

## PASA publishes GMP equalisation tax guidance

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### Introduction

The latest addition to PASA's suite of GMP equalisation guidance notes was published yesterday, the highly anticipated [tax guidance](#) ("the Guidance").

### Key points

- The duty to equalise for the effect of GMPs **only applies in respect of GMPs accrued on and from 17 May 1990 up to and including 5 April 1997**, ie from the date of the *Barber* decision to the day before GMPs were abolished (on 6 April 1997).
- The "good practice" Guidance dissects HMRC guidance published to date, providing commentary and practical approaches to dealing with the pensions tax consequences of GMP equalisation.
- Whilst the Guidance was shared with HMRC prior to publication, HMRC did not comment on it.
- Crucially, like HMRC's guidance before it, the Guidance stops short of giving a clear steer on the tax repercussions of GMP conversion. However, separate guidance on conversion is expected to be published before the end of April.
- Whilst noting the most recent instalment of the *Lloyds case* saga (see our [Alert](#)), the Guidance also omits the tax implications of past transfers.

### Background

Following the *Lloyds No. 1 case* back in October 2018 (see our [Alert](#)), PASA set out up a cross-industry working group ("the GMP Equalisation Working Group") with the aim of producing guidance to help schemes equalise for the effect of GMPs in a "cost effective, proportionate and pragmatic way".

HMRC has already produced two separate pieces of guidance on the tax implications of GMP equalisation. The first (published in February 2020) focused on the impact on the AA and LTA of benefit adjustments solely for the purpose of GMP equalisation (see our [Alert](#)), and the second on the payment of past and future lump sums (see our [7 Days](#) dated 20 July 2020). In other words, HMRC's guidance stopped short of looking at some of the trickier areas, such as the pensions tax implications of reshaping benefits as part of a GMP conversion exercise.

## Interaction with HMRC guidance

By way of quick recap, HMRC's guidance to date makes clear that it applies where the "reason for the adjustment is solely for GMP equalisation". The GMP Equalisation Working Group considers "that there is latitude" to extend HMRC guidance to reasonable adjustments (in each case where such adjustments are made solely for GMP equalisation) to:

- address deficiencies in the data (at the member or scheme benefit level)
- operate (comparatively small) simplifications to make calculations practicable, and
- interpret the operation of contracting-out legislation and its interaction with scheme rules.

In the absence of perfect data, trustees will need to exercise judgment, taking advice where appropriate. This means that, even for apparently identical schemes, different trustees could reach different decisions as to how to implement the adjustments.

Leaving open the possibility of trustees adopting a different approach where appropriate, the Guidance also states that HMRC guidance does not "address all possible circumstances" relating to the tax consequences of GMP equalisation and is not intended "to be exhaustive in nature".

## Pensions in deferment

Inequalities can occur during a period of deferment. This can be because the split between GMP and the excess over it is different between men and women (because their GMPs accrued at different rates), and/or different rates of revaluation applied to GMP and the excess under a scheme's rules.

### Annual allowance

HMRC's February 2020 guidance confirmed its position in relation to the annual allowance ("AA"). In brief, provided any adjustment is made for the sole reason of achieving GMP equality:

- where an individual became a deferred member under an arrangement **before 6 April 2006** (when the AA first came into force), and has remained outside of the AA provisions since that date in relation to that arrangement, there is no need to carry out an AA calculation
- if the "[deferred member carve-out](#)" applies to a member, the member should be treated as having no pension input amount for AA purposes, assuming that benefits do not increase above the permissible inflationary amount.

Where an individual does not fall into either of the above categories, HMRC guidance confirms that there is no need to revisit past pension input calculations. However, calculations of the pension input amount in the tax year of implementing GMP equalisation, as well as tax years thereafter, will need to take into account the revised amount of benefit entitlement (in both the opening and closing values).

The Guidance notes that "certain practical questions" arise here. For example, it queries what "in the past" might mean in a scenario in which implementation is delayed. How long can pension input calculations be undertaken without taking into account the adjustment to achieve GMP equality?

### Interaction with tax protections

Appendix 1 of the Guidance looks at how adjustments interact with tax protections during deferment (and in payment; see below). Amongst other things, it notes that there are exceptional circumstances in which fixed

protections could be lost, and recommends taking legal advice where appropriate.

## Pensions in payment

### **Lifetime allowance and benefit crystallisation events (“BCEs”)**

Where equalisation results in an increase to an individual's original pension, trustees should consider the impact on lifetime allowance (“LTA”) calculations and disclosure obligations, as well as the tax treatment of any arrears payments.

A BCE is an event which prompts the testing of a member's benefits against the LTA. HMRC decided that a GMP equalisation adjustment should be treated as an upward adjustment to the individual's original BCE2. As a result, the revised BCE2 should be tested against the individual's LTA as at the date they became entitled to pension. This approach treats the member as having been underpaid up to the point of actual equalisation.

