



In Touch technical update

Guidance on GMP conversion for equalisation

The cross-industry GMP Equalisation Working Group (GMPEWG) chaired by the Pensions Administration Standards Association, has published its promised *Guidance Note on GMP conversion*. This aims to show how schemes can use conversion in a proportionate and pragmatic way, by providing examples, in the absence of further guidance or legislation from DWP and HMRC.

At a glance...

- Guidance builds on the legislation, and the DWP conversion guidance issued in April 2019
- Outlines examples of approaches that either have already been adopted or are being considered
- GMPEWG is not advocating a particular course of action

The Guidance Note is based on GMPEWG's current understanding of the law, official guidance and industry practice.

GMP conversion legislation

The Guidance Note addresses the conditions that must be satisfied, including the requirement for actuarial equivalence and certification, the requirements on benefits for pensioners and survivors, and the procedural requirements, including consent, consultation and notification.

Conversion decisions

The guidance lists the possible benefits of GMP conversion, such as: reducing administration costs and complexity; simplifying the benefits to aid member understanding and communication; modifying the benefits to make them easier to hedge or buy out; and removing restrictions on member options. However, the impact of these issues will vary by scheme, and some schemes will be less likely to consider conversion.

Trustees will also need to consider:

- Which members are included in any conversion exercise (possibly including all members with GMPs rather than just those with post 1990);
- Which benefits are included; and
- The nature of post-conversion benefits - this could involve relabelling the GMP as a "pseudo GMP", minimal interference where some simplifications

Why bring you this note?

The GMPEWG guidance is long but we have set out the main issues and reference points.

Next steps

The practical approaches suggested by the GMPEWG will help schemes to progress GMP conversion if they choose to equalise using this approach.

Decision

You will need to decide who is being converted, the benefits included and the post-conversion benefit design.

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are made but three tranches of benefit are retained or much wider changes such as pension increase exchange “PIE” (with actuarial equivalence). GMPEWG notes that schemes could go further and offer PIE or bridging pension options at less than “actuarial equivalence” but the Guidance Note does not cover these situations.

Using GMP conversion - sample processes

Flowcharts illustrate how the process of using GMP conversion can work in practice, including the initial consideration of whether the conversion should proceed. For a bulk exercise GMPEWG suggests that a small scheme with good data could complete the process in six to nine months, but in other cases it could take a year or more.

Initial steps include designing the process, discussion between trustees and the employer and carrying out the consultation with members. GMPEWG sets out the expected workstreams that can run in parallel if it is decided to proceed with conversion.

For individual conversions at retirement the initial process is similar, with the design of the conversion being agreed up front, but the individual calculations and certifications will then proceed over time, as members retire. When notifying members of the outcome of the consultation, schemes have tended to refer to the intention to use GMP conversion at retirement, to leave open the flexibility to use an alternative method in future.

The guidance also sets out the key dates from a legal and actuarial perspective.

Technical aspects of GMP conversion

The GMPEWG approach to conversion seeks to provide both:

- equality of present value on the conversion date (setting the present value of the pre-conversion benefits as the greater present value of the total unequalised benefits for the member and the comparator)
- equality of post-conversion benefit payments, regardless of the member's sex (by designing the post-conversion benefits accrued from 17 May 1990 such that the amount of pension payable at all times in the future is equal regardless of the member's sex)

The GMPEWG notes that the Lloyds court case did not explicitly address whether the second aim is a legal requirement, but suggests trustees and employers should take legal advice if they propose a different approach.

The guidance then discusses the various options for post-conversion benefits – whether just relabelling benefits and creating a pseudo GMP, making further changes to remove the complications of GMP, or reshaping benefits more fundamentally. It also draws the distinction between a “one-step” process where future benefits are equalised at the same time as GMP conversion is applied, and a “two-step” process where benefits are first equalised using an alternative dual-records-based method and then

Action

Project planning will form an important part of a GMP Equalisation conversion project in order to meet the range of legislative and tax requirements.

Decision

We expect most schemes will want to achieve equality of both present value and future payments for men and women.

Decision

You will be able to choose between a “one-step” and “two step” process.

GMP conversion is applied separately to those equalised benefits (either immediately or after a period of time).

The GMPEWG also points out the possible different interpretations of the legislative requirement for the minimum survivor's benefits post-conversion: whether it should be at least half the "actuarial value" of the member's pension, or at least half the "amount" of the pension to which the member would have been entitled in respect of the relevant period.

Taxation issues

The Guidance Note seeks to explain the main pensions tax issues that have been raised in the context of using GMP conversion to achieve GMP Equality and demonstrates how schemes have in practice sought to address these issues.

The main areas of concern are in relation to the Annual Allowance (including the possible loss of the 'deferred member carve out') and possible loss of Fixed Protections and Enhanced Protection. The guidance notes that constraints have been applied to GMP conversion for members who may be affected.

It sets out some possible approaches to help address tax consequences:

- not converting GMP to scheme benefits until members retire.
- A "constrained conversion" approach, setting deferred revaluation at a level such that it does not create annual allowance issues, and making up for the lower revaluation through higher increases in payment
- "internal transfers" between arrangements in the same pension scheme to avoid creating an Annual Allowance input

Further detail of these is given in the appendices to the guidance.

Common situations and worked examples

The guidance covers three common situations in which GMP conversion is being used. For each exercise, the guidance sets out comments on the trustees' considerations, the eventual conversion benefits chosen, the process taken and any tax issues (including details of the reassurance trustees have sought from HMRC on an individual basis). There are also worked examples for sample members, to illustrate the particular problems.

A bulk one-off exercise for existing pensioners and dependants (for a scheme in the process of winding up)

Examples are given of a pensioner over age 65 and pensioner under age 60.

On-going pension scheme undertaking a bulk GMP conversion exercise for existing pensioners and conversion at retirement for non-pensioners

Examples show a member with benefit in payment, and a member whose benefit was not yet in payment and would be converted at retirement.

Decision

You will need to consider implications for spouses' benefits in order to meet the minimum legislative requirement.

Decision

Tax consequences are manageable but the right approach may depend on your scheme circumstances.

A bulk one-off exercise for deferred members.

Examples here show a member approaching retirement age, with benefits converted in deferment, and a younger member to demonstrate the impact on future deferred revaluation.

Benefit checklist

The guidance also sets out a benefit checklist to ensure proper understanding of the pre- and post-conversion benefits. The checklist would also help ensure that:

- member communications cover what they need to;
- scheme documentation is complete and accurate;
- the actuarial calculations achieve equivalence; and
- future pensions administration is as intended.

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