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Mr Matt McLaughlin and Mr Derek Lindsay  
Co-Chairs  
NHS Pension Scheme (Scotland) Advisory Board

Dear Matt and Derek,

As co-chairs of the NHS Pension Scheme (Scotland) Advisory Board ('the SAB'), I am writing to you in relation to the recent consultation on proposed changes to the member contribution structure in the NHS Pension Scheme from 1 October 2023.

Firstly, I would like to place on record my thanks to the SAB for its engagement on this issue over an extended period and for providing formal advice to Ministers on the reform of member contributions in your letter of 13 August 2021.

While the SAB was not able to provide unanimous advice, you helpfully outlined guiding principles to which all SAB members subscribed, including moving to actual pay as a means of determining contribution rates, maintaining the annual indexation of contribution tiers and seeking to maintain a high level of membership. The SAB also agreed that the review of member contributions should fundamentally deliver a structure which is fair and equitable across the whole of the pension scheme membership.

The SAB were, however, unable to make a recommendation to Ministers on a preferred contribution structure and key staff-side groups disagreed on the extent to which the contribution structure should be flattened. In the absence of clear advice and agreement from the SAB, a contribution structure proposal was developed and put forward for consultation (shown in Annex A). The consultation proposals sought to provide a compromise position and to meet our key objectives of designing an employee contribution structure that:

- delivers the 9.8% target contribution yield as required by HM Treasury
- protects affordability for lower earning members of the scheme and aims to maximise pension scheme participation amongst all NHS Scotland staff
- better reflects the nature of pension accrual in a career average revalued earnings (CARE) pension scheme, where all members receive the same proportional pension benefit.

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Following the end of the public consultation, officials have been carefully considering the large number of responses received. As expected, responses demonstrate that there remains distinct views between those who wish to see a flatter or single rate structure, with more members paying closer to the average 9.8% yield, and those who wish retain the current range of tiers.

I understand the concerns raised by stakeholders about the impact of contribution increases at this time. However, the current rates being paid by scheme members are not enough to meet the contribution yield required by HM Treasury. As you are aware, the change to using actual pay to determine contribution rates will mean that most part-time staff will pay a reduced level of contributions.

The Scottish Government have postponed these reforms for over two years, and a year longer than other schemes in the rest of the UK, during a period where inflation was at its peak. It is also the intention, as proposed in the consultation, to phase the implementation of these changes over two years which provides some further protection for lower paid members from full contribution increases until October 2024.

However we recognise the continued high cost of living and have therefore made adjustments to the final contribution structure which is shown in Annex B. The new structure limits contribution increases in the first year to a maximum of 0.9% for staff up to, and including, salary point one of AfC pay band six.

The consultation responses revealed significant differences of opinion on the structure and number of the contribution tiers, with some respondents advocating a single contribution rate as the fairest solution. A full response to these arguments will be published in due course, but taking the differing positions into account, we remain committed to a tiered structure in the scheme, which is a mutual scheme for all NHS staff. A tiered structure provides protection for the lower paid and aims to maximise participation across the membership. It worth also noting that in its review of public service pensions in 2011, the Independent Public Service Pensions Commission in recommending the introduction of CARE schemes also recommended that, in those schemes, the differing characteristics of higher and lower earners should be addressed through tiered contribution rates.

A number of stakeholders made specific points in response to the consultation about the impact of contribution increases of staff in particular earnings bands. There was concern expressed about the increases required for staff in the proposed tiers six and seven, and that these increases were disproportionate to other increases. While these members are set to see the largest contribution increases, they are currently paying below the average contribution rate of 9.8% and are, therefore, having their pension contributions subsidised, despite earning more than the average salary in the NHS. The increases required for this group of staff seek to correct that anomaly as part of rebalancing the contribution structure. We are, however, mindful of the potential take-home pay impact, as highlighted in consultation responses, and have therefore sought to adjust the contribution rates as much as possible in the revised structure shown in Annex B. The rate for the new tier 7 is reduced in year one from 11% to 10.8% and for tier 8 the rate is reduced from 11.6% to 11.3%.

