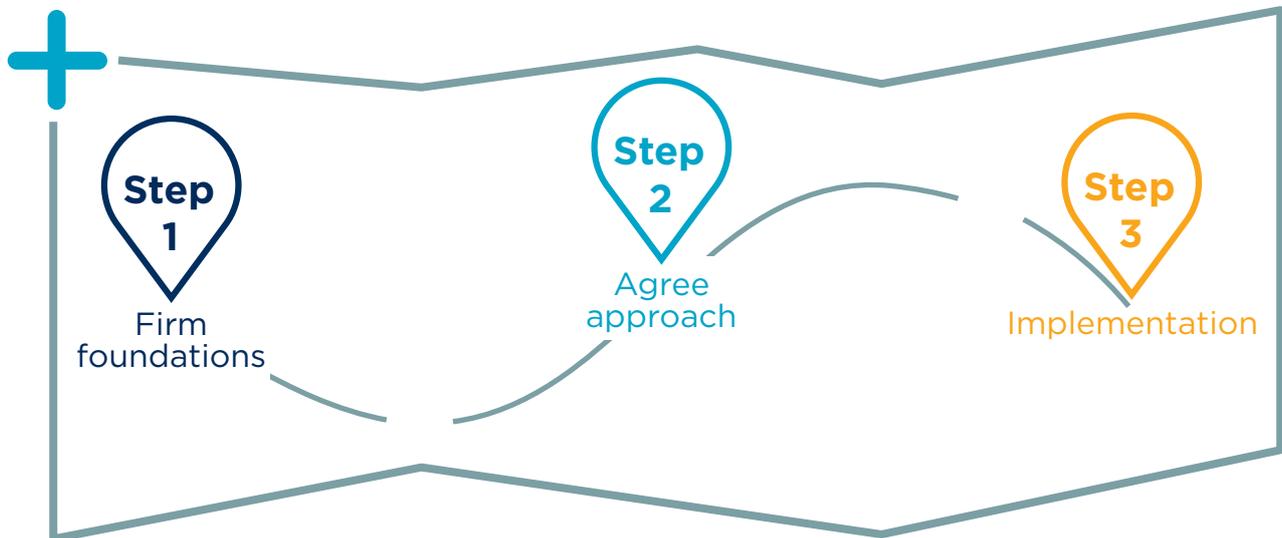


Addressing GMP inequalities – A road map

December 2018

In the light of the judgment on 26 October 2018 in the Lloyds Bank case, trustees and sponsors of pension schemes with Guaranteed Minimum Pensions (GMPs) are being advised by their lawyers that action needs to be taken.

In a topic fraught with complexity, we set out our road map to help you navigate the journey.



Step 1

Firm foundations



Member Communication

A first step is to ensure member communications have been updated to reflect the Lloyds Bank judgment and the potential need to adjust benefits in future.

A significant amount of work has been undertaken on this topic ahead of the 31 October 2018 deadline for raising bulk queries with HMRC. In some cases work continues ahead of the extended deadline of 31 December 2018.

Three important points are:

- It is still possible to resolve some queries with HMRC after the 31 October and 31 December 2018 deadlines. Valuable work can therefore still be done in 2019 to resolve remaining issues ahead of further clarity on the Lloyds Bank case.
- Just because HMRC records differ from those of your scheme does not necessarily mean the HMRC record has to be accepted. It may be appropriate to take legal advice in cases where the scheme is clear what the correct position should be and this appears to differ from HMRC's record.



GMP reconciliation

Before adjusting benefits to remove inequalities arising from GMPs it would be very helpful to be confident that the existing unequalised benefits are correct. An issue that many schemes are still working through is to ensure that all the GMPs have been reconciled with HMRC and a decision taken on rectifying any errors that have been identified.

- A decision needs to be taken whether rectification work resulting from the GMP reconciliation should be completed before addressing GMP inequalities, or if both projects should be run together.

On this last point, it may be helpful to members to communicate the results of the two projects as one, even if work is undertaken separately.



Administrative practices

Another important step is to establish current and past administrative practices in relation to:

- 1.1 Revaluation of benefits in deferment;
- 1.2 Early and late retirement;
- 1.3 Commutation for lump sum;
- 1.4 Any adjustments to pensions in payment at age 60 for women and age 65 for men;
- 1.5 Indexation in payment;
- 1.6 Dependants' benefits and transfers.

Our experience shows that many schemes have already implemented administrative practices that act to reduce inequalities arising from GMPs. There is also a wide range of administrative practices in relation to areas such as anti-franking and the application of actuarial factors (eg unisex or sex-specific). The practices your scheme follows and how these have changed over time could have a material impact on which members need an adjustment to their pension and how much that adjustment might be.

We would be happy to help you draw up a detailed set of questions specific to your scheme to ask your administrators.



Legal advice

It is important to understand how the Lloyds Bank judgment applies to your pension scheme. This requires scheme-specific legal advice. In obtaining this it is important to ask the right questions, recognising the current legal uncertainties.

