



GMP EQUALISATION WORKING GROUP Guidance Note on Tax Issues

Equalising for the Effects of Guaranteed Minimum Pensions

Version 1.0 – February 2021

Contents

Section	Content	Page
1	Introduction	1
1.1	The Lloyds Bank case and unanswered issues	
1.2	GMP Equality	
1.3	HMRC Guidance	
1.4	Focus of this Guidance Note	
	Steps in a project to achieve GMP Equality: Putting the tax issues in context	
2	Scope & applicability of the HMRC Guidance	5
2.1	Scope of the First Newsletter	
2.2	Scope of the Second Newsletter	
2.3	Latitude in application of HMRC Guidance to benefit adjustments: "Where the <u>reason</u> for the adjustment is <u>solely</u> for GMP equalisation"	
2.4	Consideration of certain individuals on a "case by case" basis when applying HMRC Guidance	
3	Reviewing benefits generally	9
3.1	Requirement to review past payments	
3.2	How could GMPs have produced inequalities?	
3.3	Dual record keeping approach	
4	Reviewing periods of deferment	11
4.1	Introduction	
4.2	How do adjustments interact with a member's annual allowance during deferment?	
4.3	How do adjustments interact with tax protections during deferment?	
5	Reviewing periods where benefits are in payment	20
5.1	Introduction	
5.2	How do adjustments interact with a member's lifetime allowance when benefits are in payment?	
5.3	Practical approach for retesting members' benefits against the lifetime allowance	
6	Tax treatment of arrears payments	32
6.1	Obligation to pay arrears	
6.2	Approach to payment of arrears and deduction of tax	
6.3	Payment of interest on arrears and taxation of such a payment	
6.4	Benefits which are subject to forfeiture provisions	
7	Lump sum payments	35
7.1	Second Newsletter	
7.2	Previous lump sum payments	
7.3	Future lump sum payments	
8	GMP conversion	44
8.1	HMRC Guidance	
8.2	This Guidance Note	
8.3	Current activity	
Appendix 1	Tax protections (fixed protection, enhanced protection, primary protection, and individual protections)	
Appendix 2	Template communication to a member regarding the need to consider the tax effects of recalculated benefit crystallisation events	
Appendix 3	Template communication to a member incorporating an arrears schedule (which could be forwarded, by the member, to HMRC)	

Acknowledgments

PASA is grateful to the authors of this Guidance Note (the members of the Tax Issues Sub-Group of the GMP Equalisation Working Group) and to their employers.

Daniel Gerring (Chair)	Travers Smith LLP
Catherine McAllister	Addleshaw Goddard LLP
Chris Widdison	Travers Smith LLP
James Riley	Isio
John Wilson	Spence and Partners
Kathy Cruse	Willis Towers Watson
Mark Riordan	Capita
Rebecca Shevill	AXA
Richard Wyatt	Mercer
Shayala McRae	Lane Clark & Peacock LLP
Wendy Pitcher	Willis Towers Watson

If you want to get involved in future authoring, please get in touch with PASA at info@pasa-uk.com

Disclaimer

This document does not provide legal, tax or actuarial advice. Where appropriate, schemes should take their own professional advice in relation to the issues addressed in this document

Background

The High Court's decision in the Lloyds Bank case:

- requires schemes to equalise benefits earned in the period between 17 May 1990 and 05 April 1997 to correct for the inequalities of GMPs; and
- approved a range of methods which could be adopted to achieve this requirement.

However, given the complexity of the subject, the Lloyds Bank case couldn't deal with all issues which can arise in an equalisation project. In this context, HMRC has published two newsletters providing guidance on the tax issues relating to GMP equalisation.

Purpose of this Guidance Note

Most schemes will want to implement GMP equalisation projects as soon as reasonably practicable. This Guidance Note has been prepared to help them do so in a proportionate and pragmatic way. It highlights tax issues which schemes may encounter in doing so, to enable schemes to make informed decisions and suggests possible approaches for dealing with those issues.

Given the technical nature of certain tax-related issues, this Guidance Note may include more background information and analysis than some of the other guidance produced by the GMP Equalisation Working Group. Nevertheless, it's been assumed readers will have a working knowledge of GMPs and why they can produce unequal benefits between male and female members.

