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Armed forces pension reform - 1995 to 2005

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Summary

Armed forces pensions can be traced back as far as 1831, although it was not until April 1975 when legislation was changed to provide the right to a preserved pension for early leavers. Prior to that, while entitlement to an Immediate Pension was reached with after 22 years' reckonable service (16 years in the case of officers), commissions or engagements for shorter periods were on non-pensionable terms. Those who had served 12 years (or nine in the case of officers) were awarded a gratuity. The Armed Forces Pension Scheme (AFPS) 1975 incorporated the requirement to award "preserved pensions" for early leavers. It is a Defined Benefit scheme, based on representative pay for the rank and length of service.

A consultation document on the review of the AFPS was published in March 2001. The intention was to be 'cost neutral', while modernising scheme benefits and ensuring affordability for the future. A new scheme, AFPS 05, was introduced in April 2005 for new entrants. AFPS 75 was closed to new members that date. Members of AFPS 75 in April 2005 were offered the opportunity to transfer to AFPS 05 in April 2006.

Both AFPS 75 and AFPS 05 are unfunded, defined benefit, salary-related, contracted-out occupational pension schemes. They are non-contributory for members, although the value of the scheme is taken account in setting pay.

This note looks at the review process that led up to the introduction of AFPS 05. In particular, it looks at the ways in which it is different to AFPS 75 and why. Separate notes cover the campaign for retrospective improvements to AFPS on a number of "legacy" issues – SN01424 [Armed Forces Pension Scheme legacy issues – survivors' benefits](#) (12 November 2014) and SN01151 [Armed Forces Pension Scheme and preserved pensions](#) (15 May 2014). More recent reforms are covered in SN05891 [Armed forces pensions – 2015](#) (24 August 2015).

1. Background

1.1 History

Armed forces pensions can be traced back as far as 1831. A description of the development of the scheme was given by Parliamentary Under Secretary of State for Defence Kevan Jones in the second reading debate on the *Forces Widow's Pensions (Equality of Treatment) Bill*.¹

Briefly, a significant change was made in April 1975, from which date when occupational pension schemes were required to provide preserved pensions for early leavers who satisfied the relevant conditions. The Armed Forces Pension Scheme 1975, which incorporated this requirement, is a defined benefit scheme. It is salary-related with pensions based on a representative rate of pay for the rank and length of service.²

AFPS 75 was closed to new entrants on 5 April 2005.³ For new entrants from that date, a new scheme - Armed Forces Pension Scheme 2005 (AFPS 05) – was introduced.

1.2 1995 review

The AFPS was reviewed in 1995 as part of the *Independent Review of the Armed Forces' Manpower, Career and Remuneration Structures* under the chairmanship of Michael Bett. The review suggested a number of reforms to the scheme including pensions based on the best 12 consecutive months' earnings over the last three years before retirement, as opposed to based on rank at retirement; immediate pensions payable only from the age of 50 rather than after 16 years' service (22 for non-officers) regardless of age; and widow(er)s' pensions payable for life and a sufficiently flexible scheme to enable beneficiaries to include partners in stable relationships outside marriage. These changes were not implemented because it was considered that the recommendations on career structures needed to be addressed before the proposals on the AFPS could be taken forward.⁴

In 1997, the Government decided that a fresh examination of Armed Forces pensions should be commissioned. The review began in late 1998.⁵ The review compared the benefits offered by the AFPS with those available in the private and public sectors generally. In particular, it examined whether aspects of the scheme needed to be modernised. It also looked at whether special features of the scheme designed to cater for the particular circumstances of a career in the armed forces were "still necessary and cost effective in the light of the wider availability of

¹ [HC Deb, 19 June 2009, c584-606](#)

² For more detail, see HC Library Briefing Paper SN01424 [Armed Forces Pension Scheme and preserved pensions](#) (15 May 2014)

³ With the exception of those taking advantage of the Gurkha Offer to Transfer. For more detail, see SN04375 [Gurkha Pensions \(September 2014\)](#)

⁴ Ministry of Defence, [The Armed Forces Pension Scheme Review: a consultation document](#), March 2001, p2 [Intranet]

⁵ [Ibid](#), p2

modern, portable occupational and personal pensions".⁶ The March 2001 consultation document explained the Government's reasons for considering changes and some of the unusual features of the current scheme:

3.1 A number of features of the scheme are inconsistent with other public sector schemes and some provisions fall short of best practice in modern pension schemes generally. Maximum pension entitlements for occupational schemes are determined by Inland Revenue rules and the Review Team explored whether there would be any headroom within the rules to introduce improvements in the level of benefits, if these were otherwise considered desirable and affordable.

3.2 Benefits are set according to a single representative rate of pay for each rank. An individual's pension is not, therefore, precisely linked to actual earnings, so that those on higher pay bands do not receive pension benefits for their higher earnings; conversely, those on lower pay bands benefit. Another feature of the system is that it is possible for 2 Servicemen of the same rank and reckonable service to leave on successive days, either side of a pay award, with very different pensions. In addition, a system of representative pay would not sit well with the new pay system (Pay 2000) which is linked to job weight, qualifications and experience.

3.3 The scheme has some other unusual features. First, reckonable service for pensions does not begin until age 21 for officers and age 18 for other ranks regardless of when an individual joins the Armed Forces. Second, accrual of a full service pension at age 55 then takes 34 years for officers and 37 years for other ranks. This kind of difference within a single scheme is unusual. And third, accrual is uneven over a career with higher accrual at the outset, up to the immediate pension point (IPP).

3.4 An IP is available to officers from age 38 and to other ranks from age 40. No other major scheme provides such an early IP. That is an expensive provision of the pension scheme. It dates from before the days when people could carry their pension entitlements with them when they changed jobs. However, it recognises that the Armed Forces need to shed a substantial proportion of manpower around the age of 40, and acts as a retention incentive to pull people through to this point. But there is certainly an argument that alternative, more flexible tools would serve the same purpose.

3.5 The fact that Specialist Pay is not pensionable is a source of considerable discontent amongst those who receive Specialist Pay over a long period and for whom this pay is seen as a consistent part of overall remuneration (eg flying pay, submarine pay). Their pension on retirement may be a much lower proportion of final earnings than that of other members of the Armed Forces. However, Specialist Pay is currently set at levels which take account of its non-pensionable status.

3.6 Pension and terminal grant accrue separately. If they accrued together (and therefore produced a higher base level of pension, with no terminal grant payable unless the member commutes part of his pension), widows' pensions might rise as they are normally set at half the scheme member's pension entitlement. Indeed, there is room, under Inland Revenue limits, for a general increase

⁶ [Ibid](#), p4

in pensions benefits. Pensions benefits for the scheme member account for 62.5% of pay and half that figure for the widow. The Inland Revenue limit is up to 2/3 pay for the scheme member, and up to 4/9 pay for the widow. There would, therefore, be headroom within the usual rules governing pensions schemes to increase the level of benefits, although the benefits and affordability of an increase of this sort would need careful consideration.

3.7 Ill-health benefit pensions are paid at the same rate for all individuals discharged on invaliding terms with the same rank and length of service. As a result, those in most need may receive inadequate pensions while some individuals whose earnings capacity is not unduly affected by their condition receive a comparatively more generous amount.

3.8 The death-in-service gratuity is significantly lower than in many other pension schemes. There has also been pressure for widow(er)s' benefits not to be withdrawn on remarriage.

3.9 The Review examined all of these issues to establish the case for change. Its objective was to set a benchmark for new pensions arrangements which supported Armed Forces career structures by contributing to recruitment, retention and morale, and which provided a fair level of benefits for individuals while remaining cost effective and affordable. It did not approach its task with the premise that change was necessary in all areas: it was concerned to identify the right arrangements for the circumstances of the Armed Forces.⁷

Comment on the proposals was invited by 31 July 2001,⁸ although this was later extended to October 2001.

