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GMP inequalities – is GMP conversion the answer?

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What we are covering today

The issue

- How GMP inequalities arise and why they matter
- What solutions are potentially available
- An outline of the GMP conversion solution

The GMP conversion solution in depth

- Methodology
- Model building and processing

Work outstanding

- Legislative difficulties
- Keeping the cost down



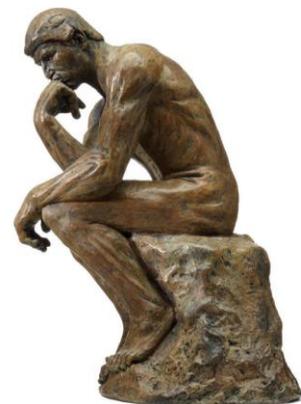
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The issue



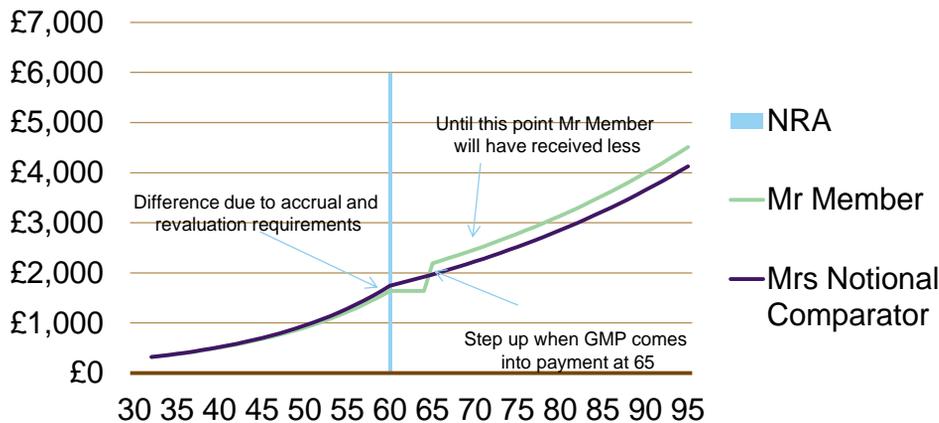
How unequal GMPs create unequal scheme benefits

- DWP legislation requires that a woman's GMP accrues at a greater rate than that of a man in recognition that a woman's working life for State pension purposes was five years shorter than that of a man.
- An equal scheme pension becomes unequal due to further DWP legislation under which:
 - The rate of GMP revaluation may differ to that on the excess;
 - Increases on the GMP in payment may differ to that on the excess;
 - There is a potential uplift on the GMP on coming into payment set by reference to a sex discriminatory GMP pensionable age.



An example of introduced inequality

Equal pension on leaving at 30, unequal payments begin at 60, man loses out until 70



Why the issue needs to be tackled

For GMPs (and excess) accrued 16 May 1990 – 5 April 1997

- Because DWP believes that Allonby implies that the need to resolve GMP inequalities is not dependent on finding an actual opposite sex comparator
 - And they could lay the 2012 regulations to turn their interpretation of an ECJ judgment into UK law
- Because DWP is of the view that it is not appropriate to make the GMPs themselves equal



Does Brexit affect any of this?

What options are potentially available?

Not all give certainty



- Do nothing and wait for any discrimination claim
- Set up a dual record
 - Each year pay the greater of the member and the opposite sex comparator; or
 - Each year pay what is needed so that there is no disadvantage when looking at the accumulation of past payments
- Establish a compensatory actuarial value
 - By valuing either of the two above and subtracting the value of the member's benefits
 - By valuing the member and the opposite sex comparator separately
- Deliver the compensatory actuarial value
 - As a one-off special payment?
 - Through setting up a new benefit?
 - As part of a GMP conversion exercise



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Why not the dual record system?