Status of Guidance Note

This Guidance Note isn't a definitive guide to the issues nor is it a substitute for professional advice. In addressing GMP equalisation it's recommended employers and trustees work collaboratively, involving scheme administrators and advisers as appropriate.

This version of the Guidance Note is based on current understanding of the law, official guidance and industry practice as at January 2021. This version of the Guidance Note doesn't address in any detail the tax implications for schemes choosing to use the conversion method (but see Section 8 of this Guidance Note). Nor does it address past transfers. It's intended to update this Guidance Note to reflect changes to the law, guidance (including guidance published by HMRC) and practice.

Other guidance published by the GMP Equalisation Working Group

This Guidance Note is focused solely on tax considerations which may arise in GMP equalisation projects. The GMP Equalisation Working Group has published other guidance on the topic of GMP equalisation:

- [In September 2019, we published a separate guidance note outlining methods which schemes could use to correct for the inequalities of GMPs.](#)
- [In March 2020, we published 'When to Rectify', providing guidance on the timing of GMP rectification and equalisation exercises.](#)
- [In July 2020, we published a separate guidance note on data considerations in the context of correcting for the inequalities of GMPs.](#)
- [In August 2020, we published a separate guidance note on communications, for schemes in the early planning stages of GMP equalisation.](#)

All of the GMP Equalisation Working Group's guidance notes, together with the Call to Action, are available online at www.pasa-uk.com.

1. Introduction

1.1 The Lloyds Bank case and unanswered issues

Since the Lloyds Bank judgment¹ was issued in October 2018 schemes which were contracted out have known they need to equalise benefits for the effects of GMPs. Whilst the judgment approved some methods for schemes to achieve equality, a number of ancillary issues arising in implementing an equalisation project remain unresolved.

Certain issues may be resolved as case law develops. For example, in the Lloyds Bank case, the High Court has issued a further judgment addressing the treatment of past transfers. However, the complexity and cost of going to court, coupled with the modest financial impact for most members of equalising benefits for the effects of GMPs, means many ancillary issues may never be subject to judicial scrutiny and therefore could remain unanswered by the Courts.

1.2 GMP Equality

The aim of a GMP equalisation project is to make sure a member with a GMP relating to contracted out pensionable service during the period 17 May 1990 to 05 April 1997² receives benefits which aren't less than those which would have been provided had the member been of the opposite sex during this period. In this Guidance Note, this is referred to as achieving 'GMP Equality'.

Whilst achieving GMP Equality sounds simple, there are, in practice, tax complexities caused by the fact benefits in respect of the period 17 May 1990 to -05 April 1997 should have been different from the benefits which have been administered to date. For example:

- the starting pension may have been greater than previously thought; and
- increases in payment may have been different than previously thought

These effects can change the amount of pension which was payable in any year and may have tax implications.

There may also be questions as to whether revaluation in deferment may have exceeded what is permitted under the deferred member carve out (see **4.2(c)** below³) and/or whether lifetime allowance protections could, in rare circumstances, be lost (see **Appendix 1**).

¹ *Lloyds Banking Group Pensions Trustees Limited v Lloyds Bank Plc* [2018] EWHC 2839 (Ch) (26 October 2018), <https://www.bailii.org/ew/cases/EWHC/Ch/2018/2839.html>. Following a second hearing on matters consequential to the earlier judgment, a further judgment was issued: *Lloyds Banking Group Pensions Trustees Limited v Lloyds Bank Plc* [2018] EWHC 3343 (Ch) (06 December 2018), <https://www.bailii.org/ew/cases/EWHC/Ch/2018/3343.html>

² It's possible certain GMP equalisation exercises will address a period which extends prior to 17 May 1990, but the requirement set out in the Lloyds Bank case related to the period of contracted out pensionable service between 17 May 1990 and 05 April 1997.

³ The key message is members who would otherwise benefit from the deferred member carve out in respect of a pension input period, and are therefore treated as having a nil pension input amount, won't lose the deferred member carve out as a result of adjustments to achieve GMP Equality, but further information is provided in **4.2(c)** below. With regard to GMP conversion, see **8** below.

It's recognised schemes may feel a sense of frustration at having to incur additional administration and adviser costs to make what will be, for most members, relatively modest changes to the value of benefits. The prime aim of the GMP Equalisation Working Group is to help schemes achieve GMP Equality in a cost efficient and pragmatic way.

