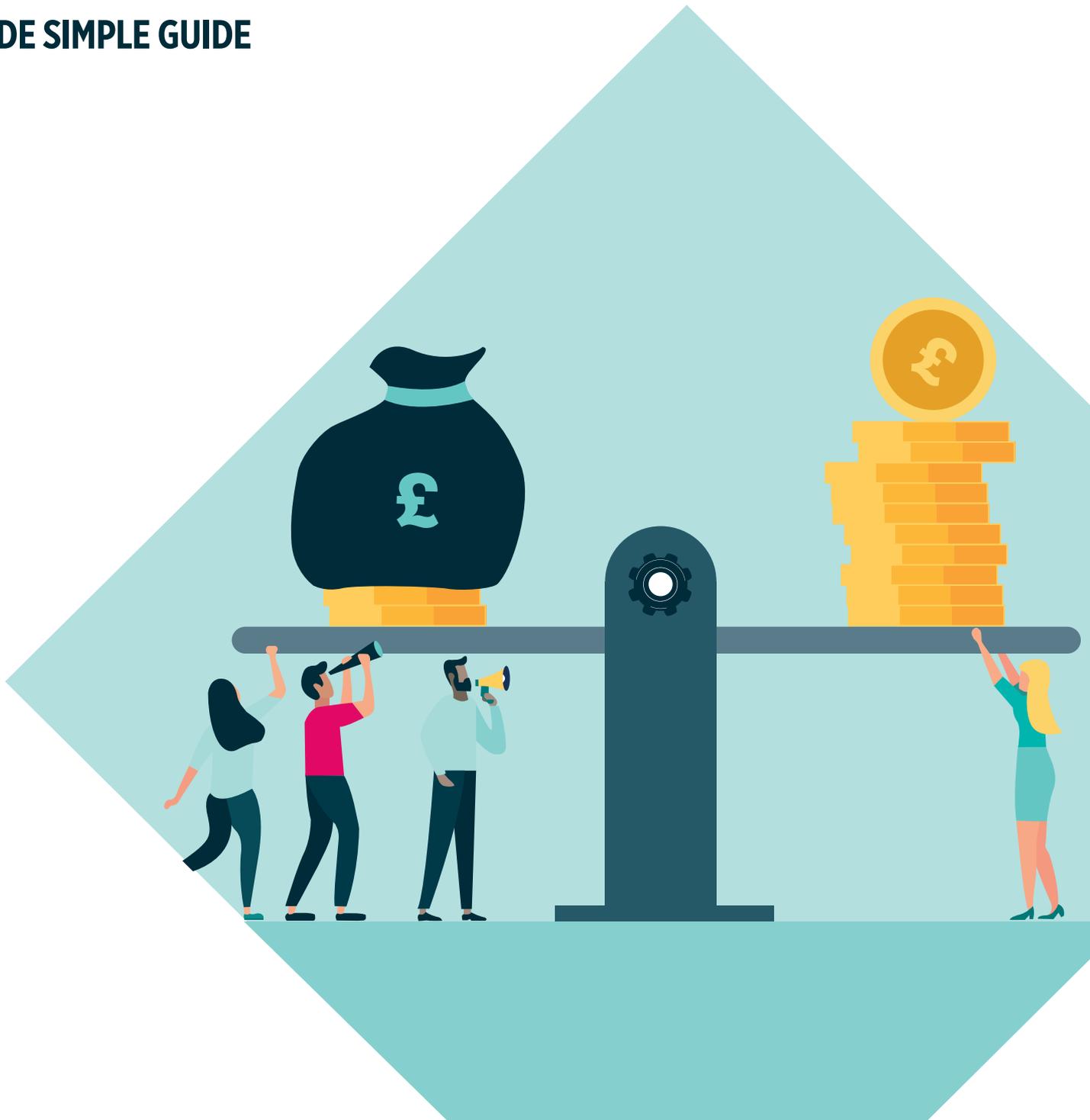


GMP EQUALISATION

MADE SIMPLE GUIDE





ACKNOWLEDGEMENTS

We would like to thank Equiniti for its help producing and sponsoring this guide. For further information visit

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1 INTRODUCTION – WHY GMP IS IMPORTANT

THE MATTER OF GUARANTEED MINIMUM PENSIONS (GMPS) MAY APPEAR TO HAVE ASSUMED GREAT IMPORTANCE ALMOST OVERNIGHT, BUT IN TRUTH, IT'S BEEN A LONG TIME COMING.

The spectre of GMP equalisation has been hanging over every contracted out occupational scheme for over 30 years. But the 2018 Lloyds case in the High Court upped the ante.

Doing nothing – or considering one's options – is no longer considered to be the same as taking a long term view. That does not mean that schemes and employers must put their collective shoulder to the wheel in order to wrap this project up in double quick time.

The process of equalisation remains a long game. There is no complete roadmap available, yet. And even if you have begun that journey, your destination is likely to be a long way off.

Guidance and insights will continually be offered by The Pensions Administration Standards Association (PASA). Meanwhile the Government continues to contribute to this process through the efforts of working groups at both the Department for Work & Pensions (DWP) and HMRC. The HMRC working group published its latest guidance in February 2020.

What schemes must do now is prepare to engage actively with the equalisation process. That means going beyond remaining compliant, to proactively prepare for the future.

The greatest obstacle to beginning a major project such as GMP equalisation is not knowing where to start. It should not be. Data is at the heart of the process and is a perennial problem for most schemes. The GMP reconciliation is top of the list – so you start with the right GMP figures.

For active and deferred members, getting on top of any scheme data imperfections will pay dividends over time. This is an opportunity to invest and scrutinise the existing TPR common and scheme specific (conditional) reports.

For pensioners and dependants, a more nuanced and intelligent approach is required. A scattergun approach to historical data is wasted resource. Historical data work should be targeted, proportionate and have clear purpose. There is a widely misconstrued view that past claim calculations will require reconstruction as a matter of course. This is not the case – it would be using a sledgehammer to crack a nut. For most schemes and the vast majority of pensioners, accurate GMP equalisation adjustments and arrears can be calculated from readily available member data starting with the current payroll. This nuanced approach will allow finite data budgets to be focused on the pensioners where it really matters. Expensive and data intensive reconstruction should only be used where it is strictly necessary (see Section 6).