Could be delivering more than legally obliged

Pensions Admin systems will need to be materially amended

Expensive to set up and maintain

Difficult for members to understand

Cannot be certain that the adjustment is correct

For many the adjustment will be very small

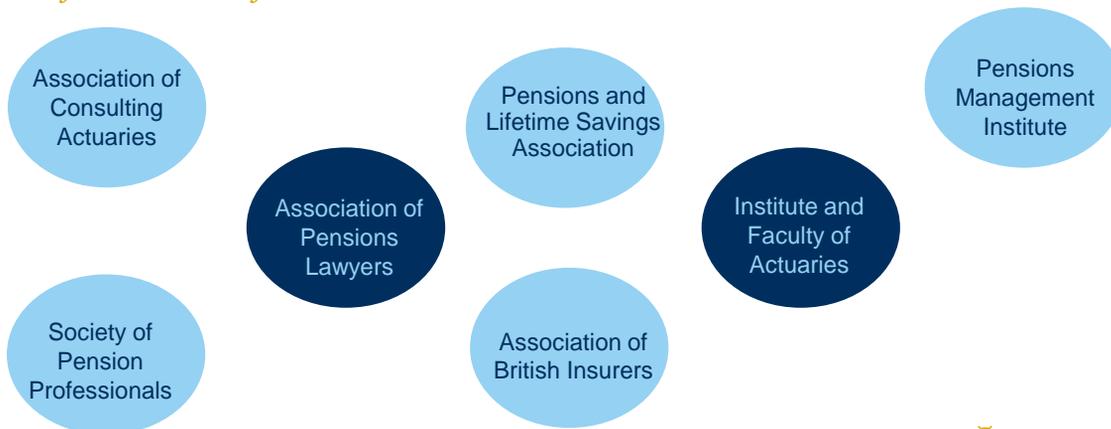


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The GMP conversion working group

Objective – to see if GMP conversion could be used



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Why GMP conversion to resolve GMP inequalities

- It preserves actuarial value and so is fair to affected members
- It will be much more popular with trustees than dual record keeping as
 - It is “once and done” so should be significantly cheaper to implement
 - It avoids fundamental rewrite of all admin systems, some of which are legacy and may not be able to cope
 - Members are more likely to understand it
- The Government says that the method put forward by the working group is acceptable

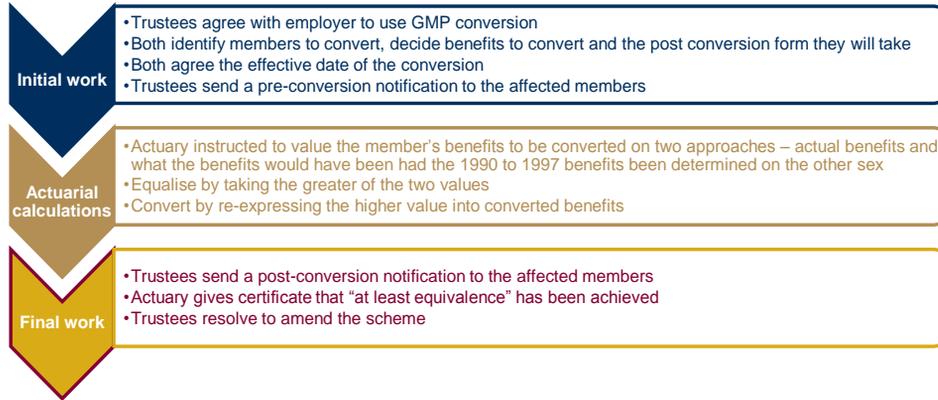


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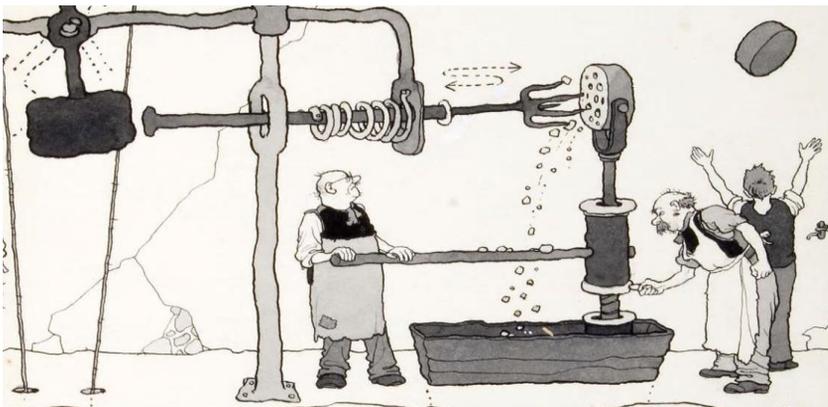
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How GMP conversion could work