⁷ [Ibid](#)

⁸ [Ibid](#), p13

2. Framework for a new AFPS

The Government published a report on its March 2001 consultation proposals in September 2003.⁹ It published its *Framework document for the new Armed Forces Pension Scheme* in October 2003.¹⁰ This addressed most of the anomalies identified in the consultation document. In the new AFPS:

- the representative rate of pay would be replaced by individual earnings as the basis on which pension is calculated;
- reckonable service would start from the first day of service for officers and other ranks;
- accrual would be the same for officers and other ranks (1/70ths) and will be even throughout service;
- the Immediate Pension would be replaced by a system of Early Departure Payments to those leaving after age 40 and 18 years' service, regardless of rank;
- there was no proposal to make specialist pay pensionable;
- pension and terminal grant would continue to accrue separately;
- non-attributable widow(er)s' pensions would be increased to up to 62.5% of the spouse's pension;
- there would be three-tier system of non-attributable ill-health benefits, dependent on the seriousness of the disability;
- the death-in-service gratuity would be increased from one to four years' pensionable salary;
- widow(er)s' benefits would not be withdrawn on remarriage

2.1 Cost basis of review

Regarding the cost of the proposals, the March 2001 consultation document said:

It is Government policy that improvements in public service pensions should generally be paid for either by savings elsewhere in the scheme, or by scheme members through contributions. The recommended new scheme would introduce important modernisations compared with the compared with the current arrangements, and a number of worthwhile improvements; resources have been provided for the improvements by adjusting some other provisions of the scheme. The recommendations are cost neutral as a package.¹¹

The Defence Committee published a report on the Ministry of Defence's reviews of armed forces pension and compensation arrangements in May 2002. This was critical both of delays in the review and its cost-neutral basis:

The review process, however, has been dogged by delay and incompetence. The consultation documents were weak and uninformative. It is only in response to our own long list of

⁹ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003 [Intranet]

¹⁰ MoD, [A Framework Document for the new Armed Forces Pension Scheme](#), October 2003 (Dep 03/2568)

¹¹ MoD, [The Armed Forces Pension Scheme Review. A consultation document](#), March 2001, para 6.3 [Intranet]

questions that the detailed information needed to assess the new proposals has emerged from the MoD and been put in the public domain. Overall the MoD appears to be little further advanced in its thinking now than it was when the reviews began. Both proposed schemes are at best inadequately thought-through and at worst fundamentally flawed.

Pensions

The pension review was hamstrung from the outset by the MoD's decision to require any new scheme to be cost neutral in effect. The result is that it proposes improving ill health and dependants' benefits by reducing the pensions of other Service personnel. This is unacceptable.

The MoD also decided not to examine or cost alternatives to immediate pensions. Immediate pensions are an expensive part of the AFPS, but their principal purpose is as a manning tool to assist retention and recruitment. We believe that it was wrong to let manning considerations stand in the way of a properly thorough review of Armed Forces pensions.

The Armed Forces deserve a pension scheme which recognises the unique commitment they make to this country and which compares favourably with what is available to other public service employees. The MoD needs to do a great deal more work on its proposals before they meet this requirement, taking best practice as its starting point, rather than cost-neutrality.¹²

In December 2003, the Defence Select Committee produced a further report. This welcomed aspects of the review but was again critical of the MoD's interpretation of "cost neutrality":

On the plus side, entitlements for widow(er)s have been improved, and new rights for unmarried partners have been included. An independent appeals mechanism has been formulated for dealing with unsuccessful claims under the compensation scheme; and the period in which claims will be eligible has been extended.

On the negative side, however, the Ministry of Defence's interpretation of 'cost neutrality' in fact means that the value of benefits to Armed Forces personnel are to be reduced on the basis that they will live for longer; and most personnel will have to wait an extra five years before receiving their pension.¹³

The Committee found that savings within the pension scheme would be used not only to improve other benefits, but also to cover the cost of increased longevity:

22. What the actuarial assumptions disguise, however, is that the MoD's gross pensions bill is actually expected to decrease in 30 to 40 years' time, as a result of the reduction in Service numbers from around 330,000 in 1975 to about 200,000 now. What this means is that the MoD is currently making payments to pensioners drawn from a workforce much larger than that to which the Ministry is currently paying salaries. However, by the time the actuarial assumptions on life expectancy are realised, the MoD will be making payments to pensioners drawn from a workforce of roughly today's strength. **The Government is**

¹² Defence Committee, [Ministry of Defence's reviews of armed forces pension and compensation arrangements](#), Third Report 2001-02, HC 666, 1 May 2002

¹³ [Ibid](#), Summary

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.¹⁴

A Parliamentary Written Answer of 28 November 2006 said that the new AFPS 05 was broadly intended to be "cost neutral". The main purpose of the review was to modernise scheme benefits and ensure affordability for the future:

Mr. Laws: To ask the Secretary of State for Defence what estimate he has made of the significant long term savings from the reformed armed forces pension arrangements introduced in 2005 referred to in the answer of 7 November 2006, Official Report, column 1487W; and if he will make a statement.

Derek Twigg: The new Armed Forces Pension Scheme (AFPS 05) was broadly intended to be 'cost neutral' at the time of introduction in April 2005 in comparison with AFPS75. The main reasons for introducing the new scheme were to modernise the schemes benefits and at the same time ensure affordability in the future as factors such as increased longevity took affect.

The scheme's actuary is confident that there will be significant long term savings if a comparison is made between the emerging costs of the new scheme and the costs that would have resulted if we had continued exclusively with the old scheme.

The estimate is that the eventual long term savings will be in the region of £120 million per year once the vast majority of personnel are active members of the new AFPS 05—in about 20 years time. An accurate net present value at this point in time could only be provided at disproportionate cost.¹⁵

This issue is covered in more detail in Library Research Paper 04/05, [Armed Forces \(Pensions and Compensation Bill\)](#).

¹⁴ Defence Committee, *Armed Forces Pensions and Compensation*, First Report of 2003-04, HC 96-I

¹⁵ [HC Deb, 28 November 2006, c627W](#)

3. Review issues

This section looks at the questions considered as part of the review of AFPS. The end of each section summarises the relevant current provisions of AFPS 75 and AFPS 05.

A common scheme

The March 2001 consultation paper considered the different arrangements for officers and other ranks in the AFPS and recommended that the new scheme should be a common scheme:

The Review Team considered the differences between officers and other ranks' arrangements were out of step both with pensions practice elsewhere and with the modern ethos of the Armed Forces. The practice of not counting service before the age of 21 for officers and 18 for other ranks for pension purposes appeared similarly out of line with normal practice. The Review Team therefore recommended a revised common scheme for officers and other ranks with the following features:

- Service reckonable for pension purposes should count from the day of joining the Armed Forces.
- The pension should accrue evening with a full career pension payable after 35 years reckonable service.
- A terminal grant of three times pension should be paid.¹⁶

The October 2003 report on the consultation found "overwhelming support for a common scheme although there was a desire among some officers to maintain the current differentials" although there some concerns were raised. The MoD considered that:

- it was right in equity to propose a common early departure point for officers and other ranks;
- work would be undertaken to ensure the terms of engagement took account of the revised structure of the new AFPS;
- the final structure of the scheme allowed long servers the opportunity to continue to earn benefits over 35 years;
- although officers would have to serve longer, the new scheme offered a number of improvements to offset this.¹⁷

The Defence Committee welcomed the fact that the MoD had taken the opportunity to ensure that all ranks were treated equally under the new schemes.¹⁸

AFPS 05 was introduced as a common scheme, with pensions calculated on the same basis for officers and those of other ranks. In AFPS 75, the rules differ for officers and those of other ranks (see below).