It is said that a thousand mile journey begins with a single step. Don't get off on the wrong foot by thinking this can be managed by a subcommittee, through occasional admin reports or by an in house team.

For your scheme's GMP equalisation project to be a success requires all of your team members to be fully briefed and pulling together for the cause. This is not to be considered optimal, but paramount.

Schemes must involve all stakeholders and advisers from the start. And that means everyone: sponsor, actuary, investment consultant, lawyer, administrator, even technology partner. Without all these groups working together, then the notion that GMPS represent a nightmare project will become a self-fulfilling prophecy.

That doesn't mean it is going to be easy. It will stretch resources and try everyone's patience. But GMP equalisation must be achieved, and if your team doesn't pull together as one, the project will take considerably longer. There are many opportunities to shorten the road.



With the bill estimated at anything up to 4% of liabilities, that would have an obvious – and unpleasant – impact upon costs.

We recognise that GMP is hard to get to grips with. But it must be dealt with and so we offer this Made Simple Guide as an introduction to this highly complex subject.

We hope you find it useful and would welcome any feedback you have on the guide or the subject in general.

Duncan Watson

CEO – EQ Paymaster, Equiniti

NOTE

This guide makes reference to past and ongoing legal action and summarises key points for the purpose of giving a clear overview of a complex subject. Trustees should take appropriate advice on the circumstances of their own scheme before deciding what action to take when approaching GMP equalisation.



2 THE STORY SO FAR

A) HOW DID WE GET HERE? THE HISTORY OF GMPS

The old state pension was comprised of two components – the Basic State Pension (BSP) and the State Earnings Related Pension Scheme (SERPS).

Everyone paying National Insurance Contributions (NICs) at the full rate would build up a BSP. SERPS was a secondary top-up benefit that was based upon earnings.

Many employees opted out – or ‘contracted out’ – of SERPS, either voluntarily or because their pension scheme did so on their behalf.

The benefit to the employer was reduced, or redirected NICs, with employees giving up SERPS in exchange for at least as good or, more commonly, a higher scheme pension benefit.

Contracting out was limited to those in Defined Benefit (DB) or final salary schemes until 1988, when it was extended to members of Defined Contribution (DC) also known as money purchase occupational schemes and personal pensions. By 1992 more than five million had contracted out of SERPS.

In 2002, SERPS was renamed the State Second Pension (S2P) and contracting out was ended in April 2016, in favour of a single tier state pension.

To account for the benefits of opting out of SERPS, the **Guaranteed Minimum Pension (GMP)** was created. It was the minimum amount of pension that must be paid by a UK occupational pension scheme to employees who were contracted out of SERPS between 6 April 1978 and 5 April 1997.

B) HOW DOES GMP WORK?

The system that accrued GMP only ran between 1978 and 1997, when it was discontinued by the government. Notionally, GMP should be equivalent to the amount the individual would have received had they remained in SERPS.

There are two sets of rules that apply – one for 1978-1988 and another covering 1988-1997.

Accrual rates are different for these two periods. And there is no obligation for schemes to provide inflation-linked increases on service before 1988. That is not the case for service between 1988 and 1997, where inflation-linked increases are required but are capped at 3%.

If a DB scheme was contracted out, some – or all – of a member’s pension accrued between 6 April 1978 and 5 April 1997 will be made up of GMP.

C) SO WHAT’S THE PROBLEM?

Everything was fine until the *Barber vs Guardian Royal Exchange Assurance Group* case went before the European Court of Justice in 1990. Prior to this judgment, it was normal practice for UK occupational pension schemes to have different retirement ages for male and female members; typically 65 for men and 60 for women, which reflected state pension ages.

The case was brought by a Mr. Barber under the UK’s Sex Discrimination Act 1975, because he felt he had been treated differently by his scheme than a woman of the same age. Though this element of the case failed, because that act excluded pensions, a later European Court of Justice ruling, based on a definition of pension being a form of ‘pay’ would have implications for all contracted out occupational pension schemes.



From 17 May 1990, and later clarified in 1994, all UK occupational pension schemes were required to pay equal benefits to comparable men and women in relation to their service. Most schemes equalised pension ages and benefit scales between males and females, but few addressed inequalities arising from the calculation of GMPs based on sex. But it was not clear on how the unequal GMP should be treated.

Due to this uncertainty, most schemes did not equalise for the impacts of the GMP element of pension. Instead they chose to only equalise any non-GMP elements.

D) WHEN LLOYD'S BANK WENT TO THE HIGH COURT

In 2018, there was a landmark case when Lloyds Banking Group Pension Trustees Limited agreed with the sponsor of its schemes, the bank, and a union to seek clarity on whether it was the duty of the Trustee to remove inequalities in scheme benefits that arise as a result of unequal GMPs.

The Lloyds Banking Group case asked the High Court to determine whether GMPs need to be equalised and, if so, the method that should be used to adjust members' benefits. The judgment confirmed that GMP equalisation is required and provided a number of approaches that trustees might use – **see section 3**.

E) WHAT CREATES GMP INEQUALITIES?

Inequalities arise from the fact that GMP was designed to replicate the SERPS given up by the individual, and is covered by different rules. Some of these differences include:

- ▶ The age for receiving GMP is 60 for females and 65 for males.
- ▶ The GMP accrual period is shorter for a female to a male because female accrual ceases at 5 April before age 60 whereas male GMP accrual ceases at 5 April before age 65.
- ▶ The GMP accrual rate is normally higher for a female to a male (to compensate for the shorter accrual period).
- ▶ GMP will often have a different increase rate to non GMP – it can be higher or lower. For GMP accrued from 6 April 1988, schemes must provide inflation-linked increases in line with CPI up to 3% (RPI prior to 2010). There is no statutory requirement to provide increases on non-GMP pension accrued prior to 6 April 1997. However, some schemes chose to provide an increase on this pension under their scheme rules although where they did it is generally a different rate from the increases on GMP.
- ▶ GMP will often receive a higher revaluation rate in deferment than non-GMP benefits, depending on when a member has left contracted out service.
- ▶ There are anti-franking provisions that apply from age 60 for a female but from age 65 for a male. These are rules to prevent the offsetting of GMP revaluation against a member's non-GMP (excess) benefits once a member left contracted out employment. While affecting few members, this can be a material source of inequality. Specifically, GMP steps ups and later earnings additions in respect of 1990-1997 accrual may need to be applied or disappplied.

