

## PASA's GMP conversion guidance

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### Introduction

The latest addition to PASA's suite of GMP equalisation guidance was published on 9 July 2021, the eagerly awaited [GMP conversion guidance](#) ("the Guidance"). The Guidance "provides examples of how GMP conversion is being used by early adopters", explaining the issues faced, how they were addressed, and how simplification can be achieved in many cases without "a significant impact on members".

### 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).
- Introduced on 6 April 2009 (under the Pensions Act 2007), "conversion" is a legislative facility which allows GMPs to be converted into ordinary DB scheme benefits, following which the GMP rules cease to apply.
- The DWP issued guidance back in April 2019 (see our [Alert](#)) on a 10-stage process for using the conversion legislation to address GMP equalisation. To date, HMRC has not issued any guidance on GMP conversion.
- Recognising that many schemes will wish to go down the GMP conversion route, the Guidance helps to "show how they might do so in a proportionate and pragmatic way". However, PASA is not advocating "a particular course of action".
- Given the complexity of using the conversion legislation, the Guidance warns trustees to seek legal advice in any number of circumstances.

### Background

Following the *Lloyds No.1* case in October 2018 (see our [Alert](#)), PASA set up a cross-industry working group with the aim of producing guidance to help schemes equalise for the effect of GMPs.

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 [7 Days](#) dated 20 July 2020). But HMRC has 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.

## What are the conversion conditions?

To the relief of many, the judge in *Lloyds No.1* confirmed that GMP conversion (referred to as **Method D2**) is a lawful method for dealing with GMP equalisation. Worked examples of how different schemes have dealt with the issues raised by the conversion process, including pensions tax issues and the effect on members, sit at the heart of the Guidance. These primarily focus on a bulk conversion exercise for pensioners and dependants, GMP conversion at retirement, and a bulk conversion exercise for deferred members.

The trustees are very much in the conversion driving seat, although the process itself presents certain challenges in practice because it is not always clear how the conditions summarised below should be met.

### Condition 1

As a minimum, post-conversion benefits must be actuarially equivalent to pre-conversion benefits. Whilst technically determined by the trustees, unsurprisingly actuarial equivalence requires certification by the scheme actuary.

### Condition 2

There must be no reduction to pensions in payment.

### Condition 3

DB benefits must be provided, likely to be an issue only for DC schemes with a GMP underpin.

### Condition 4

A minimum contingent survivor's benefit of "at least half the value of the pension to which the earner would have been entitled" must be provided following conversion (as opposed to 50% of the GMP pre-conversion). As the Guidance notes, the upshot of this condition is that a scheme may not always be able to:

- divert pension to the same degree where there is a financial dependant as well as a legal spouse / civil partner
- apply a reduction to the survivor's pension where the survivor is significantly younger than the member or withhold a pension on a so-called "death bed marriage".

### Condition 5

Certain procedural requirements must also be complied with, including:

- the need for employer consent in advance – this raises questions over what this means where participating employers have changed over the years, and whether the principal employer can consent on behalf of all in a multi-employer scheme. Based on specific legal advice, the latter approach was adopted by one of the example schemes
- trustees consulting members in advance – distinct from the 60-day consultation requirement falling on employers when certain changes (known as "listed changes") are being proposed, there is no minimum consultation timeframe set out in the conversion legislation. Interestingly, two of the example schemes opted for 30-day consultation with only one scheme allowing 60 days
- notifying members and survivors whose benefits have been converted either in advance or as soon as reasonably practicable after the conversion date (according to DWP guidance, "survivors" here

means those with an immediate entitlement to benefits), and

- notifying HMRC – whilst HMRC has stated that it no longer requires this condition be met, as it remains a legal requirement, the Guidance recommends that schemes continue to notify.

## Which schemes / which benefits?

### Which schemes might favour conversion?

The benefits of using GMP conversion to achieve equalisation can include:

- simpler future administration when compared to the year-by-year alternatives (or “dual records” approaches) discussed in *Lloyds No.1* and, as a consequence, a reduced risk of error, and
- the possibility of decreasing costs, or at least not increasing them.

Ultimately, the decision whether or not to go down the GMP conversion route is likely to be quite nuanced and specific to an individual scheme. However, the Guidance notes that some schemes are more likely to find conversion attractive than others, for example:

- those with complex benefits which the trustees are keen to simplify versus those with relatively straightforward ones
- smaller schemes heading to buy-out versus larger ones where the ongoing costs can be spread over a wider membership
- schemes with a significant number of lower earners where GMP rules restrict available options versus those with a large number of high earners (making conversion more complicated from a pensions tax perspective).

### Which benefits?

If the objective of the conversion exercise is solely equalisation, the members included are more likely to be confined to those who accrued a GMP during the relevant period (ie on and from 17 May 1990 up to and including 5 April 1997). For those in scope, the entirety of the GMP needs to be converted.

Where wider objectives are on the table, such as simplification, trustees may be more likely to include everyone with a GMP.

## What might conversion look like?

Under the legislation, trustees have power by resolution to amend their scheme to permit conversion, even if the scheme’s amendment power would restrict this. Alternatively, the trustees may use the scheme’s amendment power, in which case section 67 of PA95 is disapplied. In either case, the trustees may include other amendments which they think are “necessary or desirable as a consequence of, or to facilitate, the GMP conversion”.

What a post-conversion GMP looks like will vary from scheme to scheme, with trustees needing to consider carefully whether they fall within the definition of “necessary and desirable”. Options described in the Guidance range from:

- relabelling and “pseudo GMP” – with all elements of a member’s pension after conversion behaving

in the same way as before. Whilst this would remove the GMP in a strict legal sense, the complications and inequalities would remain making this a less attractive option

- removing GMP complications – for example, restrictions on retirement age and/or converting the benefit into a lump sum at retirement, as well as simplifying pension increases
- more radical reshaping – by reducing the number of different types of pension increases which apply to a member or by switching the index applied to different benefit tranches (eg from RPI to CPI)
- combining with a pension increase exchange exercise (“PIE”) – under which a member consents to giving up some or all of future pension increases in return for an initially higher benefit which either does not increase or only does so at a lower rate.

The Guidance notes that, in practice, schemes equalising using GMP conversion “have tended to take an approach which involves more than relabelling” but not making dramatic changes to pensions indexation.

## What are the pensions tax implications?

In the absence of HMRC guidance, helpfully, the pensions tax implications of GMP conversion are discussed at length. It recommends trustees obtain specialist advice on this topic. Where trustees are unclear as to the tax implications of any aspects of their GMP conversion exercise, they should also consider seeking non-statutory clearance from HMRC.

Particular areas of concern relate to the AA and members with tax protections, with the Guidance noting that these are limiting the way in which GMP conversion is being applied in practice. For example, there is a risk that GMP conversion prior to a member’s pension coming into payment could trigger benefit accrual and so loss of Fixed Protection. Whilst this will not be an issue for most members, “the impact could be very material” for those affected. Examples in the Guidance illustrate ways in which schemes have sought to address these problems by using a “constrained” form of GMP conversion and/or member options.

## What next?

Further PASA guidance is expected on GMP equalisation and historic transfers, anti-franking and communications. Administration Q&As will also be published as regular updates. Other events in the PASA pipeline include a “GMP equalisation week” in the autumn.

A [Private Members' Bill](#) aimed at amending and clarifying the existing conversion legislation has been introduced into Parliament, although we are unlikely to hear more until November and such Bills rarely make it onto the statute books.

If you would like to find out more about the GMP conversion process or have any questions on any of the above, please speak to your usual Sackers contact.

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