¹⁶ MoD, [The Armed Forces Pension Scheme Review. A consultation document](#), March 2001, *Ibid* [Intranet]

¹⁷ [Ibid](#), p 3

¹⁸ Defence Committee, [Armed Forces Pensions and Compensation](#), First Report of 2003-04, HC 96-I, para 23

Members' benefits

The March 2001 consultation paper proposed that the AFPS should continue to be a defined benefit scheme as this was "suited to careers where there is a substantial level of stability and where people remain in the same employment over a long period. However, the fact that AFPS pension benefits were determined by reference to final rank led to some anomalies:

The pension is based on a single rate of representative pay for each rank, calculated on the basic pay received by individuals in the rank, but not taking into account Specialist Pay or allowances. All individuals retiring at the same rank, with the same length of service and in the same year will receive the same pension, whatever their actual earnings.¹⁹

It was proposed that the new scheme should be a "true final salary scheme" i.e. one which would:

- link pensions and pay more closely;
- improve the position of higher earners;
- remove the anomaly under which quite large differences can occur in the pensions of those who retire either side of a pay award;
- help smooth the effect on the pensions of those who retire when prices are rising faster than earnings.²⁰

The majority of those responding to the consultation considered this "an improvement to the scheme", although there were concerns regarding those downgraded due to ill-health prior to retirement. The MoD commented that:

The use of the 'best in the last three tax years' approach to pensionable pay, with pay increased by price increases to protect people from artificial pay restraint or an abnormal end-of-career reduction in pay will help to mitigate problems arising from a final salary scheme such as have led in the past to pensions troughs.²¹

AFPS 75 and AFPS 05 are both final salary schemes but benefits are calculated differently. Under AFPS 75, benefits are based on a "representative pay rate". Maximum benefits are paid after 34 years' service (officers) or 37 years (other ranks). There is also a "terminal grant" of 3 times annual pension:

If you retire at age 55, with 34 years' reckonable service (Officers) or 37 years Other Ranks), your full career (maximum) pension will be index-linked from your date of retirement. You will also receive a one-off terminal grant of 3 times your annual pension. The terminal grant is normally tax-free.

Under AFPS 75, members of the Armed Forces with the same rank and same number of years of reckonable service are normally awarded the same pension, regardless of their actual pay either at

¹⁹ MoD, [The Armed Forces Pension Scheme Review. A consultation document](#), March 2001, para 2.1 [Intranet]

²⁰ [Ibid](#), para 4.5

²¹ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003, p6 [Intranet]

retirement or discharge, or earlier in their career. This is known as the representative pay rate for the rank.²²

In the case of AFPS 05, pension benefits are based on final pensionable pay. Each year of service is worth 1/70th of final pensionable pay, up to a maximum of 40 years:

The pension paid to you will be based on reckonable service at the point at which you leave the service. Each year is worth 1/70 th of final pensionable pay up to a maximum of 40 years. (See example below of pension calculation.) Your final pensionable pay will be the greatest amount of pensionable earnings you received for 365 consecutive days over your last three years of service.

Example of Pension Calculation

If your final salary is £30,000 after completing 25 years' service your annual pension would be calculated as follows:

$$£30,000 \times 25 \times 1/70 = £10,714 \text{ pension}$$

In addition to your annual pension, you will receive a pension lump sum of three times your annual pension.²³

There are a number of ways in which members can increase their benefits in the schemes: for example, through payment of additional voluntary contributions or the purchase of added years. Details can be found in the booklets for scheme members available on the Gov.UK website – [Armed Forces Pension Scheme 2005](#).

Pension age

The March 2001 consultation document explained the age at which AFPS benefits could be drawn:

- a) An immediate pensions (IP) is available from the age of 38 (or 16 years service if later) for officers and from age 40 (or 22 years service if later) for other ranks; a terminal grant of 3 times pension is paid on retirement.
- b) A full career is pension is payable from age 55; a terminal grant of 3 times pension is paid on retirement. The full career pension is accrued over 34 years from age 21 for officers and over 37 years from age 18 for other ranks.
- c) Those who retire with an immediate pension, but before accruing a full career pension, have the option of commuting part of the pension to provide an additional lump sum payment (this is known as resettlement commutation); the full pension is restored on reaching age 55...
- d) Those who leave before becoming entitled to an immediate pension receive a deferred pension payable from age 60.²⁴

²² AFPS75, [Your pension scheme explained](#), (MMP/106, re-issued May 2008), p13

²³ AFPS 05, [Your Pension Scheme Explained](#), (MMP/124, Re-issued Jan 07), p4

²⁴ MoD, [The Armed Forces Pension Scheme Review. A consultation document](#). March 2001, p 5 [Intranet]

Normal retirement age

In its December 2002 Pensions Green Paper, the Government proposed an increase in the public service pension age. Although it recognised that special factors affected occupations such as the armed forces, it said that those who left before armed forces pension age should have to wait until 65 for a pension, and that pension benefits accrued by people who are already members of the scheme should accrue as if the pension age were 65 from a future date:

66. We would welcome views on the proposal that the rules of public-service pension schemes should be changed and applied to all new members during the next few years to make an unreduced pension payable from age 65 rather than 60. Such a change would reflect improved longevity, modern working patterns and the practice in the majority of private sector pension schemes. This age would apply regardless of an employee's length of service. There will continue to be some occupations such as the armed forces, fire service and police where the need for a recognised physical capacity justifies the award of normal pension at a lower age, but for individuals who leave before they reach such an age their pension would also be deferred to age 65.

67. The Government envisages that the higher pension age might be introduced in most schemes as part of a package of changes to pension arrangements, including some features which proposals elsewhere in this Green Paper will make possible for the first time. A change of pension age would help to offset the cost of increased longevity. The reviews of the public-service schemes will be the subject of consultation and are likely to take a few years to complete, but once introduced the higher pension ages would apply to all new entrants.

68. These reviews would aim to identify scope for redirecting resources to finance greater flexibility – particularly in the transition from work to retirement – and to offer improvements to benefits which employers and staff value and will have positive impact on staff recruitment and retention. Diverse and flexible employment practices will have a key part to play. An increase in the age from which pensions are payable will also help the financial sustainability of public service pension schemes. Early retirement options would continue to be available but as a departure from a normal pension age of 65 rather than 60.

69. For existing members, accrued pension rights from service before the change would be fully protected enabling them to receive a pension from the age they currently expect. However, while it is envisaged that the new arrangements would be introduced for all new employees, the Government will also 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. In many areas there is a demand from employees to work for longer and it is appropriate to encourage and reward that accordingly.²⁵

The normal retirement age remains at 55 in both the AFPS 75 and AFPS 05.²⁶ This is “to reflect the career structure of the armed forces and

²⁵ DWP, [Simplicity, security and choice: Working and saving for retirement](#), December 2002, Cm 5677

²⁶ See, for example, MoD, [A framework document for the new Armed Forces Pension Scheme](#), 27 October 2003, para 3.2 [Intranet]

standards of fitness and health we required of Service personnel.”²⁷ However, it is acknowledged that members of the armed forces do not typically serve to age 55 or beyond. In 2005-06, approximately 10 per cent of officers and approximately 7 per cent of other ranks served long enough to receive a full pension.²⁸

Preserved pension age

The age at which a “preserved pension” could be drawn was age 60. Following the review, this has increased to 65 in AFPS 05, and in AFPS 75, for service after 6 April 2006.²⁹

The Defence Select Committee suggested that while an increase in the pension age might be reasonable in the rest of the public service, where employees will be able to continue working until 65, it might be less appropriate in the Armed Forces:

103. The effect on Armed Forces personnel of raising the preserved pension age will be different from the effect on most other public servants of raising their retirement age. For teachers and civil servants, raising the pension age from 60 to 65 means working for a further five years. This has its disadvantages for those who would rather retire early, but these people are unlikely to be seriously disadvantaged financially. Indeed, as the Government indicates, raising the pension age may bring “enhancement to benefits” to those who are able to work to age 65.

