

EQUALISING GMPs

The issue

Most people who work in pensions dread the words “GMP equalisation” and, for about 25 years, have been ignoring it as being in the “too difficult” pile. Most people who don’t work in pensions have no idea what these words mean, and that is a very enviable place to be, when it comes to this issue.

Since the Barber Judgement in May 1990 (and enshrined in the Pensions Act 1995) pension schemes must treat men and women equally for service since 17 May 1990.

During the period up to April 1997, contracted-out schemes had to provide a ‘Guaranteed Minimum Pension’ (GMP) in return for members not participating in the State Second Pension or SERPS. The problem here is that the calculation of GMP is set in legislation, and is different for men and women. The GMP formed part of the total Scheme pension so most schemes took the view that while the benefits may be split differently (GMP v Excess over GMP) for men and women, at least they are receiving the same total pension benefit. In any case, the GMP is set in legislation so hands are tied - it is unclear how a scheme would or even whether it could equalise the GMP benefit.

The two parts of pension (GMP and Excess over GMP) increase differently from each other, so over time the total Scheme pension may end up being different between a man and a woman, depending on the level of increase applied to the different parts. To complicate matters further the greater benefit could sometimes be for a male and sometimes for a female. In 2012 the government consulted on a possible method of equalising GMP under which an annual test is carried out, and the greater amount is awarded (male or female), each year. This proposal was dropped after outcry from the pensions industry relating to cost and complexity, and also because the test resulted in a pension that was better than either a male or female would have received.

New Proposals

The government is consulting on a more straightforward test, involving actuarial calculations - but at least it’s a one-off test rather than annually. The government has made it clear that, while this is one solution, it may not be the only one and schemes can choose different methods. Schemes may have to take their own legal advice. The consultation ends on 15 January 2017.

The proposed approach involves:

- recalculating each member’s pension benefit as if the member had been of the opposite sex
- calculating actuarial values of the male and female benefits. The cash equivalent transfer value basis may be appropriate for this, but not necessarily (actuarial advice will be needed). Whatever basis is used, the assumptions should be unisex
- whichever value is greater, this value is converted back to a pension amount that is not GMP, using the existing facility in legislation to convert GMP into normal Scheme pension
- Members must be notified. At the moment, consultation with members is required but the proposals include the possibility of amending this to notification (before and after the conversion)

We suspect this will not be without problems, and communicating the changes to members could be very challenging. If the proposals go through (which may take most of 2017 as there are still areas needing clarity, particularly involving tax), we may see a number of schemes going through a GMP equalisation process in 2018/19.