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Sixty second summary

GMP equalization: brace yourselves

The trustees and sponsor of a UK defined benefit pension scheme await a High Court ruling on whether they must compensate members for differences owing to guaranteed minimum pensions (GMPs). Most DB schemes in the country stand to be affected by the judgment. What is the issue, what might the solution(s) be, and how can you prepare?

What is a GMP?

From 6 April 1978 to 5 April 1997, sponsors of DB pension schemes were able to make their employees 'contracted out' of the earnings-related aspects of the State pension, ensuring that both employer and employee paid lower National Insurance Contributions, as long as the schemes provided a 'guaranteed minimum pension'. In broad terms, the GMP replaced and replicated the State Earnings Related Pension Scheme (SERPS): however, there were some differences, notably in the details of pre-retirement revaluation and post-retirement increases.

Why are GMPs unequal?

Pensionable age, for GMP purposes, is 65 in the case of a man, and 60 in the case of a woman. The GMP for a woman will accrue faster, be revalued less, and be in payment for longer than that of a man with the same dates of birth and death. When compared with the benefits in excess of GMP that have accrued in defined benefit schemes over the same period, a GMP will typically be revalued more generously, pre-retirement; but it could increase at a higher or lower rate once in payment (there being no statutory requirement to increase 'excess' pension accrued before 6 April 1997, this detail will vary from scheme to scheme).

The combined effects of GMP inequality can mean that a particular member's pension is lower at any point than it would be if he or she were of the opposite sex; they can also mean that the position is reversed at a later date, putting the same member in the 'advantaged' category.

Why is there now a court case?

The principle that men and women should receive equal pay for equal work extends to the benefits paid to employees under occupational pension schemes. That was established by the famous *Barber* judgment[1] on 17 May 1990 (which became the backstop date for equalization claims) and developed in subsequent court decisions. Ever since, there has been debate about whether and how the principle applies to GMPs, which occupy an unusual position as a quasi-State benefit. Since 2010, successive UK Governments have held to the view that any inequalities resulting from GMP differences in benefits accrued since *Barber* should be removed (regardless of whether a disadvantaged person can identify an opposite-sex comparator).[2] All legislative and other initiatives intended to settle the matter have, however, fallen by the wayside, and some commentators continue to question the need for such equalization.

Against that backcloth of uncertainty, Lloyds Banking Group, the trustees of its pension schemes, and a trade union representing its employees agreed to refer the matter to the High Court.

[1] *Barber v Guardian Royal Exchange Assurance Group* (C-262/88).
[2] *Hansard*, House of Commons, 28 January 2010, Column 66WS <https://publications.parliament.uk/pa/cm200910/cmhansrd/cm100128/wmstext/100128m0001.htm#10012850000017>.

What has the Court been asked?

The main questions put to the judge were

- does the law require equalization for GMP differences?; and
- if so, how should it be accomplished?

In the event that he decides that equalization is necessary, the judge has been asked some supplementary questions, such as:

- whether there is a limit on how far back the trustees might have to go in equalizing past instalments of pensions in payment;
- whether they should pay interest on those under-payments; and
- the implications for past transfers (both inward and outward).

Equalization methods

The Court has been asked whether there is a single correct method of equalization (if indeed it is necessary), or if the trustees have a choice of acceptable methods. The parties to the litigation put forward (broadly) four equalization methods. Roughly summarized, they involve:

1. separately considering, and where necessary equalizing, each feature of the pension (GMP and non-GMP), annually;
2. annually, calculating the member's pension and what it would be if that member were of the opposite sex, and paying the higher of the two;
3. performing the same annual comparison as in method 2, but keeping a running total of pension paid, so that a member who has benefitted from equalization increases is not overcompensated if the advantaged and disadvantaged sexes later swap places; and
4. valuing the benefits of the member and the opposite-sex comparator actuarially, at a single point in time, then paying the difference to disadvantaged members in the form of an actuarially calculated pension increase.

Many people are watching for the outcome of this case—not least the Government, which has a few GMP liabilities of its own. The judgment could kick off a flurry of equalization activity; however, it is unlikely that everyone will have their questions answered (for example, the judge does not seem to have been asked about schemes that have been wound up with benefits bought out, or death benefits), so there may be additional hearings, other cases, or an appeal in this one.

The costs involved in equalizing for GMP differences will depend on the characteristics of the individual scheme (particularly the significance of GMP as an element of members' overall benefits) and the method used. There is currently some debate about how any increase in liabilities will be recognized in companies' accounts.

For now, trustees could usefully consider the state of their administration records (it is worth bearing in mind, in this context, that the deadline for submitting queries to Her Majesty's Revenue and Customs' Scheme Reconciliation Service is 31 October 2018). An equalization exercise is a significant project, so they may wish to give some thought to how they will manage it.

Lastly, the judgment is guaranteed to generate lots of headlines, and huge sums of money will be quoted—even though it could make little or no difference to a particular pensioner's income—so trustees may want to consider how they will respond to members' questions and how they will communicate the facts to them.

Clients often ask, '*Who will benefit from GMP equalization: men or women?*' The answer is, '*It depends.*' The Lloyds case was brought to court in the names of female members, but for some schemes it will be mainly men who stand to gain. In others, it could be a complete mix.