104. In the Armed Forces, on the other, hand, the majority of personnel do not serve even to the official retirement age of 55. This majority will be financially disadvantaged by raising the preserved pension age. Even of the minority who serve to age 55, very few indeed are allowed to serve on beyond this point. It is hard to see what enhancement to benefits the higher preserved pension age could bring to Armed Forces personnel, unless they are allowed to serve to age 65.³⁰

Early departure payments

As explained above, members of the armed forces do not typically continue in service until age 55. To provide an incentive for people to continue in service until an age considered appropriate,³¹ the AFPS includes provision for earlier payment of an “Immediate Pension” - payable from age of 38 (or 16 years service if later) for officers and from age 40 (or 22 years service if later) for other ranks.³² The March 2001 consultation document noted that the Immediate Pension was an expensive element of AFPS:

The immediate pension point (IPP) was introduced before modern pension arrangements offered the possibility of transferring accrued entitlements between pension schemes. Its purpose was to assist Armed Forces personnel who could not follow a full career in the Services and would need form of financial assistance

²⁷ HC Deb, 23 November 2007, c170W

²⁸ [HC Deb, 25 June 2007, c102W](#)

²⁹ See, for example, MoD, [A framework document for the new Armed Forces Pension Scheme](#), 27 October 2003, para 3.2 [Intranet]

³⁰ <http://pubs1.tso.parliament.uk/pa/cm200304/cmselect/cmdfence/96/9607.htm#a21>

³¹ [HC Deb, 27 November 2006, c362W](#)

³² MoD, [The Armed Forces Pension Scheme Review. A consultation document](#), March 2001, p5 [Intranet]

with returning to civilian life. Today, no other major pension scheme offers such an early immediate pension (IP) and the current flexibility of pension schemes suggests there must be an argument for moving away from such an early pension point. It is a particularly expensive element of AFPS.³³

However, it also noted that there was a “deliberate shedding of personnel at about age 40 as there is a reduced ability to undertake fighting roles beyond this age.” It considered that any savings in delaying the IPP might need to be ploughed back in to a system of bonuses to encourage retention and that altering it substantially would place manpower planning at risk.³⁴

In its October 2003 report on the consultation, the MoD noted a “consensus in favour of retaining the Immediate Pension Point (IPP), with agreement that age 40 (after 18 years of service) was around the right age.³⁵ However, proposals from the Inland Revenue proposed setting a minimum age at which pensions can be drawn – 55 in 2010.³⁶ The MoD therefore proposed an alternative non-pension arrangement, known as the Early Departure Point (EDP) to deliver a *lump* sum and income stream to help Service personnel adjust to civilian life (with pension benefits being preserved until age 65).³⁷

A report by Watson Wyatt stated that the Early Departure Scheme would be:

designed to provide a benefit which is overall lower in value than the Immediate Pension. The intention is to provide a lump sum on exit from the services followed by a stream of income which may not necessarily be flat but could be targeted at those ages where it is perceived that there is greatest financial need.³⁸

The Defence Committee commented that taking early departure payments out of the pension scheme could allow the money to be used 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 need of such payments.³⁹

However, it argued that the Government “should be more explicit about its intention not to protect early departure payments from inflation:”⁴⁰

60. We understand that the MoD does in fact propose to raise the level of early departure payment later in life, but not by as much

³³ Ibid, para 4.6

³⁴ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003, p4

³⁵ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003, p4

³⁶ HM Treasury, Inland Revenue, [Simplifying the taxation of pensions: increasing choice and flexibility for all](#), December 2002, para 5.15

³⁷ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003, p4

³⁸ Watson Wyatt, *Armed Forces Pension Scheme. Addendum to the report on the proposals for a new Armed Forces Pension Scheme*, para 2.10

³⁹ Ibid, para 55

⁴⁰ Ibid, para 56

as if the payment were index-linked. In other words, the payment is likely to decline in value between the ages of 40 and, say, 55, and then to increase slightly at 55, but not to the same level as at age 40. 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.⁴¹

The Government responded that:

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).⁴²

Provisions of AFPS 75 and AFPS 05

A Parliamentary Written Answer from 25 June 2007 provides a useful summary of the ages from which pensions can be drawn in AFPS 75 and AFPS 05:

Mr. Laws: To ask the Secretary of State for Defence what the earliest age is at which a member of the armed services can receive a full pension; and if he will make a statement.

Derek Twigg: The expression 'full pension' is taken to mean a pension reflecting the maximum amount of reckonable service allowed under the pension scheme rules. As the majority of service personnel belong to either the armed forces pension scheme 1975 (AFPS 75) or the armed forces pension scheme 2005 (AFPS 05) my answer is in respect of those schemes.

Under AFPS 75 the most an officer can accrue is 34 years reckonable service from age 21 and, for an other rank, the limit is 37 years reckonable service from age 18. The earliest that a full pension can be paid is age 55 and this full pension is worth 48.5 per cent. of representative pay.

Officers who leave having accrued at least 16 years reckonable service from age 21 under AFPS 75 and other ranks who leave having accrued at least 22 years from age 18 are entitled to a pension paid immediately upon discharge but this is a proportion of the full career pension. Those who leave with two or more years service but insufficient to qualify for this immediate pension are awarded a preserved pension payable at age 60 for service before 6 April 2006 and 65 for service after that date.

⁴¹ Ibid, para 60

⁴² ['Armed Forces Pensions and Compensation: Ministry of Defence Response to the House of Commons Defence Committee's First Report of Session 2003-04, Cm 6109](#), January 2004, para 11

Under AFPS 05 the most that a member can accrue is 40 years reckonable service with no minimum age limit. The normal full pension entitlement is age 55. A full pension under AFPS 05 is worth just over 57 per cent. of final pensionable pay.

AFPS 05 members who leave before age 55 with two or more years reckonable service are entitled to a preserved pension payable at age 65. Those who have given at least 18 years reckonable service and attained age 40 are eligible for payments from the early departure payments scheme. Their pensions are preserved until age 65.

Finally, members of the armed forces do not typically serve to age 55 or beyond. In 2005-06 approximately 10 per cent. of officers and approximately 7 per cent. of other ranks served long enough to receive a full pension.⁴³

Ill-health benefits

The March 2001 consultation document described the existing system of ill-health benefits in the AFPS as follows:

g. An ill-health retirement pension is paid at a rate set according to rank and length of service, with a terminal grant 3 times the annual rate of the award. For those retiring with 2 year's service or more, on grounds of illness or injury which is not attributable to service, an immediate pension is paid from the AFPS at higher levels than the normal retirement pension.

h. Tax-free attributable pensions are paid to those who retire on ill-health grounds for reasons attributable to service. The benefits are set according to the degree of disablement. Attributable benefits are being examined separately in the Joint Compensation Review.⁴⁴

It was proposed that there should be a three tier ill-health benefit structure, to account for those who could not meet the fitness levels required by the Armed Forces but who, to all intents and purposes, would be capable of most other forms of employment.⁴⁵ It was conscious of the need to have clear criteria for each tier.⁴⁶ The framework document for the new AFPS, published in October 2003, proposed that:

4.1 A member serving within the Armed Forces with reckonable service of less than 2 years will have no entitlement to an award in the case of non-attributable invaliding.