Largely within the current GMP conversion law



The GMP conversion solution in depth



Methodology – Deferred Pensioners

Subdivision

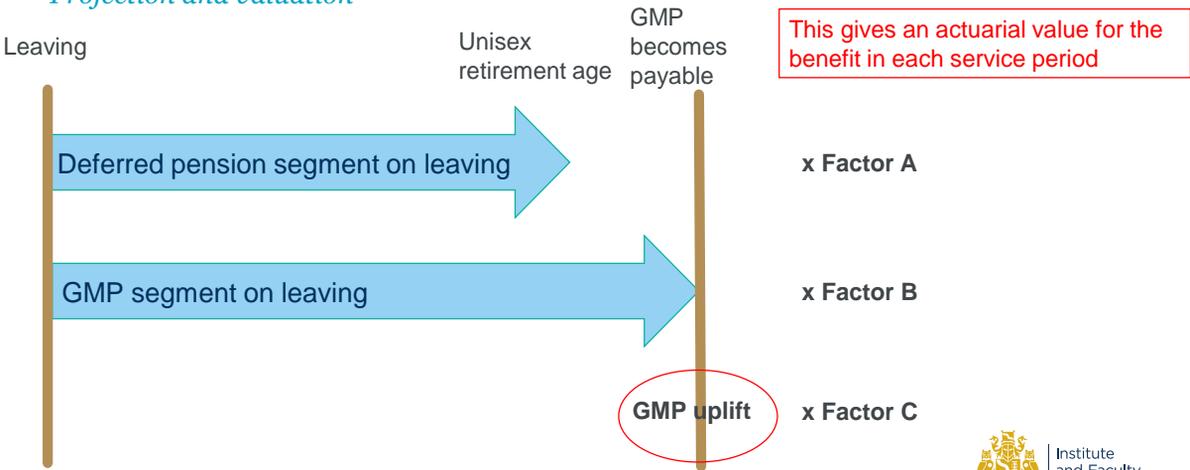
- Starting point is deferred pension (and GMP) on leaving
- Segment into service periods – three types:

	Service period	GMPs	Age at which benefits can be taken
1	Pre 6 April 1978	No GMPs accrued	Likely to have sex-based differences
2	6 April 1978 to 5 April 1988	Pre-1988 GMPs accrued	Likely to have sex-based differences
3	6 April 1988 to 16 May 1990	Post-1988 GMPs accrued	Likely to have sex-based differences
4	17 May 1990 to retirement equalisation day	Post-1988 GMPs accrued	The lower age would apply to the disadvantaged sex
5	Retirement equalisation day to 5 April 1997	Post-1988 GMPs accrued	A unisex (and potentially new) age applies
6	6 April 1997 onwards	No GMPs accrued	A unisex (and potentially new) age applies



Methodology – Deferred Pensioners

Projection and valuation



Methodology – Deferred Pensioners

Valuation and uplift

- Add together those for segments 2-5 only → **Amount A**
- Repeat the process by projecting the benefits again, but:
 - only for segments 4 and 5
 - assuming of the opposite sex (with an opposite sex GMP)
- Multiply each benefit in segments 4 and 5 by Factor A, B and C as before
- Add together new values for segments 4 and 5 with old values for segments 2 and 3 → **Amount B**

Service period	Amount A	Amount B
1 Pre 6 April 1978	X	X
2 6 April 1978 to 5 April 1988	Own sex	Own sex
3 6 April 1988 to 16 May 1990	Own sex	Own sex
4 17 May 1990 to retirement equalisation day	Own sex	Opposite sex
5 Retirement equalisation date to 5 April 1997	Own sex	Opposite sex
6 6 April 1997 onwards	X	X

Conversion Budget = max (Amount A, Amount B)

GMP inequality uplift = max (Amount A, Amount B) – Amount A



Methodology – Deferred Pensioners

Conversion

Conversion Budget = max (Amount A, Amount B)