Some questions you may wish to start with are:

1. What is known and what isn't yet clear?
2. How soon will the position become clear?

The further Court hearing that took place on 3 December 2018 is a timely reminder that the Lloyds Bank case has not yet completed the full legal process. Alongside the potential for an appeal there is the expectation of directions from the Court on the treatment of past transfers and commutations. There may also be clarifications on the application of the methodologies put to the Court and in areas such as anti-franking, approximations and de minimis cases and, previous transfers-in and transfers-out.

Guidance has also been promised by the DWP on the topic. The guidance is expected to focus on method D2 and the GMP conversion legislation, but it may have wider application.

Industry groups have also requested assistance and guidance from HMRC and the Pensions Regulator.

With so many parties involved and due process to be followed it could be several months before there is clarity. That said, there are questions that you can usefully ask now to ensure you have a firm foundation to work from once the uncertainties have been resolved.

Points that you might like to consider with your lawyers include:

- 1.7 Confirmation the Lloyds Bank judgment applies to my pension scheme.
- 1.8 Is there anything specific to my scheme that could restrict the options available to me?
- 1.9 Is full documentation (historic deeds and rules) back to 1990 available?
- 1.10 Do my scheme rules limit the arrears that need to be paid?
- 1.11 Are there any alternatives to adjusting benefits available to the trustees or sponsor? For example, a settlement or compromise payment.

We would be happy to help you draw up a detailed set of questions specific to your scheme.

Having established the details of administrative practices, there will likely be further questions to ask the scheme's lawyers to confirm the consistency of administrative practices with the scheme rules and legislation. Legal advice will also be needed to address areas where past practice cannot be established.

Step 2

Agree approach

Once the legal position is clearer and organisations such as the DWP and HMRC have issued any guidance, it should be possible to agree an approach to addressing GMP inequalities for your scheme.



Governance

Addressing GMP inequalities is likely to be a complex and time-consuming task. The exercise will be most efficient if good governance and strong project management is in place. In doing so we recommend a collaborative approach between the trustees and sponsor, with advisers being given clear roles and responsibilities.

In our experience a joint working group with delegation from the full trustee board and regular reporting can be very effective.

Clear communication is important to ensure that member expectations are managed.



Principles and objectives

To help guide decision making it is helpful to set clear principles and objectives from the outset.

The primary objective is likely to be the removal of inequalities in scheme benefits arising from unequal GMPs. Further objectives (which might conflict) could for example include:

- 2.1 To pay benefits no more than those required by the Scheme Rules and law;
- 2.2 To provide benefits in a form that will be straightforward and cost-effective to insure in future;
- 2.3 To minimise future administration costs and reduce the risk of administrative errors;
- 2.4 To simplify benefits for all members.

A number of principles may also be set to help agree a framework for achieving those objectives. Examples could include:

- 2.5 Treating members consistently;
- 2.6 Pensions in payment not reducing;
- 2.7 Not disturbing benefits in payment and existing administrative practices any more than necessary;
- 2.8 Not triggering material adverse tax consequences for members, where avoidable.

Consideration will need to be given to the implications of the proposed principles and whether they are realistic.

A key part of the process will be to consider how the requirement to address the inequalities in scheme benefits that arise from GMPs should interact with other sources of inequality and how the scheme has addressed these in the past. For example:

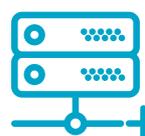
- Some schemes chose to remove inequalities in retirement ages for all pensionable service, not just post 17 May 1990 benefits.
- Some schemes treat all dependants equally, no matter what their gender or the nature of their legal relationship to the member. Others do not.
- Some schemes use unisex member option factors, others do not. In many cases the administrative practice will have changed over the years and may still vary depending on the purpose of the factor.
- The availability of some options (such as early retirement or a tax-free lump sum) may still be restricted differently for men and women under legislation, as a result of the continued existence of unequal GMPs which would remain in place under the A, B or C methods.

All these issues need to be considered to ensure a coherent approach.



Document methodology

Our experience shows that it is often the fine detail of the methodology that drives which members receive an adjustment to their benefits and how much it will be. We therefore recommend ensuring that the approach is fully documented in advance and signed off by all the relevant parties. This will mitigate the risk of misunderstanding and inconsistencies in treatment between members. It will also reduce significantly the need to revisit calculations as the project progresses.



Availability of data

The Court will set out the principles of what should be done in theory, but many schemes will be restricted in what can be done by a lack of available data. Any method will need to take account of the data available and the impact understood of different assumptions where there is a lack of data.

Step 3

Implementation

It is likely to be much easier to implement the agreed methodology for some groups of members sooner than for others.

Once a methodology has been agreed and documented, it should be possible to make updates to calculations such as transfer values and trivial commutations for non-pensioners relatively quickly, for example by the second half of 2019.

Making adjustments for benefits already in payment, particularly for those members who retired many years ago (some as long as 28 years ago, in 1990), is probably more likely to be a task for 2020. Schemes will need to obtain data, to test that data for consistency and to make appropriate assumptions where data is not available or inconsistent.

A key part of the project throughout, and particularly during step 3, will be clear and timely communication with members.

Want to find out more?

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