4.2 A member serving within the Armed Forces who is invalided with reckonable service of at least two years may be awarded an ill-health pension or gratuity. The benefits will be calculated according to the level of ill-health.

4.3 Invaliding pensions will be calculated according to the level of ill-health.

⁴³ [HC Deb, 25 June 2007, c101W](#)

⁴⁴ MoD, [The Armed Forces Pension Scheme Review. A consultation document](#), March 2001, para 2.1

⁴⁵ [Ibid](#) para 4.17

⁴⁶ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003

4.4. The ill-health pension benefits will be calculated according to the level of ill-health.⁴⁷

The criteria for the three different tiers were described as follows:

Tier 1

4.5 Members invalidated out of the Service because they are unable to do their Service job, but whose earnings capacity in civilian life is not affected, will be awarded a gratuity. The gratuity will be related to the member's salary and the number of years served...

Tier 2

4.6 Members who are invalidated out with an impairment that significantly affects their earnings capacity in civilian life will be awarded a pension lump sum and an ill-health pension enhanced by one-third of their remaining service (based upon the normal retirement age of 55).

Tier 3

4.7 Members who are invalidated out of the Service with a serious disability which renders them permanently incapable of any further employment will be awarded a pension lump sum and an ill-health pension enhanced by half of their remaining service (based upon the normal retirement age of 55) with a minimum pension guarantee of 20 years' accrued pension.⁴⁸

Provisions of AFPS 75 and AFPS 05

The AFPS 05 has three tiers of ill-health awards, according to the seriousness of the condition:

If your career is cut short by illness or injury and you have completed more than two years' reckonable service, you will receive an ill-health award. The amount is based on a three tier system. For less serious conditions, Tier 1 provides a tax-free lump sum only. If you have a serious condition, covered by Tiers 2 and 3, the ill-health pension will be based on your actual service, plus an enhancement. (See pages 14-15 for further details.)⁴⁹

Members of AFPS 75 may be entitled to an "invaliding pension" depending on length of service:

If you are invalidated from the Armed Forces because you are no longer fit enough for military employment you will initially receive, provided that you are eligible, a non-attributable Service Invaliding Pension (SIP). The benefits paid depend on your length of service.⁵⁰

"Attributable benefits" (where an injury or illness was cause or aggravated by service, or a death was caused or significantly hastened by service) are not paid by AFPS. Benefits are paid under two schemes, depending on the date when the injury or condition was caused:

- For injuries or illnesses caused before 6 April 2005, a top-up may be made to the *AFPS 75* pension under the Armed

⁴⁷ MoD, [A framework document for the new Armed Forces Pension scheme](#), 27 October 2003 [Intranet]

⁴⁸ Ibid, p 4-1

⁴⁹ AFPS 05, [Your Pension Scheme Explained](#), (MMP/124, Re-issued August 2012)

⁵⁰ AFPS, [Invaliding](#), MMP 115

Forces Attributable Benefits Scheme and additional benefits under the War Pensions Scheme.

- For injuries or illnesses caused on or after 6 April 2005, pain and suffering lump sums and Guaranteed Income Payments (GIP) (where appropriate are paid under the Armed Forces Compensation Scheme (AFCS)).⁵¹

Information about the development of the AFCS can be found in the Library Standard Note SN/SP 5553 [Armed Forces Compensation Scheme](#) and Research Paper 04/05, [Armed Forces \(Pensions and Compensation\) Bill](#).

Commutation

The March 2001 consultation document explained that:

Commutation

4.14 In the current AFPS, the pension and terminal grant accrue separately. It would in principle be possible to allow the scheme member's entitlement to accrue wholly as a pension, and then to give him the option of commuting part of it. Some schemes do this. But in such schemes, experience suggests that almost all people commute their maximum entitlement, to give them the benefit of money up front, tax-free. Such a system requires a member to make a positive choice on retirement, and could add administrative complexity. There seems no particular reason to pursue this idea. The Review felt, however, that if individuals wished to commute all or part of their terminal grant inversely to give them additional pension rights, they should be permitted to do so. That would in practice provide the same flexibility as true commutation but on a 'by exception' basis.

Resettlement commutation

4.15 under the current scheme, individuals who retire before age 55 with an immediate pension can commute part of that pension to provide them with an additional tax-free lump sum. The full pension is restored at age 55. A new AFPS would be subject to the *1989 Finance Act* which limits lump sums under pension schemes. Retaining resettlement commutation would breach the Inland Revenue limits. The Review Team considered that the proposed pension and gratuity arrangements were sufficient and do not recommend that resettlement commutation should form part of the new scheme. It noted that the provision of an optional bonus (paragraph 4.9 above) would provide an additional facility for the scheme member to be paid a lump sum.⁵²

The September 2003 report on the consultation said:

Although it was considered that inverse commutation offered choice and flexibility, many were disappointed with the loss of Resettlement Commutation. They saw this as a major factor in their decision as to whether not they should transfer to the new scheme.⁵³

⁵¹ AFPS 75, [Your pension scheme explained](#), (MMP/106, re-issued May 2008)

⁵² MoD, [The Armed Forces Pension Scheme Review - A consultation document](#), March 2001, para 4.14

⁵³ MoD, [New Armed Forces Pension Scheme. Report on consultation process](#), September 2003, p 6

Provisions of AFPS 75 and AFPS 05

AFPS 05 offers a pension based on reckonable service, with each year worth 1/70th of final pensionable pay up to a maximum of 40 years. In addition, members receive a lump sum of three times the annual pension.⁵⁴ Members are offered an option of “inverse commutation”:

You may opt to exchange the whole or part of your tax-free pension lump sum for an increase in the amount of taxable pension payable to you and your dependants. The value of the exchange is calculated by the scheme actuary. Once the exchange is agreed, the lump sum is reduced by the amount exchanged, whether or not the pension that is to be increased as a result of the option actually becomes payable. For example, if you reduce your lump sum to improve both your and your spouse's, civil partner's or eligible partner's benefits but he/she dies before you, the exchange will not be reversed.⁵⁵

AFPS 75 offers a full career (maximum) pension at 55 (with 34 years' reckonable service for an officer, 37 years other ranks) and “a lump sum (normally tax-free) of 3 times the annual rate of pension”.⁵⁶ A resettlement grant is also payable in certain circumstances:

If you complete more than 9 years from age 21 (or date of entry if later) (officers) or 12 years from age 18 (or date of entry if later) (Other ranks) and leave the Armed Forces with no immediate benefits, you may qualify for a tax-free resettlement grant to aid your resettlement into civilian life.⁵⁷

Survivors' benefits

The Armed Forces Pension Scheme Review consultation document said:

The main cause of discontent with the current Scheme is the practice of withdrawing widow(ers) pensions on remarriage and the level of death-in-service gratuity which, at 1-1 ½ times pensionable salary compared favourably with other schemes.

It recommended the following benefits for widow(ers) and children:

- a) The widow(ers)' pension should remain set at half the spouse's pension.
- b) The pension should be paid for life, even if the widow(er) remarries.
- c) Children's pensions should be made available to the children of post-retirement marriages.
- d) The death-in-service gratuity should be raised from 1 to 1 ½ times pensionable salary to cushion the changes immediately following death. This removes the need for the short-term (3-9 months) pension; long-term pensions would begin immediately.
- e) Should death occur early in retirement, the widow(er) should receive the pension that their spouse would have received during the first 5 years of retirement, abated by the terminal grant. This is, in effect, a 2-year guarantee for the pensioner. The short term pension for death-in-retirement should be withdrawn.