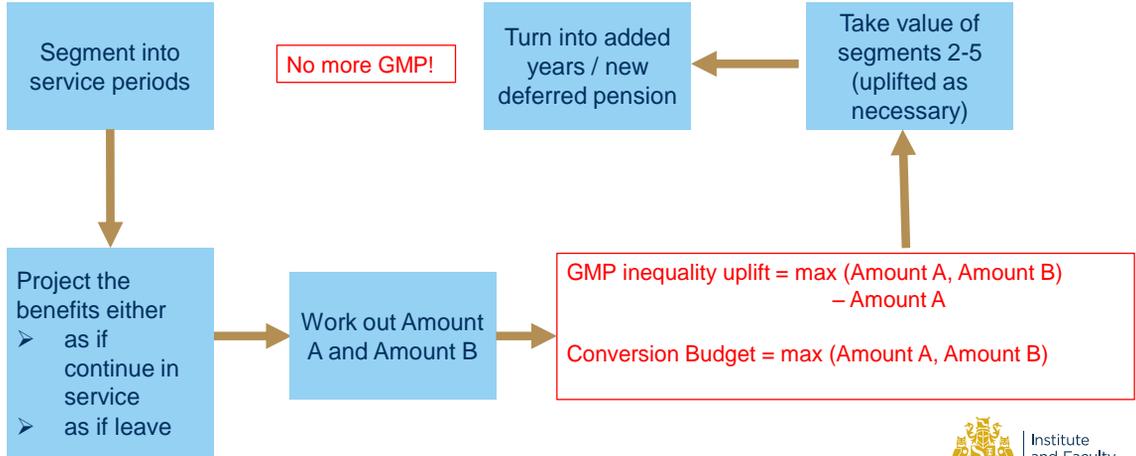
- Take the conversion budget (the value of segments 2-5 uplifted where applicable)
- Turn into a new deferred pension at date of leaving on the basis of actuarial equivalence
- The GMP no longer exists

Service period	Converted?
1 Pre 6 April 1978	No
2-5 6 April 1978 – 5 April 1997	
6 6 April 1997 onwards	No



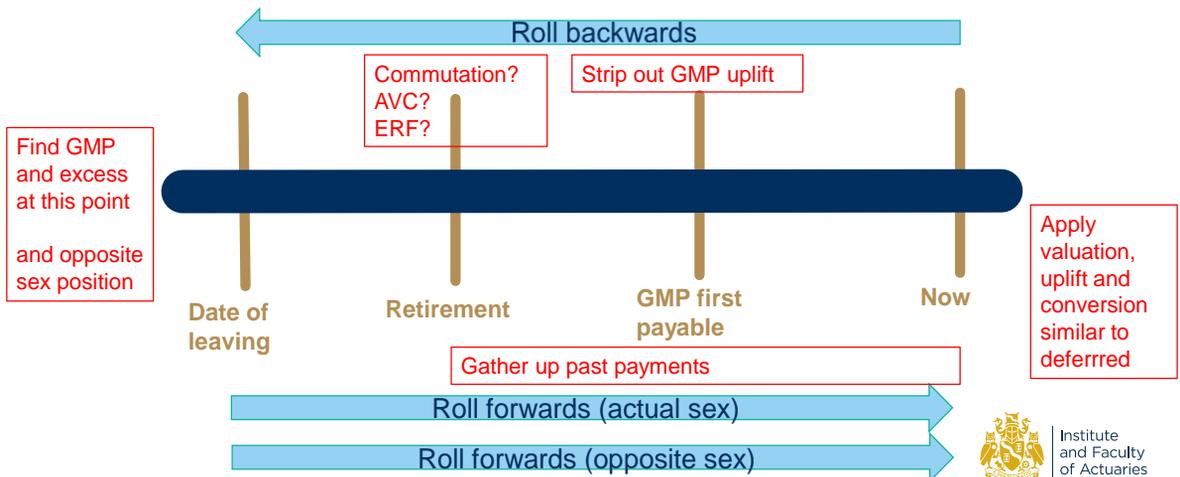
Methodology – Actives

Very similar for deferred pensioners



Methodology – Pensioners

Roll back and roll forwards – for each segment



Data

(the new rock 'n' roll)

“It's fair to say I'm sexually aroused by the collating of data.”