F) WHAT DOES IT MEAN FOR SCHEMES AND WHO DOES IT AFFECT?

Though it concerned the schemes of Lloyds Banking Group, the judgment provides a legal precedent for other schemes. This is likely to affect many UK DB pension schemes with members who built up a GMP between 17 May 1990 and 5 April 1997.

It will also include some DC schemes that have a GMP ‘underpin’ benefit.

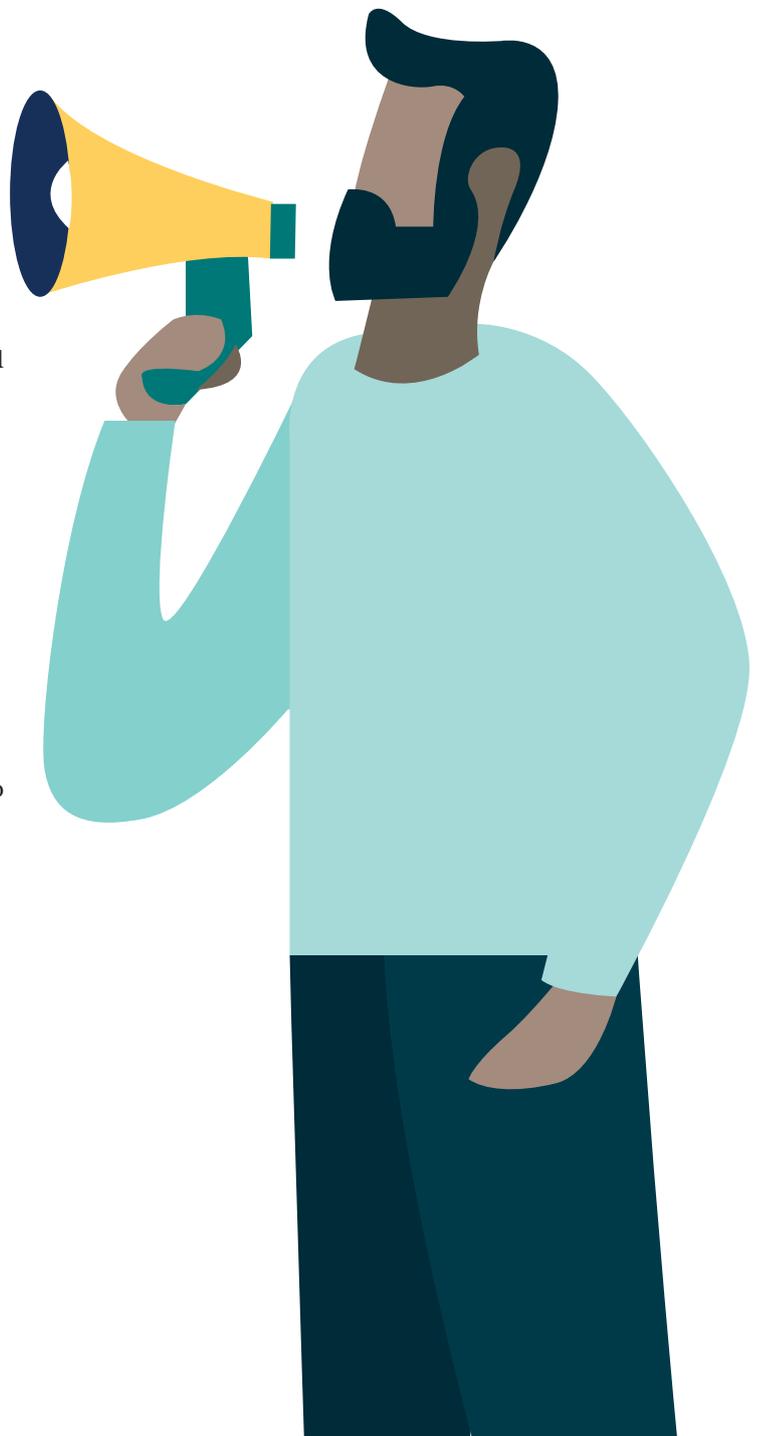
The fact that occupational pension schemes would have to adjust scheme benefits to remove the inequalities that arise from unequal GMPs came as little surprise. This was the position the Department for Work & Pensions (DWP) had maintained since 2010.

The difficulties facing schemes arise from the need to recalculate benefits over a period of almost 30 years. Next, schemes must determine which of a number of methods they will use. Trustees should follow the method that requires the least interference with the benefits of any group of members, unless the employer agrees to a more generous method or to GMP conversion. Trustees must also consider whether this requires them to adjust future transfer values to reflect the judgment.

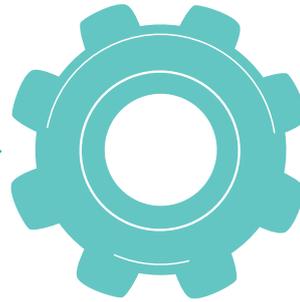
If there is any change, then additional benefits will have to be funded. Employers must decide what impact this is likely to have on their profit and loss and their year-end accounts.

Trustees should also consider whether GMP equalisation has been allowed for sufficiently, where:

- ▶ A scheme is winding up or has recently been wound up
- ▶ The trustees have entered into a buy-in or are in the process of negotiating a buy-in or buyout
- ▶ A recent corporate transaction has taken place.



3 BALANCING THE BOOKS



A) WHAT ARE THE 'METHODS' FOR GMP EQUALISATION?