⁵⁴ AFPS 05, [Your Pension Scheme Explained](#), (MMP/124, Re-issued August 2012)

⁵⁵ [Ibid](#), p10

⁵⁶ AFPS75, [Your pension scheme explained](#), (MMP/106, re-issued May 2008), p11

⁵⁷ [Ibid](#), p12

f) A general increase in the pension paid following death-in-service to half the level of the Tier 3 ill-health pension.⁵⁸

Respondents to the consultation welcomed the improvements in spouses' benefits although some concerns were expressed about the loss of short-term pension. The widow's associations were concerned that, given the intention to improve widow(er)'s benefits, a widow might be disadvantaged by a poor decision made by the spouse prior to death i.e. not to transfer to the new scheme. The MoD responded that:

We understand the concern expressed by ex-Service organisations at the loss of the short-term pension, but it cannot be retained in the new scheme as it is no longer compliant with Inland Revenue rules. We recognise the higher than normal incidence of widowhood in the Armed Forces, the limits on the ability of some Service spouses to accrue their own pension as a result of mobility demands, and our responsibility to dependants. We have also discussed with the ex-Service community their concern regarding the level of widow's benefits. In response, we are increasing the death-in-service benefit further to 4 times pensionable salary and the level of pension by 25% (worth up to 62.5% of member's pension). A widow whose spouse remained under the current AFPS would not benefit from higher pension benefits or pensions for life, (pension for life for attributable only in current scheme); we recognise that this will be an important consideration for every member of the current scheme in deciding whether to move to the new scheme, but also for their spouses, and we will be taking special steps to ensure that both are aware of the availability of this valuable benefit enhancement.⁵⁹

The Defence Committee "welcomed 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."⁶⁰

Unmarried partners

The March 2001 consultation document did not address the question of benefits for unmarried partners. The AFPS (at least before 15 September 2003) only provided survivors' benefits for widows and widowers. Unmarried partners did not benefit. However, the issue was raised in responses to the consultation. The MoD said:

In view of the responses received concerning unmarried partners, those within a substantial relationship will be eligible for 'widow's' benefits under the new scheme. Further work is being undertaken in this area to define the arrangements for the registration of partners.⁶¹

A number of cases of servicemen killed in action, leaving long-term partners and children with no pensions, highlighted this omission and, on 20 March 2003 as war started in Iraq, the Government announced

⁵⁸ MoD, *The Armed Forces Pension Scheme Review, A consultation document*, March 2001, para 5.1

⁵⁹ MoD, *New Armed Forces Pension Scheme. Report on consultation process*, September 2003, p5

⁶⁰ Defence Committee, *Armed Forces Pension and Compensation*, First Report of Session 2003-04, HC 96-I, para 33

⁶¹ MoD, *New Armed Forces Pension Scheme. Report on consultation process*, September 2003, p5

that unmarried partners of service people who died as a result of service related to conflict would qualify for ex-gratia payments equivalent to benefits paid to surviving spouses.⁶² The statement of 15 September 2003 extended this provision by announcing that the AFPS would provide attributable benefits to unmarried partners where there is a substantial relationship for all attributable deaths with an effective date of 15 September 2003.⁶³

The Government's consultation document on *Civil Partnership: a framework for the legal recognition of same-sex couples*, published in June 2003, made it clear that public service schemes would be amended to provide survivors' benefits for registered same sex partners, and that schemes can, if they can afford it, extend benefits to unmarried partners of opposite sexes:

The Government proposes that members of public service pension schemes will earn entitlement to survivor benefits, including a survivor pension, for registered partners in the same way as for married partners.

9.14 The Government's policy is that if the membership of a public service scheme wants to extend eligibility for survivor pensions to unmarried partners and is prepared to meet the additional costs, the Government is prepared to consider how practicable arrangements could be devised for achieving this. The Civil Service has introduced a new scheme, which includes unmarried partner benefits on this basis. There is no change to the Government's policy regarding partners who are neither married nor registered. A number of public service schemes, however, are conducting reviews on whether and how to introduce unmarried partner benefits, among other reforms.⁶⁴

The October 2003 *Framework document for the new Armed Forces Pension Scheme* said that registered unmarried partners would also be eligible to receive a widow/widower's pension subject to the relationship being substantial at the time of death.⁶⁵

The Defence Committee recommended that the schemes should be "as clear as possible about when unmarried partners will qualify for benefits, both to avoid ill-feeling among non-qualifying unmarried partners, and to avoid potentially expensive legal action."⁶⁶

Provisions of AFPS 75 and AFPS 05

AFPS 05 provides dependants' pensions for former spouses, civil partners and "eligible" unmarried partners. These are payable for life, irrespective of re-marriage or cohabitation:

Dependants' pensions are only payable if you have two years' or more reckonable service. If at the time of your death you have a spouse or civil partner, they will be eligible to receive a pension. A former spouse, from whom you have divorced, or former civil

⁶² [HC Deb, 20 March 2003, c54WS](#)

⁶³ [HC Deb, 15 September 2003, cc39-40WS](#)

⁶⁴ DTI Women and Equality Unit, [Civil Partnership: a framework for the legal recognition of same-sex couples](#), June 2003, paras 9.11-9.14 [Intranet]

⁶⁵ MoD, [A Framework Document for the new Armed Forces Pension Scheme](#), October 2003, para 6.1 [Intranet]

⁶⁶ Defence Committee, [Armed Forces Pensions and Compensation](#), First Report of Session 2003-04, HC 96-I para 41

partner, if you have legally dissolved the civil partnership, is not eligible to receive a pension.

If the marriage or civil partnership ceremony took place within six months of your death, the award of a pension will not be automatic. The circumstances will be examined by SPVA to ensure that the marriage or civil partnership has not been entered into purely for financial gain. Partners, other than civil partners, are also eligible to receive a pension, providing that it can be demonstrated that a substantial relationship existed and there is no spouse or civil partner. These examinations will be conducted with sensitivity so far as possible.

Your spouse, civil partner or eligible partner will receive an index-linked pension worth 1/112ths of *pensionable pay* for each year of service you are entitled to count towards pension, up to a maximum of 37.33 years. This gives a pension of up to 62.5% of your pension entitlement, which is payable for life, irrespective of remarriage or cohabitation. In certain circumstances the pension may be less than 62.5%...

CHILDREN'S PENSIONS

These pensions may be payable in respect of natural, adopted or stepchildren and any other children who are financially dependent upon you. This includes children who are born or become eligible after you leave the Armed Forces. (See eligible child on page 4.)

CHILDREN'S PENSIONS CALCULATION

The amount of your pension entitlement available for children's pensions is normally the balance of the pension remaining after the payment of any spouse's, civil partner's or eligible partner's pension...

PENSION LUMP SUM

You can nominate more than one person or organisation to receive your pension lump sum. If you die and you have not made a valid nomination, your pension lump sum will normally be paid to your spouse, civil partner, eligible partner or, if you have no dependants, to your estate...

DEATH-IN-SERVICE

If you die in service, a tax-free lump sum payment of four times pensionable pay will be made to your nominee. As a Death In Service lump sum is paid there will be no preserved pension lump sum payable. In addition, your spouse, civil partner or eligible partner will normally receive a pension which will be calculated as if you had been medically discharged on the date of your death at Tier 3 (pension enhanced by half your remaining service, based upon the normal pension age of 55) or, if greater, your actual pensionable service up to 37.33 years, subject to a minimum pension based on 20 years' service.⁶⁷

AFPS 75 provides benefits to a surviving spouse or civil partner, but these are suspended upon remarriage or cohabitation with a new partner or new civil partnership. Unmarried partners are not eligible for non-attributable benefits:

A pension is paid to a *surviving spouse* or *civil partner* who are eligible under the rules of the Scheme. The pension is normally one half of your pension (ignoring *commutation*) if you die in

⁶⁷ AFPS 05, [Your Pension Scheme Explained](#), (MMP/124, re-issued Jan 07)

retirement, or one half of the pension you would have received on non-attributable invaliding if you die in service. Different arrangements are likely to apply in respect of widows' benefits for any service given on or before 31 March 1973 and for the widow(er)s of post-retirement marriages only service from 6 April 1978 will count towards benefits. A higher rate may be due to children who have no surviving parent.

