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Government proposals to fix the NHS pension crisis still miss the mark

Opinion

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It has been an unfortunate theme over recent years that public services have to reach crisis point before the government is stirred to take action.

And here we have the mother of all crises (that is, the NHS crisis) made worse by a desperately confusing pensions system.

When a tax rule is effectively stopping doctors from saving lives, you know

that something is amiss.

But despite the repeated warnings about the damaging implications of one specific tax policy – the pensions taper – it is only now senior doctors are reducing their workload to avoid being lumbered with hefty tax bills that the government is getting serious about reviewing the rules.



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The tapered allowance was introduced by George Osborne in 2016 to limit the amount of tax relief available to high earners. While the standard annual allowance (the amount you can pay into your pension without being taxed at your marginal rate) is £40,000, the pensions taper means that anyone earning more than £150,000 a year sees their tax-free annual allowance gradually reduced.

Essentially, for every £2 your adjusted income goes over £150,000, your annual allowance for that year falls by £1.

The general premise sounds relatively simple, but the taper is calculated for each individual using additional metrics (a mind-bogglingly complex set of rules that you can find on the HMRC website), which mean that if you're earning £110,000 a year, you could still be hit.

Defined benefit pensions (which are commonplace in the public sector) add another layer of complexity, because they are based on accrual rates and adjustments for inflation, rather than contributions, and tricky to predict.

The result is that it is ludicrously difficult for high earners – particularly those in the public sector – to understand what's going on with their

those in the public sector, like top doctors – to work out how much they are putting into their pension pots, and therefore how close they are to crossing the tax-free threshold and getting caught in the tax trap.

The general public doesn't usually have much sympathy for high earners in receipt of gold-plated pensions, but the issue hit the headlines when senior doctors and consultants started choosing to simply avoid the risk of massive tax penalties by turning down overtime, or even retiring early.

The costs of exceeding the limit can be huge. In some cases, doctors and nurses have ended up worse-off for doing overtime, and there have been reports of people having to remortgage their homes to foot the tax bills. But while the stakes are high, the rules are fiendishly complicated and time-consuming to understand. As former pensions minister Ros Altmann points out: "Surely we want the senior NHS staff to be medical experts, not pension buffs."

Sticking plaster



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TAKING BOOKINGS

The Department of Health has finally promised to review the system. Last week, it proposed new rules that would give NHS staff more flexibility around how much they contribute into their pensions, allowing them to set the exact amount of contributions and accrual at the start of each financial year.

By allowing staff to opt out of the NHS pensions scheme mid-year, the idea is that they would then be free to work additional shifts without breaching limits for pensions tax relief.

However, experts are dubious about whether this is the right solution.

“Offering the flexibility to reduce pension contributions will only create confusion and require NHS members to seek advice from their accountants and financial advisers to try to guide them through this,” says Gary Smith, chartered financial planner at Tilney.

And there’s a wider issue too. Tapering affects those in the public sector more (most private sector workers contribute eight per cent of their salary into their workplace pension scheme, while NHS trusts pay in 20 per cent), but it’s the taper allowance in general that’s the problem, not the NHS pension scheme specifically.

The government has pledged to review how the tapered allowance system “supports the delivery of public services such as the NHS”, but the phrasing suggests that it only plans to look at how the tapered allowance affects public schemes, when really a wider review of this unfairly complex system is needed.

If reform only looks into the public side, Smith warns that it would create a two-tier pension system that would further exacerbate the public-private sector pension divide.

And there’s another concern with allowing clinicians to opt out of their pension and sending the contribution to their salary instead. A doctor who opts out of the pension scheme would incur a 40 per cent income tax charge on their increase in salary, not to mention a two per cent National Insurance charge.

Smith also points out that the NHS would have to pay employers National Insurance of 13.8 per cent on this salary too, representing an increased cost to the overstretched health service compared to making a pension contribution, plus the additional administrative burden.

There are questions about whether the proposal will even work as intended. As AJ Bell’s Tom Selby says: “Many affected by the taper will inevitably decide they don’t want to jump through hoops, only to end up with a smaller pension in the end.”

No miracle cure

So what are the solutions? Baroness Altmann suggests that problems could be addressed by basing the tapered allowance on last year's earnings, not the current year, so that staff know what the allowance will be for the year they are in.

"The calculation should also be much simpler, so it is straightforward to work out the allowances, without being a pensions aficionado," she says.

But some pension pros are going further and calling for the taper to be scrapped entirely, for public and private sector workers alike.

Steve Webb, former pensions minister and director of policy at Royal London, points out that the problem is not unique to the NHS nor even to the public sector. "Any review must be comprehensive and cover everyone affected by this absurdly complex taper, including in the private sector," he says. "The best solution by far would be outright abolition, even if this meant a slightly lower annual allowance across the board."

However, while getting rid of the taper might be the simplest way to deal with this problem, it would also leave a huge £1bn hole in the chancellor's finances that would need to be plugged – hardly an attractive proposition for the Treasury.

Sorry state of affairs

The government hopes that the new rules will relieve the pressure on hospitals and their mounting waiting lists, but regardless of what the final versions look like, it will be months before they come into force, meaning hospitals face another winter crisis in the meantime.

Claudia Paoloni, president of the Hospital Consultants and Specialists Association (HCSA), warns that without an urgent solution to the pensions crisis, the NHS is facing its worst winter on record. "It is tragic that the government has known about this growing crisis in the NHS for months, yet it has sat on its hands," she says.

"Without tax reform, we fear that waiting lists will hit five million by next year. We need to see action in weeks not months – that means a firm

year. We need to see action in weeks not months – that means a firm commitment to tax change at the next Budget.”

Staff shortages are already at critical levels, with half of hospital doctors not doing overtime, while 26 per cent have reduced their extra hours, according to figures published by the HCSA last Thursday. Right now, the tax system is incentivising them to stay away.

The NHS is in dire need of urgent medical attention. And a sticking plaster will be no substitute for system-wide pensions reform.

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