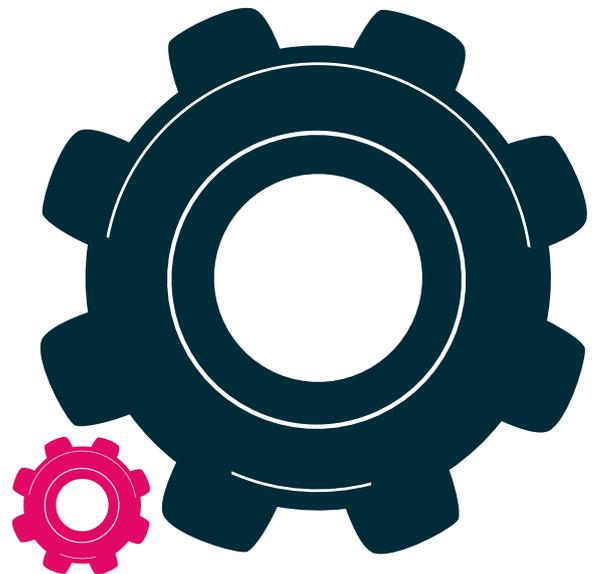
There are a number of alternative methods that may be used in the calculations for GMP equalisation.

Before the Lloyds Bank case, few schemes had made adjustments to equalise GMPs. The case has made it clear that schemes must adjust benefits to achieve GMP equality and that this should have been done since the Barber judgment of 17 May 1990.

Specific benefit designs will influence inequalities, but all schemes embarking on an equalisation project must review payments that have been made in the past and correct any examples of underpayment.

Past payments should be reviewed using a year by year approach for all members with pensionable service between 17 May 1990 and 5 April 1997, which is the date GMPs ceased to be accrued in contracted out schemes.

A correction payment will be due where a member's comparator – their equivalent of the opposite sex – would have received a higher benefit.



B) ONE YEAR AT A TIME...

The year by year approach requires schemes to operate a shadow pension record tracking the pension the member received against the pension their comparator would have received.

A shadow record is created from the date the member retired, tracking forward to compare the benefit paid to the member against what that benefit would have been if they had been the opposite sex during the period 17 May 1990 to 5 April 1997.

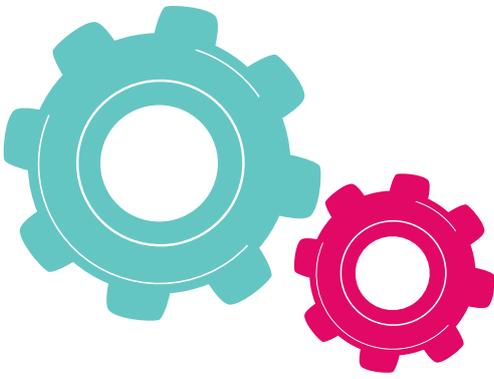
In its judgment, the High Court approved three different year-by-year approaches, referred to as methods B, C1 and C2 (see box GMP Equalisation Methods). A fourth, method A was opposed by the employer as the most expensive approach.

In reality, there are two leading methods that ongoing schemes are most likely to consider – C2 and D2. Some schemes may adopt B instead of C2 to avoid its complexity.

C2, which provides the higher of the male and female comparator pension each year, subject to accumulated offsetting, with interest should be applied first and the data retained. It may never be used for pensions in payment, but is the calculation to use to retain accurate GMP records.

If a scheme is heading towards GMP conversion, they will use D2 having already run their calculations under the C2 method.

Like D1, D2 compares an actuarial value of unequalised benefits with those of an opposite sex comparator. If lower, the member will receive additional pension. However, D2 then converts GMP into non-GMP benefits and is the method expected to be preferred by insurance companies offering bulk buyout contracts to schemes.



GMP EQUALISATION METHODS – AT A GLANCE

The different methods have been summarised here. They are not comprehensive definitions, but designed to give the reader an understanding of the general concept.

Method **A**

The pensions of an analogous male and female member are compared each year. Almost every year will see both receive an increase and whichever is the higher is paid to both leading to a hybrid pension.

There are three A methods and the union representing the members in the Lloyds Bank case preferred A3. Under A3, the higher increase is paid each year, but once done, it is acknowledged the equalising increase is not GMP.

The following year, the process is repeated. For schemes where the excess over GMP increases at a higher rate than GMP because you have 'banked' last year's equalising uplift as excess over GMP, the equalising uplift also receives the more generous non-GMP increase.

However, A is the most expensive method requiring dual records and is only permitted with the consent of the employer.

Method **B**

One of the three "better of" methods, this was proposed by the government in 2012.

The member's pension is calculated each year when an increase is due. Simultaneously, a calculation is made of what the pension would be if the member were of the opposite sex. Then, the higher amount is paid. This method requires the use of dual record keeping.

Method **C**

Annual increases to unequalised male and female pensions are calculated in the same way as method B. However, instead of the higher pension being automatically paid to both members, the accumulated amount of pension paid to date is examined.

The member will receive pension based on the highest accumulated pension to date, but that does lead to some unintended consequences, for instance where Method B and Method C get out of kilter – a pensioner would struggle to comprehend an arrears payment accompanied by a reduction in future pension.

The judgment allowed for two different method Cs, C1 which attracted no interest and C2, which did.

Method C1 is a cumulative method and produces a lower amount of past underpayment to Method B where the member has been a 'crossover' member (moving from advantaged to disadvantaged over the period of retirement – or vice versa).



Under Method C1, while the member is advantaged, a credit is built up reflecting the higher benefit than that payable to the comparator. When the member becomes disadvantaged in relation to the comparator this credit unwinds and only when it has been fully used up¹ does the member's pension step up to that of the comparator.

Method C2 is similar to C1 but interest is applied to the credit.

Both C1 and C2 require the use of dual record keeping. C2 is the lower cost approach and employers can require trustees to adopt the lowest cost method.

Method **D**

This may involve a one-off actuarial calculation of future rights to benefits of male and female comparators. Two variations were identified.

Method D1 is often used when a scheme is preparing for a bulk buyout of member benefits with an insurance company. The difference that arises as a result of unequal GMP is paid to the disadvantaged members as additional pension.

Method D2 uses GMP conversion legislation to provide “a pension which converts GMP structures into an alternative format (for example in line with non-GMP benefits) and is of equal actuarial value to the larger of the compared values”. This is similar to the approach the government proposed in 2016.

Method D uses single records. It requires employer consent, but could prove cheaper than C2.