1.3 HMRC Guidance

HMRC has published two GMP equalisation newsletters:

- the first was published on 20 February 2020⁴ (First Newsletter)
- the second was published on 16 July 2020⁵ (Second Newsletter)

The First Newsletter and Second Newsletter are together referred to in this Guidance Note as the "HMRC Guidance".

The scope and applicability of the HMRC Guidance is considered in **Section 2** below.

1.4 Focus of this Guidance Note

For clarity, this Guidance Note is based on HMRC Guidance and our understanding of HMRC's current view on the interpretation of the legislation governing taxation issues associated with the equalisation of GMPs. Whilst this Guidance Note has been shared with HMRC prior to publication, HMRC hasn't commented on this document.

The authors don't intend this Guidance Note to be interpreted as an endorsement of HMRC's approach or in a way suggesting other approaches aren't legitimate in appropriate circumstances.

⁴ <https://www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020>

⁵ <https://www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-july-2020/guaranteed-minimum-pension-gmp-equalisation-newsletter-july-2020>

Steps in a project to achieve GMP Equality: Putting the tax issues in context

For most schemes, a project to achieve GMP Equality will include the following steps:

(a) Project initiation

Planning an overall approach to achieving GMP Equality

This includes determining, with appropriate advice, the potential methods to be used to correct past underpayments (which will inform the data required (see the GMP Equalisation Working Group's separate Guidance on Data) and benefit audit process). See the GMP Equalisation Working Group's separate Guidance Note on Methods, which outlines methods schemes could use to correct for the inequalities of GMPs.

Trustees may wish to consider illustrative, scheme-specific examples of the impact on members (including potential tax issues), the impact on scheme liabilities and administration costs.

More than one method can be used by a scheme, either concurrently or consecutively (provided different treatment can be objectively justified).

An 'in principle' decision on preferred method(s) should be reached early in the project as it can impact the steps which follow (noting the method to be used could change in time — for example, initial adoption of a dual record methodology, followed later by GMP conversion).

(b) Data and benefit audit

Understanding the data available and the data required for the project

For further information on this fundamental step, see the GMP Equalisation Working Group's Guidance on Data published in July 2020.

Trustees and sponsors will also need to check administration systems, whether in-house or outsourced, have the necessary functionality for an equalisation project, such as the ability to hold dual or even multiple records for the same members, and the ability to carry out retrospective testing of members benefits against the lifetime allowance.

(c) Rectification following GMP reconciliation (GMP rectification)

Will GMP rectification take place prior to the project to achieve GMP Equality or will implementation of the two projects be combined?

GMP equalisation can't be implemented until schemes know what the GMP is. Therefore, a GMP reconciliation process must be completed to identify any changes required to GMPs. However, whether or not changes identified during GMP reconciliation are implemented prior to a GMP equalisation exercise is a scheme-specific decision. For relevant considerations in this regard, see the GMP Equalisation Working Group's Guidance Note on 'When to Rectify'.

Where trustees intend to delay implementing GMP rectification, they should check if continuing to pay benefits at incorrect levels for an extended period of time won't lead to any adverse tax consequences (e.g. as a result of payments no longer being "authorised payments"⁶).

(d) Achieving GMP Equality

Finalising and implementing the plan

Advice will be required as to the possible approaches to populations and equalisation calculations for both past and future benefit payments.

Considerations include interest on underpayments; limitation periods in scheme rules; methodologies, including benefit conversion; consultation and communication; and, of course, tax issues, which are explored in detail in this guidance.

(e) Member communications and record-keeping

Communicating the outcome and preparing for business as usual

This administrative step will include informing members of changes to their benefits, trustee decisions on underpayments and, in connection with GMP rectification, overpayments of benefits. It may also include updating records, implementing new record-keeping processes, reporting to HMRC, managing member queries and revising scheme tools for specific calculations. Before any payments are made, schemes need to understand the tax implications.

