to be a reasonable measure when the majority of these schemes were introduced. Increasingly, modern pension schemes include provision for pensions for life, and the new AFPS follows this approach. Spouses of currently serving members of the Armed Forces will benefit from this provision if they choose to transfer to the new scheme. The cost of this benefit will be offset by changes elsewhere in the new scheme and is not therefore being extended to those in the old scheme.

34. The special position of Armed Forces widows and widowers whose spouses' deaths were due to service has been recognised by the Government by the introduction of pensions for life for them in October 2000. The arguments which brought about this very exceptional measure do not extend to widows whose spouses' deaths were not due to service; their position is comparable with other non-attributable widows across the public sector.

The Government needs to ensure that the important effects of these kinds of choice are properly conveyed to personnel, and that the transition to the new schemes is smoothly handled, if future 'legacy' grievances are not to arise. The Government should examine, for example, whether it would be possible to ensure that dependants of existing personnel do not lose out if their partner in the Armed Forces should die between the new pension scheme coming into effect for new entrants, and their partner being given the opportunity to choose between the schemes (Paragraph 128)

35. We accept the Committee's point regarding the need to ensure proper understanding of changes and smooth transition. On unmarried partners, ex-gratia payments have, since 20 March 2003, been made to unmarried partners of Service personnel for death due to conflict and from 15 September for all deaths due to service, and we are amending the current AFPS to ensure that unmarried partners of Service personnel who die due to service will be entitled to benefits.

We agree that former personnel whose pensions have been improperly taxed, and their dependants, should be compensated at a rate which ensures they are no worse off than they would have been if they had lent their money to Government through National Savings plus an element for damages. This was the Government's mistake and veterans and their families have already suffered enough for it. They deserve proper recompense. (Paragraph 131)

We expect a package of compensation to be announced by 18 December, as promised, to be implemented promptly and to include compensation along the lines of that recommended by the Forces' Pension Society. (Paragraph 134)

36. A copy of the Written Ministerial Statement of the 15 December 2003 resolving this matter is attached at Annex.

Conclusion: Parliament's role

The overall annual value of the new schemes has been diminished to account for new estimates of increased longevity, in a way which seems to us to be arbitrary and unfair. The MoD refuses to increase the value of the schemes because it is supposedly committed to cost neutrality. This decrease in the cost of the schemes should also have been resisted on the same grounds. (Paragraph 139)

In 2002, we stated our belief that the proposed pension scheme needed to take best practice as its starting point, rather than 'cost neutrality'; and our conviction that the proposed compensation scheme sacrificed fairness and justice for simplicity. At the same time neither scheme did justice to Armed Forces personnel. (Paragraph 140)

The schemes remain hamstrung by 'cost neutrality', and therefore fail to recognise the unique commitment that the Armed Forces make to their country. There have been some welcome changes to elements of the schemes, but these are, and can be, little more than tinkering in the absence of a broader outlook. We are also unhappy that important aspects of the schemes have yet to be finalised. (Paragraph 141)

37. The Government does not accept that the major changes made following consultation and as a result of wider changes to Government policy on pensions can be regarded as tinkering. They address directly the special demands of a career in the Armed Forces, notably through the major improvement to the benefits payable on the death of a Service man or woman, and they fully reflect the practical implications of the unique commitment made by members of the Armed Forces to the country. The independent reviews of the schemes show that the new schemes are good compared to those offered in other occupations. The MOD is confident that they will address fully their recruitment and retention needs, as well as meeting their 'good employer' responsibilities to provide a proper level of security to those personnel and their families who may be adversely affected by the demands of a Service career.

When it comes to negotiating pension and compensation entitlements, it seems to us that the Armed Forces are disadvantaged, because they have no-one to negotiate on their behalf as employees. Parliament therefore has a vital role to play in ensuring that the Armed Forces get the pension and compensation schemes that they deserve. (Paragraph 142)

38. The Government does not accept that the current arrangements for representing the interests of the Armed Forces in this or other areas are inadequate. The Principal Personnel Officers of the three Services have the main responsibility to provide good employer relations and advice to Ministers. We accept that Parliament will continue to take a keen interest in the Armed Forces Pension and Compensation Schemes and the Government welcomes that continuing scrutiny.

Annex

Written Ministerial Statement: 15 Dec 2003: Column 130WS

Service Pensions Taxation Error

The Parliamentary Under-Secretary of State for Defence (Mr. Ivor Caplin): The report of the internal inquiry into the incorrect deduction of tax from Service attributable pensions recommended that, in addition to the Inland Revenue refund and repayment supplement, consideration should be given to further compensation for those affected by the error. The Inland Revenue allowed a significant concession in waiving the time limits that normally apply in refunds of tax. However, representations have been made that the Ministry of Defence should pay further compensation to those pensioners for whom the effect of the error persisted over a considerable number of years. The Government accept that, where individuals suffer a financial loss as a result of its administrative errors, then the onus is on that Department to restore those individuals to the position they would have enjoyed had the errors not occurred. The Ministry of Defence has already accepted responsibility for the errors which led to tax being wrongly deducted and has apologised unreservedly. We further accept that, in certain cases, payments made so far have not provided full compensation for the cost of the errors to individuals.

I have therefore decided that further ex-gratia compensation will be paid to those who were in receipt of pensions outside the normal six-year Inland Revenue repayment period. Compensation will be calculated by applying compound interest, using the Retail Prices Index plus 2 per cent. to the tax wrongly deducted, net of the estimated repayment by the Inland Revenue. We will also pay ex-gratia compensation, calculated in the same way, to those who suffered from the related error of delays in payment of benefits under the AFPS, including using the Inland Revenue Repayment formula for compensation for errors within the normal six-year period. Payment will be made as quickly as possible.

It will, however, take some months to complete all payments because the necessary data on each individual are held mainly on manual records. We deeply regret the errors made but I hope that this offer of compensation will draw matters to a satisfactory conclusion.

Finally, I would like to express my considerable gratitude to those pensioners, in particular Major John Perry and Captain John Lewis, who have worked tirelessly to bring this matter to our attention and to help with its resolution.



Published by TSO (The Stationery Office) and available from:

Online

www.tso.co.uk/bookshop

Mail, Telephone, Fax & E-mail

TSO

PO Box 29, Norwich NR3 1GN

Telephone orders/General enquiries 0870 600 5522

Order through the Parliamentary Hotline *Lo-Call* 0845 702 3474

Fax orders 0870 600 5533

Email book.orders@tso.co.uk

Textphone 0870 240 3701

TSO Shops

123 Kingsway, London WC2B 6PQ

020 7242 6393 Fax 020 7242 6394

68-69 Bull Street, Birmingham B4 6AD

0121 236 9696 Fax 0121 236 9699

9-21 Princess Street, Manchester M60 8AS

0161 834 7201 Fax 0161 833 0634

16 Arthur Street, Belfast BT1 4GD

028 9023 8451 Fax 028 9023 5401

18-19 High Street, Cardiff CF10 1PT

029 2039 5548 Fax 029 2038 4347

71 Lothian Road, Edinburgh EH3 9AZ

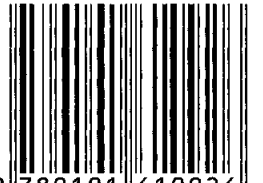
0870 606 5566 Fax 0870 606 5588

TSO Accredited Agents

(see Yellow Pages)

and through good booksellers

ISBN 0-10-161092-0



9 780101 610926