

Sixty second summary

Government suggests ‘GMP equalization’ solution

The Department for Work and Pensions has put forward a possible method of equalizing pension scheme benefits to compensate for differences in guaranteed minimum pensions for men and women.¹

The problem with GMPs

The guaranteed minimum pension (GMP) is a creation of statute, and every aspect of it is determined by law. The calculation of GMP for a woman differs from that for a man, primarily because it is payable five years earlier (at age 60). It creates disparities in the rates at which the benefit accrues to men and women, and the periods for which it is subject to pre- and post-retirement increases. As a consequence, two people with identical birth dates and details of service and earnings can expect to receive different GMPs simply because one is a man and the other is a woman. There are side effects upon the calculation of any scheme benefits in excess of the GMP.

The GMP itself cannot be equalized for men and women without eliminating the disparities from the underlying legislation. Successive UK governments have, however, argued that European Union law obliges the trustees of occupational pension schemes to take into account the idiosyncrasies of GMPs when equalizing their benefits overall (not all legal experts agree with the analysis of EU jurisprudence that has been put forward in this context). In 2012, the DWP circulated draft legal amendments that would have brought the matter to the fore, in conjunction with a proposed, officially sanctioned procedure for equalization. The method advocated was, however, widely criticized as being overly arduous and costly to administer, and because it would have inflated liabilities to an unnecessary degree, and so the issue was parked to allow time for a group of industry experts to formulate more acceptable proposals.

Plan B

The procedure that is now being suggested would involve a one-off comparison of the value of the benefits accrued by a member during the period at issue (17 May 1990 to 5 April 1997) against the value of the benefits for that member’s hypothetical, opposite-sex counterpart.² The higher of those two values would then form the basis for conversion of the GMP into an ordinary scheme benefit. The second-stage conversion avoids the need to maintain running parallel GMP calculations for the lifetime of the member (and that of his or her survivors), which was the primary criticism of the previously mooted method.

The facility to convert GMPs into other scheme benefits already exists, but has been seldom if ever used. The equalization working group has suggested several changes to the minutiae of the GMP-conversion legislation. The consultation document mentions some matters about which the Government has made a decision, and other issues on which discussions continue. It says that the resulting changes will have to wait ‘*until a legislative vehicle becomes available*’ (that is, for the DWP to be given a slot in the Parliamentary timetable for an amending Act). Official guidance on GMP conversion—and perhaps the final version of the suggested equalization method?—will be published once those changes have been made.

The Government emphasizes that the UK is, for the time being, a full member of the European Union, and that EU law will continue to have effect for as long as that remains the case.

¹ <www.gov.uk/government/uploads/system/uploads/attachment_data/file/572751/consultation-occupational-pension-schemes-draft-regulations-and-related-issues.pdf>.

² <www.gov.uk/government/uploads/system/uploads/attachment_data/file/564536/ten-stage-possible-process-for-resolving-the-gmp-inequalities-issue-for-comment.pdf>.

Other matters

The consultation document covers other matters related to contracted-out benefits. A set of draft Regulations would, for example, allow extension of the notification and payment deadline for a contributions equivalent premium where trustees are trying to agree the details of a member's contracted-out record with HMRC, using the scheme reconciliation service.³ It would also set the fixed-rate GMP revaluation percentage at 4 per cent per annum for those members who were still in contracted-out service on 5 April 2016 (immediately before contracting out was abolished) and leave pensionable service on or after 6 April 2017.⁴

Other possible legal changes are being considered. The Government has, for example, been asked to allow transfers of contracted-out benefits to take place in some cases without a requirement to obtain members' consents, to schemes that have never been contracted-out. This might be desirable if an employer is seeking to restructure its pension arrangements by consolidating several schemes. The consultation document indicates that any such changes will not be made before autumn 2017.

Responses to the matters covered by the consultation document should be submitted by 15 January 2017.

The Government emphasizes that the suggested method would be just one way of equalizing, and that it is neither advising trustees that it is the best option, nor obliging them to adopt it. Schemes that have already equalized do not have to take any further action as a result of the Government's proposals. Nevertheless, given the Government's belief that those who follow the procedure would thereby satisfy their GMP equalization obligations under EU law, it is probably as close to an officially endorsed solution to the problem as one is going to get.

The process laid out is deceptively simple. In practice, it is likely to be very costly and time-consuming, especially given that matching scheme records with those held by Her Majesty's Revenue and Customs, using its Scheme Reconciliation Service, is an (understandably) integral part of the plan. The SRS is already groaning at the seams, and users are experiencing long delays in receiving responses to their queries (we note as an aside that in another consultation paper published on the same day the Treasury mentions the possibility that the public-sector schemes will be put through the SRS too⁵).

Whilst the legislative changes and guidance discussed by the Government are probably two to three years away at least, there are sensible steps that trustees can take to prepare their schemes. These include data-cleansing exercises and preliminary discussions with their actuarial and legal advisers.

³ <www.gov.uk/government/uploads/system/uploads/attachment_data/file/564824/annex-c-draft-occupational-pension-schemes-and-social-security-contracted-out-and-grb-misc-amdts-regulations-2017.pdf>.

⁴ The Government Actuary's advice to the DWP about fixed-rate revaluation is available at <www.gov.uk/government/uploads/system/uploads/attachment_data/file/564535/gad-report-fixed-revaluation-rate-for-guaranteed-minimum-pensions.pdf>.

⁵ <www.gov.uk/government/consultations/indexation-and-equalisation-of-gmp-in-public-service-pension-schemes/consultation-on-indexation-and-equalisation-of-gmp-in-public-service-pension-schemes>.