The Guardian

Wednesday 27 February 2013



Model building and processing

Is far from straightforward

- The processing tool will be very complex to build and test
- Considerable professional time will be needed in relation to each scheme.....



Model building and processing

Specimen results – deferred pensioners

% uplift (% of 90-97 benefits)	Number of members	Value of uplift (£)	Average uplift (£)	All members		Total value	Uplift as % of Total value
				Value of 90-97 benefits (Amount A)	Uplift as % of Amount A		
No uplift	101	-	-	3,298,094	0.0%	8,885,641	0.0%
0.00 < x < 1.0	8	3,267	408	789,230	0.4%	2,065,786	0.2%
1.0 ≤ x < 2.0	24	20,020	834	1,258,628	1.6%	3,341,934	0.6%
2.0 ≤ x < 5.0	142	175,755	1,238	5,753,963	3.1%	12,323,989	1.4%
5.0 ≤ x < 10.0	3	3,470	1,157	63,465	5.5%	66,829	5.2%
10.0 ≤ x < 20.0	7	11,881	1,697	67,729	17.5%	609,770	1.9%
20.0 and above	3	9,206	3,069	44,398	20.7%	549,104	1.7%
No 90-97 service	413	-	-	-	n/a	20,062,636	0.0%
Totals	701	223,599	319	11,275,506	2.0%	47,905,688	0.5%



Model building and processing

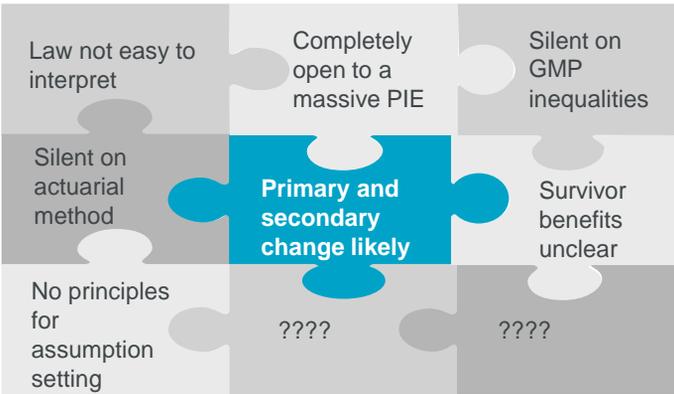
What makes the equalisation uplift higher?



Work outstanding

GMP conversion law difficulties

Has not been tested so unsurprising that there are difficulties



Observations on GMP conversion

Sections 24A-24H of the PSAct 1993 and Regs 69A-69B of SI 1996/1172

Does Condition 1 relate to accrued rights?

- Condition 1; post-conversion benefits must be actuarially at least equivalent to the pre-conversion benefits
- Contrast the following with s67...
- “Benefits provided under the scheme immediately before the conversion date (disregarding money purchase benefits)”



Observations on GMP conversion

Sections 24A-24H of the PSAct 1993 and Regs 69A-69B of SI 1996/1172

How does Condition 1 work for actives?

- Again, contrast with s67
- If future service / salary growth is allowed for, then the anti-franking and revaluation requirements will not have been triggered...

Condition 1 flexibility in actuarial basis

- Again, contrast s67
- Different bases have different impacts, which means sensitivity testing and consultancy, which means cost



Observations on GMP conversion

Sections 24A-24H of the PSAct 1993 and Regs 69A-69B of SI 1996/1172

Condition 1 open-ended!

- Trustees can change their decision on assumptions, perhaps years later

Condition 2 may prevent simplification

- Condition 2 is that a pension in payment must not drop
- Shape of converted benefit is a largely blank canvass, so could end up PIE type approach to prevent reduction
- Different for deferreds – so potential lottery as to effect



Observations on GMP conversion

Sections 24A-24H of the PSAct 1993 and Regs 69A-69B of SI 1996/1172

Condition 4 survivor benefit complexity

- Required on an individual basis, and seems to import the whole widow's, widower's or civil partner's GMP structure

The GMP notification in Condition 5

- Condition 5 means HMRC must be notified on or before the conversion date that the conversion is occurring and which earners are affected
- Via form CA8476 – for each earner whose GMP is converted ... one for every member!