Respondents to the consultation also highlighted concerns about unintended consequences of where the tier boundaries are drawn in the proposed structure and the potential impact on take-home pay between different AfC pay bands. It was highlighted that where staff earn only their core salary, the effect of contribution increases could see a negative take-home

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pay impact for staff moving between AfC band five and six and also between bands six and seven. We have sought to correct this position by creating an additional tier of 9.8% and adjusting the tier thresholds from the original proposal. This change also allows the introduction of a 9.8% tier in line with the target yield, and the absence of this rate in our original proposals was a source of criticism.

In conclusion, I believe that the revised contribution structure presents the best possible compromise position and, while it includes contribution increases for some, it maintains the NHS Pension Scheme (Scotland) as a valuable part of the remuneration package for all NHS staff. The scheme provides index-linked retirement benefits which are fully protected against inflation, on some of the most generous terms available from a pension scheme.

The preferred structure meets our key objectives of achieving the target yield, minimising increases for lower and middle earning staff while also rebalancing the structure. I also consider that, importantly, the structure delivers on the fundamental principle set out in the SAB's advice, that it is fair and equitable across the whole of the pension scheme membership. Therefore, we intend to move to implement this structure from 1 October 2023.

Looking beyond the two-year implementation set out in the proposals, we believe a cautious pace is appropriate for any future changes to contribution rates and it may be prudent to align future adjustments to valuation cycles. The SAB will be asked to keep the contribution rates under review, monitoring membership and participation data to inform the timing and nature of any future adjustment.

Yours sincerely,



**MICHAEL MATHESON**

## Proposed structure presented in consultation

A	B	C	D	E	F	G
Current Structure			Proposed new structure			
Current tiers	Pensionable earnings in 2022/23	Current rate	Pensionable earnings in 2022/23	Rates from 1/10/2023	Rates 1/10/2024	New tiers
		WTE pay		Actual pay	Actual pay	
Tr 1	Up to £23,819 →	5.2%	Up to £13,330	5.8%	5.8%	Tr 1
		5.2%	£13,331 to £23,819	6.2%	6.5%	Tr 2
Tr 2	£23,820 to £25,981 →	5.8%	£23,820 to £28,186	6.8%	7.1%	Tr 3
Tr 3	£25,982 to £32,914 →	7.3%	£28,187 to £35,365	8.3%	8.7%	Tr 4
Tr 4	£32,915 to £66,017 →	9.5%	£35,366 to £43,421	10.5%	10.6%	Tr 5
		9.5%	£43,422 to £48,784	11.0%	11.4%	Tr 6
		9.5%	£48,785 to £68,222	11.6%	11.7%	Tr 7
Tr 6	£66,018 to £92,423 →	12.7%	£68,223 and above	13.7%	12.7%	Tr 8
Tr 7	£92,424 to £123,147 →	13.7%				
Tr 8	£123,148 and above →	14.7%				

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## Amended final structure

A	B	C	D	E	F	G
Current Structure			Proposed new structure			
Current tiers	Pensionable earnings in 2022/23	Current rate	Pensionable earnings in 2022/23	Rates from 1/10/2023	Rates 1/10/2024	New tiers
		WTE pay		Actual pay	Actual pay	
Tr 1	Up to £23,819 →	5.2%	Up to £13,330	5.7%	5.7%	Tr 1
		5.2%	£13,331 to £23,819	6.1%	6.4%	Tr 2
Tr 2	£23,820 to £25,981 →	5.8%	£23,820 to £28,186	6.7%	7.0%	Tr 3
Tr 3	£25,982 to £32,914 →	7.3%	£28,187 to £35,364	8.2%	8.7%	Tr 4
Tr 4	£32,915 to £66,017 →	9.5%	£35,365 to £35,521	9.8%	9.8%	Tr 5
		9.5%	£35,522 to £37,086	10.0%		
		9.5%	£37,087 to £45,079	10.5%	10.5%	Tr 6
		9.5%	£45,080 to £48,784	10.8%	11.2%	Tr 7
		9.5%	£48,785 to £68,222	11.3%	11.6%	Tr 8
Tr 6	£66,018 to £92,423 →	12.7%	£68,223 and above	13.7%	12.7%	Tr 9
Tr 7	£92,424 to £123,147 →	13.7%				
Tr 8	£123,148 and above →	14.7%				

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