¹ While this is what was said in the case, in practice if the 'own sex' pension under the rules is higher, it must be paid.



C) DECISIONS, DECISIONS

While the Lloyds Bank case judgment outlined a number of acceptable methods, it is up to trustees and sponsoring employers to determine which is the most suitable for them.

Member consent may also be required in some cases, if benefits are being converted. For instance, any changes could adversely affect fixed protection in place, breaching the lifetime allowance, resulting in a sizeable tax liability.

There are a number of factors that schemes must consider when deciding on the method used to correct past underpayments. They include:

- ▶ The number of members affected – e.g., if there are no crossover members in the scheme – crossover members are either advantaged or disadvantaged by the calculations at various times of their retirement (see below) – there should be no difference for members between the three methods.
- ▶ Administration costs – cumulative methods such as C1 and C2 require more complex administration. As a result, their implementation is likely to be more costly.
- ▶ How easy it will be to communicate the decision – and any calculations it generates – to the members.

D) EXAMPLES OF CROSSOVER MEMBERS – AND HOW TO DEAL WITH THEM

Not all members will be crossovers. The determining factors are both scheme and member specific, e.g. age at retirement, period of deferment and pension increase rates.

The charts illustrate how the different year by year methods B and C1/2 would apply to a crossover member. Chart 1 shows the benefit the member (red line) would receive without any GMP equality compared to the pension payable to the comparator (green line). This shows the member is initially disadvantaged but then becomes advantaged at a later date.

Chart 2 shows how method B would provide the member benefits calculated according to the dotted line – starting off on the higher (green) level and then reverting to the (dotted) red line at the point of crossover.

Chart 1

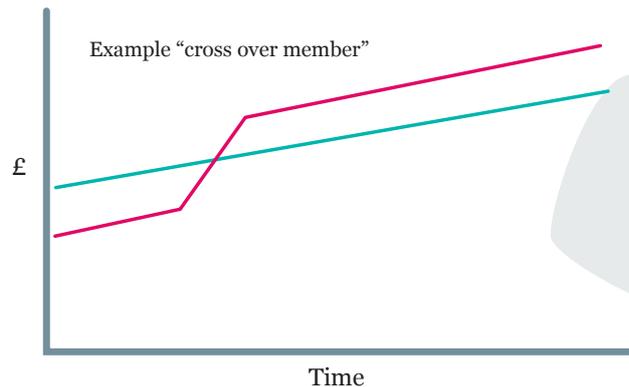


Chart 2

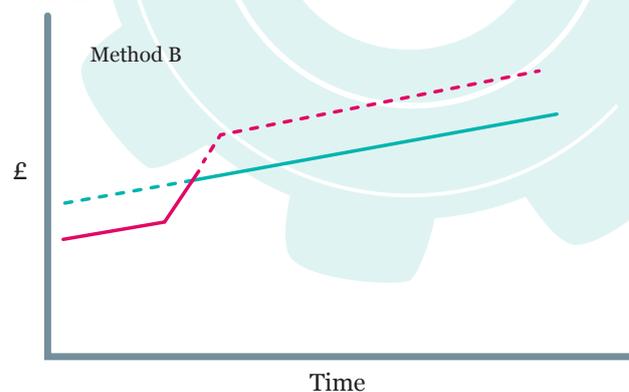
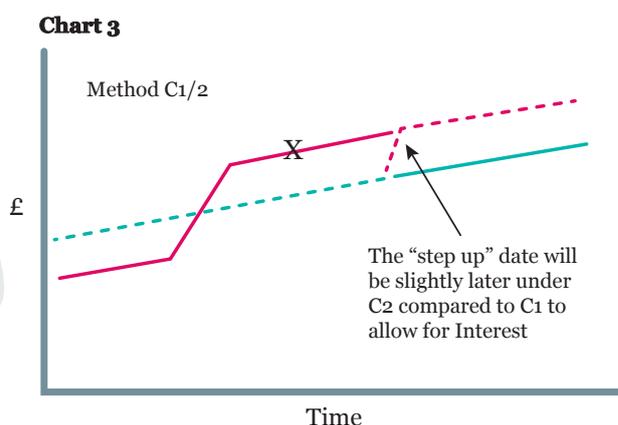


Chart 3 demonstrates a cumulative approach (method C1/2). The member's pension would again be adjusted to follow the dotted line – so would be higher, initially. However, the pension does not step up until later – once the credit for earlier higher payments has been used up. Once the credit has expired (with interest under method C2) the pension would revert to the member's (advantaged) level.



Care must be taken where a scheme adopts a cumulative method where GMP equality is implemented after a crossover member has moved from disadvantaged to advantaged status.

A member may be entitled to a payment for arrears, but the member's pension in payment must be reduced to that of the comparator. For example, if GMP equality is implemented at point X (see Chart 3), s/he would be entitled to arrears for past under-payments, but future payments should be reduced from the solid red line to the dotted green line. In practice, a modest reduction may be offset by normal annual increases, but schemes considering reducing the impact of a reduction by freezing the pension at current levels should take advice as to whether this creates any discrimination issues. It is for this sort of unexpected complexity, that some schemes may conclude Method C is too complex and instead stick to the more expensive but simpler to operate and explain Method B.

The pension in payment may not be reduced where GMP conversion is used to achieve GMP equality.

However, DWP guidance suggests the scheme actuary may take into account arrears paid to the member when assessing the actuarial value of any uplift required for GMP equalisation – although it is not clear the legislation allows for this.

E) WHAT ABOUT THE COMPARATORS?

Equality laws require a comparator of the opposite sex to the member for GMP, but this was not covered by the Lloyd's case. The parties involved in the case agreed there was no need for an actual opposite sex comparator for the purposes of GMP equality, and so the court did not decide if it was necessary elsewhere.

It is highly unlikely that any scheme, however large, would find an actual opposite sex comparator to any member, as that comparator would need to be of the opposite sex and to have (amongst other things) the same date of birth, the same joining/leaving dates and an identical earning history to the member.

Without actual opposite sex comparators, schemes must rely on hypothetical opposite sex comparators for each member and compare the benefit the member accrued in the period 17 May 1990 to 5 April 1997 against the GMP and excess the member would have enjoyed had they been of the opposite sex.