A short term family pension is additionally payable for the first 91 days of widow(er) hood, extended to 182 days if there are children. This is calculated at the daily rate of pay if death occurs during service, or at pension rate if death occurs during retirement. This rule applies equally to civil partners.

Pensions are also payable for eligible children, up to a total of one half of the member's entitlement (where a surviving spouse or civil partner's pension is also payable), with no one child receiving more than a quarter of the pension. Pensions to children will normally stop when the child reaches 17, although they may continue if the child is in full time education or training, or is unable to support him/herself for reasons of disability. The disability must have been present before the member's death.

A lump sum is payable on death in service which is normally tax-free. This amounts to about 3 times your salary or the *terminal grant* that would have been payable on non-attributable invaliding, whichever is worth more. If you die after leaving but before preserved benefits become payable, your surviving spouse or civil partner may be paid a gratuity equal to the preserved terminal grant.

If you die after leaving but before preserved benefits become payable, your surviving spouse or civil partner may be paid a gratuity equal to the preserved terminal grant.

NOTE:

- As a Scheme member, you are not entitled to nominate the person(s) who can receive any benefits when you die
- Only a legal spouse or civil partner can receive pension benefits; unmarried partners are not eligible for non-attributable benefits.⁶⁸

Pensionable pay

A question considered in the review was whether Specialist Pay should be pensionable. It noted that Specialist Pay was received by about 10% of the armed forces:

Some individuals receive it for most, if not all, of their career (flying pay is a good example) whereas others receive it for the length of a tour or for a particular activity (deep and experimental diving pay) for only part of their career.⁶⁹

However, because Specialist Pay tended to be paid for only part of an individual's career, it was considered impossible to make it pensionable in a true final salary scheme:

In his Independent Review, Sir Michael Bett recommended that Specialist pay of a continuing nature should be subsumed within

⁶⁸ AFPS75, [Your pension scheme explained](#), (MMP/106, re-issued May 2008), p20

⁶⁹ Ministry of Defence, [The Armed Forces Pension Scheme Review, A consultation document](#), March 2001, para 4.10 [Intranet]

new pay ranges that that pensionable pay should then be based on actual pay.

Specialist Pay, however, remains for most people an addition to basic pay and is not pensionable. That is taken into account in setting rates of Specialist Pay. It would not be possible to make pensionable Specialist Pay which was payable throughout a career, although this might affect the rates of Specialist Pay. It would, however, be impossible in a true final salary scheme to make these forms of Specialist Pay pensionable where it ceases in the latter part of a career, or where its level varies considerably across a career.⁷⁰

The MoD commented that it might be possible to target certain groups in receipt of specialist pay to give them better access to benefits financed through Additional Voluntary Contributions (AVCs).⁷¹

For both AFPS 75 and AFPS 05 pensionable pay is:

basic pay including the X factor but excluding allowance, bonuses, financial retention incentives, loan service pay and any form of specialist pay⁷²

The X factor is a component of military pay that is paid through a whole UK service career.⁷³ It is a "pensionable addition to pay that recognises the relative disadvantage of conditions of service experienced by members of the Armed Forces compared to those in the civilian sector."⁷⁴

Non-contributory basis of AFPS

Members do not make direct contributions to basic benefits under AFPS 75 or AFPS 05, although pension benefits are taken into account when pay is assessed. A November 2006 Parliamentary Written Answer explained the rationale for retaining the non-contributory nature of the scheme:

Mr. Laws: To ask the Secretary of State for Defence what estimate he has made of the annual revenue yield from the introduction of an employee pension contribution of 6 per cent. of pay for all members of the armed forces; and if he will make a statement. [93540]

Derek Twigg: The armed forces pension schemes are final salary based, non-contributory, contracted-out occupational pension schemes open to most members of the armed forces. The MOD does, however, make a substantial contribution into the schemes each year for current members, currently the overall contribution equates to 24.8 per cent. of the armed forces pay bill.

The non-contributory nature of the schemes was last reviewed as part of the major overhaul of the schemes which were introduced through the *Armed Forces (Pensions and Compensation) Act 2004*. The Government decided against an employee's contribution at that time because of the complexity of introducing a contributory scheme alongside a non contributory scheme, the administrative complexity and the cost of the change, the impact

⁷⁰ [Ibid](#), para 4.11

⁷¹ [Ibid](#), p4

⁷² AFPS 05, [Your Pension Scheme Explained](#), (MMP/124, re-issued Jan 07), p4; AFPS75, [Your pension scheme explained](#), (MMP/106, re-issued May 2008)

⁷³ HC Deb, 28 April 1999, c1530

⁷⁴ [Armed Forces Pay Review Body, 38th Report 2008](#), Cm 7315, para 4.3

on personnel of issuing different rates of pay for the same job and the effect on morale, recruitment and retention (HC1155 dated 25 July 2002). The changes made as a result of the review addressed the matter of long term affordability, such as increases in longevity, by rebalancing the provision to take account of modern pension practices and legislative change, and by changing the preserved pension ages.

The Armed Forces Pay Review Body, in their recommendations on the total remuneration package for the armed forces, makes an adjustment to comparator earnings figures to take account of the higher relative value of the armed forces pension scheme benefits against that of pension schemes of comparator private sector organisations. The non-contributory nature of the scheme is one of the factors taken in to account. The level of the adjustment made is currently 7 per cent.

The MOD has not previously made an estimate of the annual revenue yield from introducing an employee contribution of 6 per cent. Taking the armed forces pay bill for 2005-06 as a basis for the calculation, a 6 per cent. employee contribution would equate to £342 million.⁷⁵

Transition to AFPS 05

The report on the consultation process said:

We plan to implement the new scheme in April 2005 for new entrants to the Armed Force. Current serving personnel will be given the option to transfer into the new scheme as soon after April 2005 as possible, depending on availability of delivery systems, and no later than April 2007. There will be a separate exercise in due course to consult people on whether they wish to transfer and this will include the necessary information on the benefits people would receive under the two schemes.⁷⁶

The Defence Committee emphasised the importance of communication with personnel to ensure they were able to make an “informed choice” about the new AFPS.⁷⁷ The Government responded that “there was no doubt of the crucial importance of effective communication for implementation of the new schemes” and was considering how best to ensure that all personnel were reached.⁷⁸ In the event, those already in service on 6 April 2005 and still in service on 6 April 2006 were given the opportunity to transfer to the new schemes with a common Member Transfer Date of 6 April 2006.⁷⁹

⁷⁵ [HC Deb, 6 November 2006, c821W](#)

⁷⁶ MoD, *New Armed Forces Pension Scheme. Report on Consultation Process*, September 2003

⁷⁷ Defence Committee, *Armed Forces Pensions and Compensation*, First Report of Session 2003-04, HC 96-I para 97

⁷⁸ *Armed Forces' Pensions and Compensation: Ministry of Defence Response to the House of Commons Defence Committee's First Report of Session 2003-04*, Cm 6109, January 2004, para 24-5

⁷⁹ [HC Deb, 27 November 2006, c362W](#)

4. Introduction of AFPS 05

The *Armed Forces (Pensions and Compensation) Bill 2003-04* was introduced in the House of Commons in December 2003. Its main purpose was to give the Secretary of State for Defence the power to establish a new armed forces pension scheme: the Armed Forces Pension Scheme 2005 (AFPS 05), for new entrants to the armed forces from April 2005, and a new Armed Forces Compensation Scheme, to replace the existing War Pensions Scheme and the attributable benefits of the AFPS. The background to this is discussed Library Research Paper 04/05 [Armed Forces \(Pensions and Compensation\) Bill](#).