Observations on GMP conversion

Sections 24A-24H of the PSAct 1993 and Regs 69A-69B of SI 1996/1172

Effective date of calcs

- Certificate sent to the trustees no later than three months after the calculations are done
- But what's the effective date the calculations, and how does conversion date fit in?

tPR power to void indefinite

- So the calcs and etc need to be kept for ever



Pensions tax issues

Inevitably there are problems – some quite serious

Adjustments aimed in good faith at addressing GMP inequalities, whether through conversion or dual record keeping:

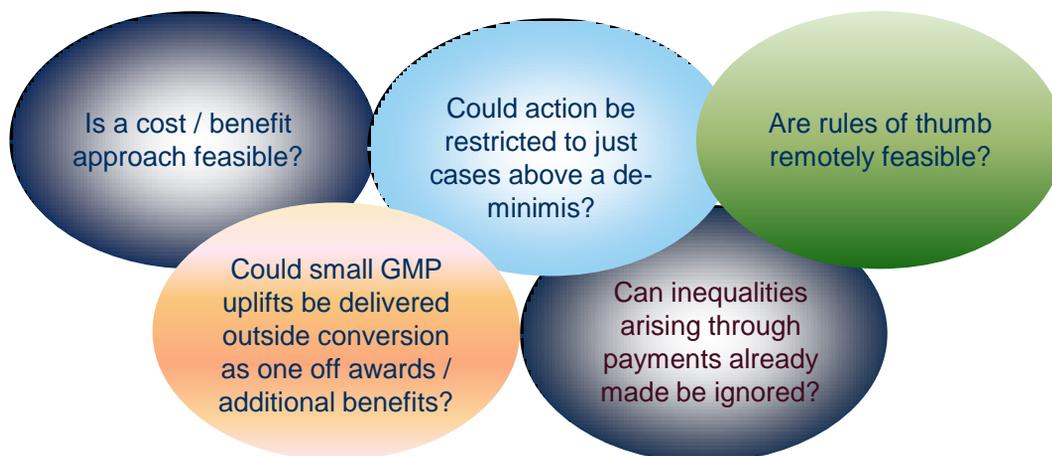
- ✓ **Should not** result in previous LTA testing having to be revisited;
- ✓ **Should be ignored** in assessing how much AA has been or will be used up;
- ✓ **Should not** cause the loss of the “deferred member carve out” in AA calculations;
- ✓ **Should not** cause any pre-existing LTA protections to fail

Measures needed are a combination of

- Changes to pensions tax legislation
- Confirmation from HMRC that it agrees certain principles from existing legislation



Keeping the cost down



What DWP needs to do next

- Reflect on the consultation responses
- Adjust important aspects of GMP conversion law (including primary)
- Work with HMRC to adjust aspects of pension tax law (including primary)
- Explore with the working group whether there are ways in which implementation costs can be kept as low as possible whilst ensuring that members are treated fairly
- Provide guidance to trustees on the issues thrown up by GMP conversion so as to facilitate this “once and done” solution



Go live April 2018?

Coda – the PPF “simplified” equalisation method

(Published Nov 2011, updated Dec 2012, first implemented Q1 2013)

- 186 pages, which covers only the base case
- But worth thinking through, because they used some nice simplifications
 - (although don't be thinking it's actually simple!)



Carve-outs

Not included in the 186 pages

- i. Scheme provides revaluation on the whole pension in deferment in line with inflation;
- ii. Scheme uses a more complex method of calculating early / late retirement pensions;
- iii. Schemes where contracting-out ceased before members left the scheme. Affected schemes may need to include the “later earnings addition” in the anti-franking minimum check;
- iv. Scheme where the revaluation on the excess pension in deferment is greater than the revaluation on the GMP;
- v. Schemes with 3 or more different Normal Pension Ages
- vi. Schemes with a NPA greater than 65; and
- vii. Schemes that provide a separate lump sum based on the member's pension



PPF Pensioners

3 part uplift

- The “inputs” to each part of the process are
 - various dates (birth, leaving, retiring)
 - male and female GMP
 - the comparative rates of revaluation and in payment increase that GMPs or XS pension would have received
 - the early / late retirement uplift that was applied
 - and finally, whether or not it’s a “GMP only” case

In other words, they don’t try to look back to the pension at leaving. This is a huge administrative saving.