It should be assumed the comparator would have exercised the same options (e.g. early retirement, commutation, etc.) as the actual member, even where this may not have been possible for the comparator at the relevant time.

Schemes that have only ever held members of one sex should seek legal advice as to whether there is a need to equalise for the effects of GMPs at all.

4

WHO IS AFFECTED BY GMP EQUALISATION?

THE MEMBERS THAT SCHEMES MUST CONSIDER FOR PAST UNDERPAYMENTS FALL INTO THE FOLLOWING GROUPS:

- ▶ Pensioners in receipt of benefits who have only ever been advantaged compared to their opposite sex comparator. There are no past underpayments for this group.
- ▶ Pensioners in receipt of benefits who have always been disadvantaged require a correction.
- ▶ Pensioners who have crossed over from being disadvantaged to advantaged (or vice versa). The calculation of past underpayments will depend on whether the scheme adopts a cumulative approach.
- ▶ Survivors in receipt of benefits following the death of an active, deferred or pensioner member who may or may not have been disadvantaged in the past. The deceased member may have been disadvantaged if they died in retirement. This includes children and financial dependents, even though they will have no GMPs.
- ▶ Former members who took a transfer value from the scheme or whose benefits were secured by an individual annuity in the name of the member.
- ▶ Other 'no further liability cases' where the scheme has finished paying any benefits such as:
 - ▶ payment of trivial lump sums;
 - ▶ the death of a member/survivor with no further benefits payable; and
 - ▶ payment of serious ill health lump sums where no survivors' pension is payable.

There is no need to consider deferred and active members for underpayments as they will have received no benefit payments. However, they must be considered for equalisation in the future.

DE MINIMIS CASES

Identifying members in these various categories and calculating any disadvantage will eat up time and resources. Not all cases will require correction. In fact, a member may always have been advantaged.

Even when corrections are identified, in most cases, they will be modest. This raises two important questions for schemes to consider:

- ▶ Can schemes agree a tolerance – the de minimis – and choose not to make any adjustment to a member's benefit if it is below this level?
- ▶ Do schemes need to review all no further liability cases?

It has been suggested that schemes will generally consider it pragmatic not to adopt de minimis tolerance levels where a benefit is currently in payment. This is because much work will already have been done determining whether a member is disadvantaged and how much the correction exceeds the tolerance level. The thinking is that as implementation savings would be insignificant, it is easier to adjust the member's benefit.

Under the conversion method (D), the cost of incorporating the corrected benefit is minimal.

Under the dual payroll methods (B&C), there is a not insignificant cost to operating the dual payrolls. If there is a chance of the disadvantage increasing or a chance of a future cross-over (e.g. an advantaged member becoming disadvantaged) then members need to be tracked whether disadvantaged or not at the point of implementation.

However schemes may still wish to apply de minimis levels and should take advice before doing so.



TRANSFERS OUT

It is possible that members who have transferred out may have received a higher transfer value had the scheme equalised for GMPs before the calculation was made. This only applies to disadvantaged members when compared to their comparator, which may not be clear at the point of calculation.

Whether schemes need to review those cases – and whether sufficient data exists to do so – has yet to be determined. Schemes may wish to wait until the legal position is clearer.

Members who have transferred out are a discrete group and should not impede equalisation for remaining members.

OTHER CLOSED CASES (ALSO KNOWN AS NO FURTHER LIABILITY CASES)

There are a number of issues that can affect not only transfers out, but other no further liability cases.

There may be a lack of, or even absence of data. The name of a former member, let alone their benefit – split between GMP and excess – may not be known.

Even where data is available, tracing a member, their next of kin or estate may be disproportionately expensive if a relatively small sum is to be paid.

In addition to operating any limitation period, schemes may decide not to incur costs in trying to review and correct such cases.

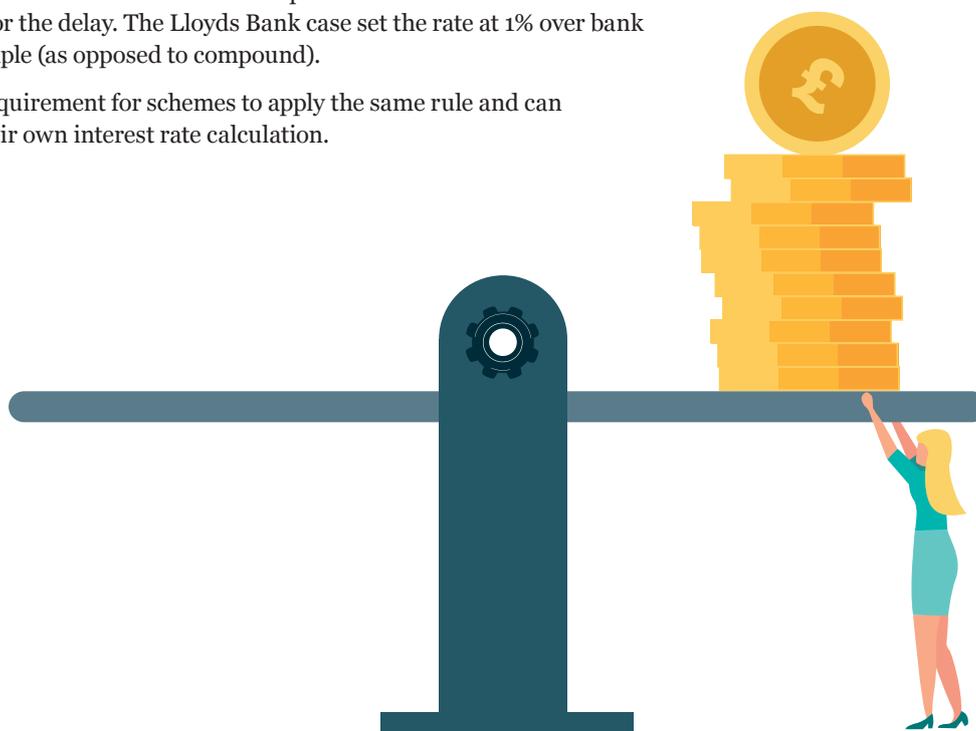
This would need to be a ‘commercial’ decision taken by the trustees with the employer. It does not remove any GMP equality liability. Therefore if a member, or their representatives made themselves known to the scheme, it must then calculate and correct any GMP inequalities, if data is available.