The *Armed Forces (Pensions and Compensation) Act 2004* received Royal Assent in December 2004. The details of the scheme are provided for in regulations. [Gov.UK explains](#):

Statutory Instrument 2005/438 and subsequent amendments are the legal basis of the scheme. See AFPS 05 legislation below:

- [AFPS 05 Order: SI 2005/438](#)
- [AFPS 05 Amendment Order: SI 2006/717](#)
- [AFPS 05 Amendment Order: SI 2009/544](#)

AFPS 05 was introduced for new entrants from April 2005. All members of the Armed Forces who were in service before 6 April 2005 and were still in service on 6 April 2006 were given the opportunity to transfer benefits they had built up in AFPS 75 to the new scheme, AFPS 05. The MOD explained the choice in a leaflet for scheme members:

The benefits offered by the two schemes are different in a number of major respects. However, where the new scheme offers improvements which may be to the advantage of you or your dependants, these are offset by changes which may be to your disadvantage. You need to consider which will be most to your advantage, not just now but at the point in the future when you leave the Armed Forces, whether it be leaving mid-career, after a full career, or if you become ill and are medically discharged.

The decision whether or not to transfer is an important one for you and your family. Your decision will affect the value of the benefits that will be payable when you leave or die. You will have only one opportunity to transfer, known as the Offer to Transfer (OTT), and once you have made your decision you cannot change it.⁸⁰

Some of the key features of the OTT were summarised as follows:

Service before 18 (for other ranks) and age 21 (for officers) is not reckonable for pension benefits in AFPS 75 but will count as reckonable in AFPS 05.

A maximum of 35 years' reckonable service can be transferred from AFPS 75 into AFPS 05, but AFPS 05 will provide the opportunity to build pension benefits up to 40 years which is not available under AFPS 75.

⁸⁰ MOD leaflet, [Offer to Transfer \(OTT\) A guide to making your pension scheme choice](#), 2005

Officers currently on an engagement to the Immediate Pension point who decide to transfer to AFPS 05 will have their commission extended to the Early Departure Payments 18/40 Point.

You have a limited time to make your decision. Your election form needs to be returned within three months of despatch. If it is not returned it will be assumed that you wish to remain in AFPS 75 so it is vital your form is returned on time.

There is one change to AFPS 75, in that preserved pensions will be paid from age 60 for all service before 6 April 2006; preserved pensions for service from that date will be payable at age 65.

The leaflet went on to compare in more detail the features of the two schemes.⁸¹ Further information about the [Offer to Transfer](#) is on an archived version of the MoD website.

4.1 Scheme guides

Information about the scheme is on Gov.UK. For example: [Guidance and documents relating to Armed Forces Pension Scheme 2005](#).

Updated [Guidance booklets](#) to explain how the schemes work include:

- [AFPS 05 - Your Pension Scheme Explained and other Benefits on your Discharge from the Armed Forces](#) (Re-issued August 2012)
- [Armed Forces Pension Scheme 1975 – Your Pension Scheme Explained](#) (February 2015)

4.2 Impact of reforms

The Pensions Policy Institute (PPI) said:

The schemes for the Armed Forces, Police and Fire have fewer members than the four main schemes. The reforms to the Armed Forces, Police and Fire schemes have reduced their average value by around 4% of salary for new entrants, from 37% to 33%. For long-serving members of the schemes, the reduction in value can be more significant. Members of these schemes can have an NPA of 55 or 60 provided that they remain in these schemes until retirement, but in future will have their NPA increased to 65 if they leave the scheme early.⁸²

PPI noted that, post reform, the schemes for the uniformed services remained more valuable than private sector schemes:

The schemes for the Armed Forces, Police and Fire are worth on average 33% of salary for new entrants. They remain more valuable than medium private sector Defined Benefit scheme and are significantly more valuable than private sector Defined Contribution schemes.⁸³

This partly reflects the fact the lower retirement ages and faster accrual in the schemes for the uniformed services.⁸⁴ These have been justified by the demands of the jobs involved. In the context of proposals to

⁸¹ Ibid

⁸² PPI, [An assessment of the Government's reforms to public sector pensions](#), October 2008, p7

⁸³ Ibid, p9

⁸⁴ [Independent Public Service Pensions Commission: Interim report](#), October 2010, para 5.20

increase the pension age in public service schemes generally, the Labour Government said in 2003:

There will continue to be some occupations such as the armed forces, fire service and police where the need for a recognised physical capacity justifies the award of normal pension at a lower age, but for individuals who leave before they reach such an age their pension would also be deferred to age 65.⁸⁵

No data was available to show the savings the Government expected from the reforms to schemes for the uniformed services. (Estimates of savings from the reforms to the schemes for teachers, NHS, civil servants and local government were produced).⁸⁶

4.3 Role of the Armed Forces Pay Review Body

In April 2004, the then Parliamentary Under-Secretary of State for Defence, Ivor Caplin, announced that the Government had decided to give the Armed Forces Pay Review Body a role in “externally validating” the provisions of the AFPS. The AFPRB provides independent advice to the Prime Minister and Secretary of State for Defence on remuneration and charges for members of the armed forces. In setting pay, it takes account of the value of the pension scheme. The Minister hoped this change would provide for more independence in reviewing the scheme:

The Parliamentary Under-Secretary of State for Defence (Mr. Ivor Caplin): During Standing Committee consideration of the Armed Forces (Pensions and Compensation) Bill in February, concern was expressed that the Government should provide more independent oversight of the arrangements provided for the armed forces in this area. I made clear to Committee members that I recognised the intent behind these concerns and we have considered how we might respond. We have now decided that we will give the independent Armed Forces Pay Review Body (AFPRB) a role in externally validating the provisions of the Armed Forces Pension Scheme (AFPS); we plan that this will be done in the context of their quinquennial valuation of the AFPS, though more frequent examinations of the scheme provisions could be undertaken if wider developments justified this.

The broad intent is that the AFPRB would compare the scheme provisions with practice elsewhere in the economy and consider the extent to which they meet the recruitment and retention needs of the armed forces. The Review Body's observations would then be made public in a supplement to the following annual report and the Government would also make public their response to these observations. I am pleased to say that the Chairman of the Review Body and his colleagues have agreed to take on this additional responsibility and we are now in discussion on the detail to determine the timing of the first such review. I am confident that this change will provide for more independence in reviewing the terms of the AFPS while equally helping us to ensure coherence across the broader remuneration package, comprising both pay and pensions. It should also provide additional reassurance for service personnel by ensuring effective

⁸⁵ DWP, HM Treasury, Inland Revenue, *Simplicity, security and choice: working and saving for retirement*, December 2002, Cm 5677, chapter 6, para 66

⁸⁶ *Ibid.*, p8

independent validation of the appropriateness of the pension provisions for our armed forces.⁸⁷

The AFPRB's first periodic independent assessment of the new Armed Forces' Pension Scheme is scheduled for 2011⁸⁸

⁸⁷ [HC Deb, 30 April 2004, c66WS](#)

⁸⁸ [Armed Forces' Pay Review Body, Thirty-Seventh Report – 2008](#), para 6.6

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