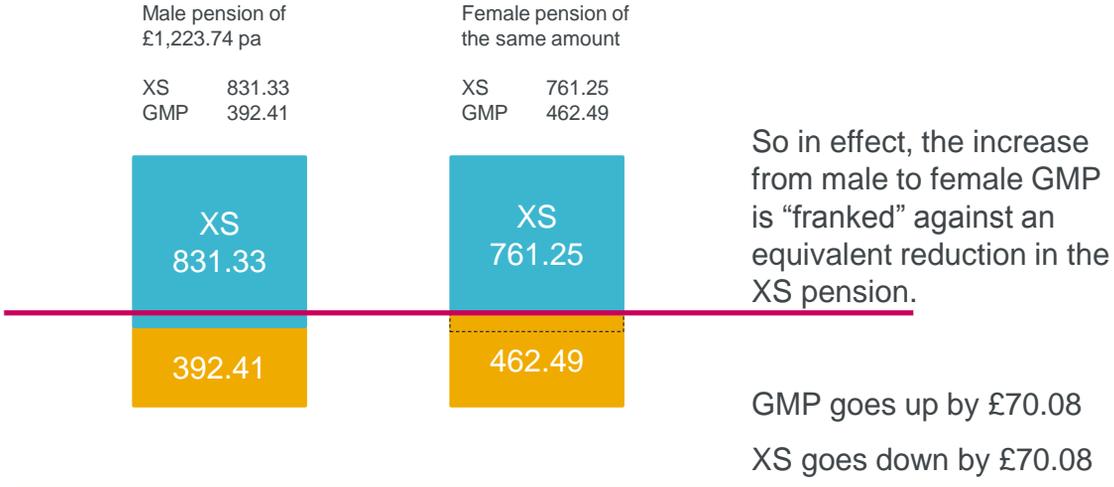
PPF Pensioners

Quid Pro Quo – other simplifying assumptions

- No comparators
- Ignore difficulties over “no benefit accrual after 60”
- It assumes either
 - you’ve got enough XS to cover the fGMP
 - or you’re a GMP only case
 - i.e. there’s no middle ground
 - and errs on generous side, since could be GMP-only by commutation



How the approximation works



Everything above the line is already equal...



PPF Pensioners

Percentage increase applied to pensions

Pension increase	Number of pensioners
0.0%-0.5%	39
0.5%-1.0%	7
1.0%-1.5%	5
1.5%-2.0%	7
2.0%-2.5%	3
2.5%-3.0%	1
3.0%+	22
Average was 2.16% , largest was 13.4%	



PPF Pensioners

Annual increase applied to pensions

Additional pension pa	Number of pensioners
£0-£25	35
£25-£50	9
£50-£75	5
£75-£100	-
£100-£125	3
£125+	32
Average was £146 , largest was £1,239	



PPF Pensioners

Backpayments applied to pensions

Total back payments due	Number of pensioners
£0-£500	57
£500-£1,000	8
£1,000-£1,500	6
£1,500-£2,000	7
£2,000+	6
Average was £540 , largest was £3,521 , median was £57	

Conversion

Summary

Starts with £2,050 pa, with bits vesting at 60 and others at 65, and some revaluing at 7% and some bits getting RPI 5 and some CPI 3

Goes into the actuary factory...

And comes out as a nice smooth – equalised – much bigger – shiny new flat pension from age 65



Conversion

Issues in benefit design

- We now have a smooth (flat?) pension
 - if the XS had say LPI
 - and you convert to flat
 - then how do you answer the question **“why did I lose my increases”**
- Presumably need to protect right to retire at 60 (reduced)
- Do you convert outside the 78-97 window, to achieve real simplicity?
- Impact on asset strategy?



Questions

Comments

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