There are no stipulated rules on limitations. But a forfeiture rule may limit the need of a scheme to correct past underpayments. This will depend upon the specific scheme rules and their wording, and advice should be sought.

INTEREST ON PAST UNDERPAYMENTS

Past underpayments because of GMP inequalities will attract interest to compensate for the delay. The Lloyds Bank case set the rate at 1% over bank base rates simple (as opposed to compound).

There is no requirement for schemes to apply the same rule and can determine their own interest rate calculation.



5

ACTION STATIONS – WHAT HAPPENS NEXT?

WHEN DECIDING WHAT TO DO NEXT, A CLEAR DISTINCTION NEEDS TO BE DRAWN BETWEEN MEMBERS IN PAYMENT AND MEMBERS NOT YET IN PAYMENT.

GETTING ON TOP OF DATA – ACTIVES AND DEFERREDS

Schemes should be ensuring the data held for active members and deferred members is complete and accurate with greater vigour than before. The Pensions Regulator common data reporting scores should be as high as possible, and ideally, 100%.

The conditional data reports should be tailored to the specific scheme and used to focus data cleansing effort. This will benefit not just the GMP equalisation calculations but also day-to-day administration. It will also align with other objectives such as preparing for the industry pensions dashboard.

The GMP reconciliation for actives and deferred members should be as thorough as possible. The sooner the contracting out data is updated onto the administration system as part of the GMP rectification project the better – again not just for GMP equalisation but so that any benefits being put into payment are correct in regard to the GMP. Where GMPs are being changed on the system, more than one table may need to be updated so that data held is consistent and accurate.

GETTING ON TOP OF DATA – PENSIONERS AND DEPENDANTS

There is a belief in some quarters that an administrator is able, or should be able, to recreate pensioners and their records at the press of a button. This is not the case.

The Pensions Regulator common data and conditional data reporting for pensions in payment will cover essential data for the ongoing running of the scheme but historical data that is no longer needed for the ongoing operation of the scheme would not be covered.

Back in the 1990s many pension calculations were undertaken clerically. Even now, few schemes have fully automated calculations for every situation.

Many thousands of calculations will have been conducted. There will have been changes of scheme rules, in-house practice, scheme factors, external administrators, Scheme Actuary, payroll and administration systems. And, importantly for GMP equalisation, there will most likely have been a range of practices to address anti-franking (or not).

Claims data such as pension at leaving, full pension at retirement (pre-commutation) and cash taken, was not always recorded electronically. If it has been recorded, then it may not be accurate because quote data is often confused with the final claims data. It is not uncommon for such claims data to reside on physical paper files, microfiche, roll films and any other arcane record storage systems that may have been deployed over the past three decades.

Few administrator changes will see complete historic data effectively carried over. At the time of the migration, there was no reasonable justification to make historic data held on paper files into electronic data; or check its integrity and completeness in regard to pensions that were already in payment. Sometimes ceding administrators may not have passed over all data and there have been different interpretations over how long data must be held.

It must therefore be appreciated that however well intentioned, there will be gaps in historic scheme knowledge and member data. It will not be possible to reconstruct every pensioner record (or, for dependants, the first life record) within an acceptable time frame or cost. The cost for such reconstruction is likely to be measured in hundreds of pounds per record and the timeframe in years.



For those cases requiring an uplift for GMP equalisation, the typical average adjustment could be in the range of £75 to £125 per annum (before conversion). Uplifts will rarely exceed £500 per annum (before conversion).

If operating to very close tolerances and without simplifying assumptions, will the expense of conducting this work greatly outweigh any benefits to be paid to members?

This poses a difficulty for schemes. They must be pragmatic about what can be achieved, or else commit to spending anything up to millions of pounds recreating records, or finding data that may not even be used.

EXAMPLE OF WHAT HISTORICAL DATA MAY TYPICALLY BE HELD FOR A PENSIONER AND WHAT MAY BE MISSING

MEMBER INFORMATION TYPICALLY HELD 	MEMBER INFORMATION OFTEN MISSING 
<ul style="list-style-type: none"> • Current pension split by escalation type • Dates (birth, service, retirement, death) • Initial pension put into payment • Contracting out data including GMP agreed with HMRC from GMP Reconciliation project 	<ul style="list-style-type: none"> • Pension at leaving • Full pension (pre-commutation) at retirement • Tax Free Cash (PCLS) • Transfer-in details • Final Pensionable Earnings at leaving

AN ALTERNATIVE ROUTE

Fortunately, there are techniques (calculation solutions) available that side step the data challenge by delivering opposite sex GMP equalisation pension calculations and arrears based on the current payroll.

These calculation solutions are described as rollback or formulaic. They have been created recognising the reality of the limitations presented by historical data and scheme knowledge described above.

These methods work on the basis of readily available data i.e. payroll tranches, basic member data and contracting out data from the GMP reconciliation exercise. They can be used safely in most situations to deliver accurate figures.

However, they rely on simplifying assumptions. For a small number of situations when the simplifying assumptions do not hold, they may not be deemed sufficiently accurate. The trick is to identify these situations and focus what budget is available to improve accuracy in a proportionate manner on this subset of cases.

The fact that GMP equalisation is following an industry wide multi-year exercise to reconcile GMPs is fortuitous – because the contracting out data held and agreed with HMRC should be readily available and is crucial for a firm foundation.



TO RECAP – WHAT CAN SCHEMES DO TO PREPARE NOW?

Focus now should be on a really good GMP reconciliation and GMP rectification so the contracting out data is robust.

Then you should focus on improving the Pensions Regulator common and conditional data reporting scores.

Then you should establish the in scope population and segment it based on your supplier's data requirements.

