

Pensions law team – May 2019

## DWP preaches conversion but is it a holy route out of GMP inequality?

DWP issues guidance about the use of conversion legislation to address unequal GMPs

Last month the Department for Work and Pensions (**DWP**) issued guidance about how occupational pension schemes could use existing guaranteed minimum pension (**GMP**) conversion legislation to address unequal GMPs.

The conversion legislation is not new but past uncertainty about how to address unequal GMPs meant that there was little incentive to adopt it. However, the spotlight is now back on conversion following last autumn's *Lloyds Banking Group* judgment, which confirmed that schemes must equalise benefits for the effect of GMPs and that one route for achieving this was GMP conversion.

### Background

The *Lloyds Banking Group* judgment made clear that trustees must amend their scheme rules to counter the effects of unequal GMP accrual. The decision went on to consider a number of different methods that could be used to achieve this. One of the methods approved by the court for these purposes was GMP conversion, provided employer consent was obtained.

For further background regarding GMP equalisation and the *Lloyds* decision please see our [briefing](#) on the topic.

### What is GMP conversion?

Equalisation through the GMP conversion method involves an actuary determining the higher actuarial equivalents of unequalised male and female benefits. The higher amount is then used for the purposes of converting GMP benefits into conventional benefits.

### How does the DWP guidance help?

At first glance there are clear benefits to GMP conversion - it involves a one-off process which enables schemes to convert and therefore rid themselves of GMPs once and for all. This may be more appealing than other GMP equalisation methods which may have administratively burdensome consequences such as the need for dual member records and/or annual equalisation exercises. As a result, conversion may lead to a scheme that is simpler to operate and more attractive to an insurer in the context of a buy-out.

However, we may be some way from a stampede toward GMP conversion. Whilst the DWP guidance sets out a helpful tenfold path toward achieving conversion through the existing legislation, it also presents a number of challenging practical issues for any conversion process. The guidance does not provide much in the way of solutions to these issues and indicates that trustees need to address them with their professional advisers.

### Practical challenges

The following are among the practical issues highlighted in the DWP guidance:

- **Active members** - potential difficulties exist with applying the GMP conversion methodology to active members.

- **Past underpayments** – the GMP conversion methodology only deals with the future and does not address any underpayments that may have arisen in relation to pensioners at the point of conversion.
- **Choice of assumptions** – difficulties may emerge in determining which assumptions should be used to value members' benefits before they are converted.
- **Consent of historical employers** – the guidance suggests that legal advice should be taken to ascertain how employer consent (which is a condition of using the statutory conversion route) applies to former employers. Where consent is a requirement, there may be difficulties in obtaining it.
- **Scheme data issues** – where there are deficiencies in scheme data, consideration will need to be given as to how to deal with this.

In addition to the above, the DWP highlights that there may be a number of tax consequences associated with GMP conversion and other GMP equalisation processes. The DWP states that there will be further guidance on this area from HMRC in its pension schemes newsletters "in the coming months".

The DWP also mentions the Government is "considering changes to the GMP conversion legislation to clarify certain issues". It is not clear what these clarifications are or how they will alter the existing legislation - the guidance hints that there may be changes affecting the payment of survivor benefits and the requirement to provide advance notification to HMRC of any conversion process.

## Comment

The guidance will be of interest to all schemes that are presently in GMP purgatory. It provides some cogent reasons to press pause on implementing a conversion approach in the short term, including:

- the likelihood of future clarifications which may simplify the conversion option;
- taking account of future HMRC guidance on the tax consequences of conversion and other equalisation methods, which may make certain options and approaches to resolving GMP inequalities more appealing than others; and
- awaiting publication of guidance from an industry group that was established earlier this year to give guidance on best practice for resolving GMP inequalities.

However, conversion in the short term may be appealing to schemes that are actively pursuing a buy-out. In addition, conversion may also offer a more definitive means of processing transfer requests.

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