



100 days later – GMP equalisation

3 February marked 100 days since the ruling in the Lloyds Bank GMP equalisation case, affecting thousands of UK DB pension schemes and millions of members. Tom Yorath, an expert witness in the Lloyds case, shares his views on how the industry has moved forward since the judgment date following almost 30 years of legal uncertainty

Scheme sponsors

With the financial impact of GMP equalisation directly impacting the profits reported in company accounts, it should come as no surprise that the largest immediate reaction to the judgment was from scheme sponsors.

While many sponsors were aware in advance of the potential for a hit to company profits, the timing of the judgment so close to calendar year ends meant that some were blindsided and were left with both a nasty financial surprise and a mad rush to calculate numbers.

The analysis conducted by Aon on more than 250 schemes suggests that the expected cost for two-thirds of schemes is less than 1 per cent of their overall liabilities and while 1 per cent of liabilities is easily lost in noise on most

company balance sheets, a reduction in profits of 1 per cent of scheme liabilities can be hugely significant and concerning for sponsors.

What's more, the submission of equalisation costs in company accounts is by no means the end of the involvement of sponsors in equalisation.

The judgment from the High Court put much of the power over which method to use in the hands of sponsors. With the overall costs and merits of the various court-approved methods so different, it should not come as a huge surprise that many sponsors are keen to take an active part in this project rather than leaving the work solely to the trustees.

Scheme trustees

Following the judgment, trustees found

a number of burning platforms that needed to be addressed.

However, for the most part, we saw most trustees adopting a 'keep calm and carry on' attitude as far as possible. The majority felt that it was disproportionate to put projects and business as usual on hold indefinitely, preferring pragmatic workarounds, particularly given that equalising GMPs is unlikely to be a quick fix. There are workarounds suitable for member option exercises, risk settlement projects and ill health retirement. Practical solutions regarding the communication around transfer values have been developed. The exceptions have been small pots and trivial commutation, where most have either needed to quickly update their process or put the projects on hold until there is guidance from HMRC that they would

not be unauthorised payments.

Over the past month, trustee attention is now beginning to turn to two main areas:

- Preparation – in particular sourcing and cleaning scheme data, and reviewing and understanding benefit practices.
- Method – in particular whether there is a preference towards converting benefits or running a dual record approach.

While some schemes have excellent historic data, many are finding that significantly more data is needed for the purposes of equalising than to administer the pension scheme. The good news is that this preparation work is not a wasted endeavour and will stand schemes in good stead regardless of which method they choose, as well as making them well-prepared for any future settlement activity.

Although schemes have started the job of preparing and considering their options on solutions, the vast majority are rightly waiting for further guidance – whether that be from industry bodies or subsequent court hearings. Many trustees are concerned that implementing too quickly risks falling on the wrong side of industry norms before they are even formed, with very limited upside.

Members

Despite the case making the front page of a national newspaper, for the most part the response from members has been quite muted. In practice this may be a combination of factors:

- It is hard for members to work out whether they are affected
- The issue is horribly complicated
- The financial impact for many is small

The most member noise has been made in response to those cases where members have had their retirement plans directly impacted by the case; for example, those members who had been expecting or relying on a trivial commutation lump sum and who now face a delay to their payment while the trustees decide how best to adjust their processes for

equalisation. Remember that, despite the name, these trivial commutation lump sums may not be trivial to the recipient.

IFAs

IFAs want to make sure they are giving best advice to members and their biggest concern is that they are making a fair comparison between options. So, typically, they are comfortable advising on a transfer value that has not been adjusted for GMP equalisation, against a benefit that also has not been altered for GMP equalisation, accepting that there may be a top-up payment at some point. This complexity again emphasises the need to have an IFA who really understands DB pensions, and the challenge that members face if they are trying to seek an IFA of their own without trustee or company support.

Insurers

Q4 2018 did not see any slackening in the pace of risk settlement project completion, despite the GMP equalisation issue. Although many schemes are at the early stage of decision making on their GMP equalisation method when considering a transaction, it is worth understanding the insurer view. Insurers have an obvious preference for the standardisation and simplification provided by GMP conversion.

But this does not mean that schemes should hold off from pursuing a buy-in or buyout while addressing GMP equalisation. For schemes looking to reduce risk using buy-ins and buyouts – and at a time when pricing is attractive – being flexible has become important to capture the best pricing. GMP equalisation is another area where flexibility from schemes is likely to increase insurer engagement. It is therefore even more important to ensure you have an experienced adviser who has a clear understanding of the solutions available and who can help you navigate through the current busy market.

Government and industry bodies

There is still a need for further guidance

from the courts, government, TPR and industry bodies. They need to tackle areas questions such as

- Will there be a de-minimus threshold?
- What is the impact on annual and lifetime allowances?
- What about transfers out?
- How will GMP conversion work in practice – for example, is it aiming for minimum interference or maximum administration simplification?
- Will there be best practice codes (similar to the Code of Good Practice in Incentive Exercises)?

To continue to facilitate a competitive administration, market standardisation of the details of implementation will be beneficial and the Pensions Administration Standards Association (PASA) are taking a look at that to bring clarity to the market. Building industry norms will help manage the costs of this complex exercise for the entire industry.

Next steps

There is plenty of work to be done, even before all this guidance is available. You need to analyse gaps in your data, understand your administration practices, and consider interaction with GMP reconciliation projects. In practice, we expect that schemes are still some way off a decision on what GMP equalisation method to use and while schemes may want to quickly address member event processes such as trivial commutations and transfer calculations, for most, full implementation of pensions is likely to be mid-2020 at the earliest.

If you'd like more detail on this please email talktous@aon.com for a copy of our technical summary on the topic.



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