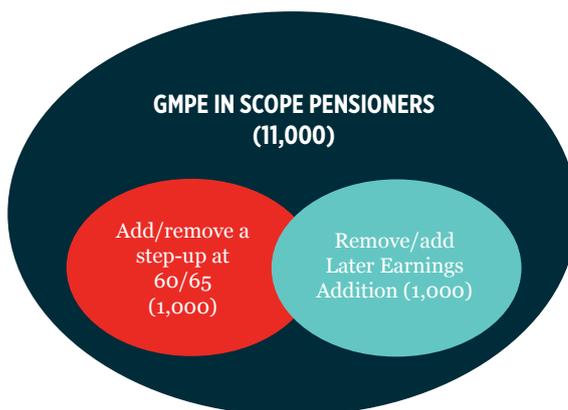
If your supplier intends to use full reconstruction to recreate some or all existing pensioner and dependant records then there will be a big historic data requirement.

If your supplier intends to use a formulaic or rollback solution to calculate the adjustment where possible, then the data challenge is much reduced and what budget exists can be focused on the cases that most need it. For example:

- ▶ there will be those who worked past the age of 60 that will require pensionable earnings data to calculate accurate Later Earnings Additions; and
- ▶ there may be GMP only members, where the circumstances that lead to them being GMP only may need to be examined and earlier (pre age 65) cashflows considered in more detail.

There may be members with complex 'step up' calculations that require full re-administration to remove the inequality. The Venn diagram "Anti-franking – what's all the fuss about?" demonstrates this significant source of inequality showing typical member proportions. Anti-franking is a difficult subject at the best of times, but when considering just the 1990-1997 component, it can become subjective and somewhat manufactured. Conundrums are created when it is found that house practices to address anti-franking have varied over time. When there is no right or wrong answer, then there should be a good case for simplifying assumptions and minimum interference to a member's benefit.

ANTI-FRANKING - WHAT IS THE FUSS ABOUT?



MEMBERS WITH ANTI-FRANKING ASPECTS REQUIRE MORE HISTORICAL DATA

Conundrums

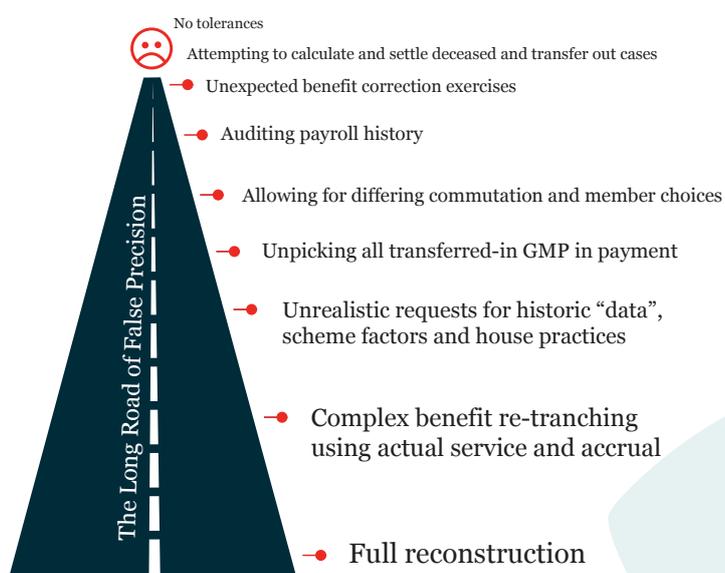
- House practice
- Actually paid?
- Consistent over time?
- 90-97 only, legislation written for all pre-97

Like most things in life, there is an easier path to follow (see Diagram Y: *Long and short GMPE roads*). A pragmatic and simplified approach using the existing payroll data and simplifying assumptions (the short road) can achieve the same outcome as the comprehensive – and costly – approach entitled *The Long Road of False Precision*.

It is not necessary for a scheme to possess or recreate every single piece of data relating to all members.

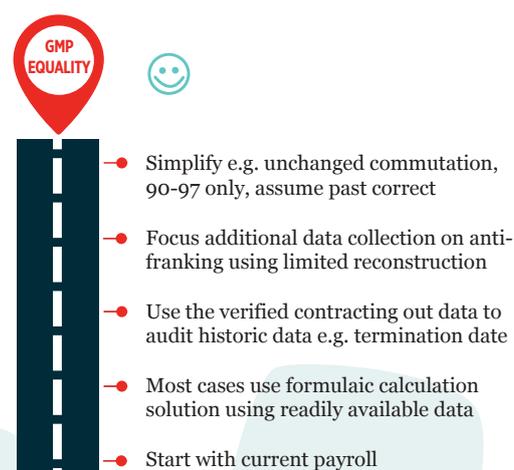
THE GMPE LONG ROAD

UNNECESSARY DATA COLLECTION AND RE-ADMINISTRATION



THE GMPE SHORT ROAD

FOCUSSED AND PROPORTIONATE



GOVERNANCE AND COMMUNICATIONS

It is essential that schemes bring together all the relevant participants – actuary, lawyers, administrator, etc. – so that all are pulling in the same direction. This will save time – and money – in the long term and keep the focus on the ultimate objective.

This will provide schemes with a strong management group with a unified view of the project, so that policy may be more easily translated into implementation.

A crucial, and often overlooked component is communication with the members. GMP equalisation is a fiendishly complex subject, and poorly communicated actions will only lead to confusion and additional cost in the form of contact from members concerned that their benefits are changing. If particular data items are required to support communications then this should be anticipated early in the data and calculation exercise.

6 SUMMARY/ CONCLUSIONS

WE WOULD LIKE TO MAKE IT CLEAR THAT WHILE WE URGE SCHEMES TO TAKE ACTION ON THEIR GMP EQUALISATION PROJECT, THERE IS AN AWFUL LONG WAY FOR THE PROJECT STILL TO RUN.

We don't have all the answers yet, and even when they come, it is likely that there will still be a lack of consensus. That is largely due to the individual nature of the project.

However much we tend to generalise, all schemes are to some extent different. Schemes must consider their particular circumstances – and those of their members - and determine which route is the right one for them.

Uncertainty should not be an obstacle to making a start on this project, but the journey may not be as wearisome or expensive as many schemes will fear.

Completing the preliminary work will only offer greater insights into the new stage of the project. And with all stakeholders and advisers operating as a single unit, work can be managed more effectively while delays and additional costs are minimised.



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