If trustees were to consider treating a correction as a new entitlement, the Guidance suggests taking advice as to the tax consequences. Otherwise, the ramifications will depend on whether, following the GMP equalisation adjustment, the individual exceeds their LTA (either from the outset, or in respect of later BCEs). Trustees should also remember that a change to the original pension could mean that previous BCE3s (which arise in respect of certain increases) did not actually occur.

GMP recalculations in one scheme may have a knock-on effect on a member's available LTA in another. Helpfully, Appendix 2 of the Guidance provides a template communication for trustees to make members aware of the possible need to notify other pension arrangements of changes to their benefits.

### **Retesting members' benefits against the LTA**

Trustees and members are jointly and severally liable for any LTA charge. The Guidance suggests that members can be split into two groups for LTA purposes; those who triggered an LTA charge when taking their benefits and those who did not:

- LTA charge already triggered – it may be possible for the increase in the member's pension and/or their arrears to be used to meet the additional LTA charge. However, because of the different ways in which the two are calculated, the LTA charge could be greater than the actuarial value of the GMP equalisation adjustment. One solution here would be “to reach agreement with the member” to redirect “an appropriate amount” of pension to HMRC to pay the charge. The Guidance sensibly cautions that “this would need to be carefully documented”
- no original LTA charge – where reliable data is not readily available, it may be impractical for trustees to ask each individual to confirm their available LTA. In contrast, it might be disproportionate to assume that a member has simply used up their LTA and to treat them as subject to an LTA charge. Whilst suggesting taking advice, unless there is data to the contrary, the Guidance notes that it would be reasonable and proportionate for trustees to assume that members had sufficient available LTA at the time of the original BCE for the equalised pension to be put into payment. This approach, together with their liability for the LTA charge, should be explained to the member (Appendix 2 contains template wording).

## Tax treatment of arrears payments

As each instalment of pension income is chargeable to tax in the tax year in which the individual became entitled to it, the Guidance includes a template “arrears schedule” for pensioners to send to HMRC, demonstrating the years to which underpayments are attributable (Appendix 3).

With regards to interest, provided it is paid at the same rate as set out in the *Lloyds No. 1* case (simple interest at 1% over base rate), the Guidance concludes that it would qualify as a “scheme administration member payment”. Such a payment would be subject to income tax in the year in which it is eventually paid.

Scheme rules often provide for the forfeiture of unclaimed benefits, for example, six years after an instalment has fallen due for payment. In some cases, a scheme's rules will give trustees a discretion to prevent forfeiture. Where trustees decide to exercise such a discretion, the Guidance suggests the “best interpretation” is that this is “preventing an existing entitlement from being extinguished” (as opposed to creating a new benefit which would affect an individual's AA and LTA calculations).

## Lump sum payments

Two of the payment conditions for lump sums can cause difficulties in relation to GMP equalisation.

### **Extinguishing all rights under the scheme (or arrangement)**

HMRC has previously stated that a “lump sum will not stop being an authorised payment purely because, due to GMP equalisation, further entitlement is later identified that the scheme administrator could not reasonably have known about at the time”. This concession reflects the “exceptional circumstances” associated with GMPs, and applies once “the scheme administrator adopts their chosen GMP equalisation methodology”.

According to the Guidance, trustees can stay within the ambit of HMRC's statement by not definitively selecting a GMP equalisation methodology until the scheme is in a position to implement payments.

### **Lump sum limits**

The payment of authorised lump sums, such as trivial commutation, is subject to monetary limits (a £30,000 limit in this case, across all registered pension schemes). Where applicable limits are exceeded because of GMP equalisation, HMRC's guidance stated that this could result in an unauthorised payment. However, it provided no indication of the action schemes should take in these circumstances.

Depending on the circumstances, the Guidance suggests that it may be reasonable and appropriate (on advice) for trustees to assume that the member was within the relevant limit. But the GMP Equalisation Working Group will give further consideration to lump sum limits.

As regards members with pre-6 April 2006 trivial commutation lump sum payments, in brief, the Guidance concludes that any equalisation top-up would be subject to the authorised payments regime as a new lump sum payment.

## What next?

The GMP Equalisation Working Group intends to publish separate guidance on GMP conversion, including tax considerations, in due course.

Given the complexity and cost of going to Court, coupled with the modest financial gain for most members, the Guidance rightly acknowledges that “many ancillary issues may never be subject to judicial scrutiny” and could “remain unanswered by the Courts”. Trustees and employers should therefore be looking to their professional advisers for help in addressing the gaps.

If you have any questions on any of the above, please speak to your usual Sackers contact.

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