⁶ Consider whether continued payment of pensions which are being overpaid would be authorised (see Registered Pension Schemes (Authorised Payments) Regulations 2009)

2. Scope and applicability of the HMRC Guidance

2.1 Scope of the First Newsletter

(a) The First Newsletter states:

"In this newsletter we are giving guidance to supplement the existing guidance in the Pensions Tax Manual relating to benefit adjustments for registered pension schemes with periods of contracted out pensionable service between 17 May 1990 and 5 April 1997." (Section 1)

Note: This appears to indicate the HMRC Guidance doesn't cover benefit adjustments in relation to periods of pensionable service prior to 17 May 1990 (even those aimed at correcting for the inequalities of GMPs)⁷. If benefits accrued prior to 17 May 1990 are equalised, this would be an augmentation of benefits since there's no legal requirement to equalise such benefits. As this would be an augmentation at the time equalisation is implemented, the tax implications would be quite different from those discussed in this Guidance Note.

(b) The First Newsletter states:

"This guidance relates to benefit adjustments where the reason for the adjustment is solely for GMP equalisation and does not cover other benefit adjustments, if any, which occur at the same time." (Section 1)

Note: The phrase "where the **reason** for the adjustment is **solely** for GMP equalisation" is considered in 2.3 below.

As a general point, we understand adjustments to achieve GMP Equality aren't the only benefit corrections schemes will make, and we appreciate schemes may wish to adopt a consistent approach to taxation of corrective adjustments. However, there are certain features⁸ of an exercise to achieve GMP Equality which could differentiate it from other benefit correction exercises (and it would therefore not necessarily be inappropriate for schemes to adopt an approach to GMP equalisation which differs from other benefit correction exercises).

(c) The First Newsletter also states:

"The guidance in this newsletter relates to those equalisation methods whereby a dual record keeping approach is used but does not apply where a conversion method is applied." (Section 1)

Comment: The First Newsletter therefore can be taken to apply irrespective of whatever dual record keeping approach is used (i.e. it's not limited in its application to Method C2).

(d) With regard to the scope of the First Newsletter, it's stated:

⁷ We appreciate the requirement set out in the Lloyds Bank case related to the period of contracted out pensionable service between 17 May 1990 and 05 April 1997. However, it's possible certain GMP equalisation exercises will address a period which extends prior to 17 May 1990 and the tax considerations for such exercises may be different.

⁸ For example, where a dual record keeping approach is used, an uplift may be required for certain years but not others (which may not be the case for other benefit corrections).

"This guidance covers pension tax issues such as:

- *annual allowance, including deferred member carve-out*
- *lifetime allowance, including fixed, primary, individual and enhanced protection" (Section 1)*

Comment: The First Newsletter addresses these issues at a high level and there are certain tax issues which aren't referred to in the HMRC Guidance.

(e) HMRC states:

"We know this is a complex area and some individuals may also need to be considered on a case by case basis depending on their circumstances". (Section 1)

Note: The potential requirement to consider some individuals on a case by case basis is considered in **2.4** below.

(f) The First Newsletter expressly doesn't cover the treatment of lump sum payments (which are covered in the Second Newsletter) and, in relation to GMP conversion, states:

"... there may be consequences for some members if this method is applied. For example, converted benefits through a higher revaluation or higher rates of pension in the year of conversion, and in subsequent years beyond conversion, which may result in either the loss of deferred members carve-out or fixed protection, or both." (Section 1)

Note: With regard to GMP conversion, see **Section 8** below.

2.2 Scope of the Second Newsletter

(a) The Second Newsletter states:

"This guidance relates to adjustments where the reason for the adjustment is solely for GMP equalisation. It does not cover other benefit adjustments, if any, which occur at the same time or as a result of GMP conversion." (See the section headed 'Introduction')

Note: The phrase "*where the reason for the adjustment is solely for GMP equalisation*" is considered in **2.3** below.

(b) With regard to the scope of the Second Newsletter, it's stated:

"If pension schemes have started to pay pensions and made lump sum payments, further payments may be due if schemes find that benefits have been underpaid due to GMP equalisation. This guidance covers tax issues in respect of lump sums previously paid and the payment of lump sums as a result of GMP equalisation." (See the section headed 'Introduction')

Comment: In other words, the Second Newsletter covers both previous lump sum payments and future lump sum payments. The types of lump sums covered include:

- defined benefit lump sum death benefit (DBLSDB)
- pension commencement lump sum (PCLS)
- serious ill health lump sum (SILS)
- small lump sum under Regulations 11 or 12 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (small lump sum)
- trivial commutation lump sum (TCLS)
- trivial commutation lump sum death benefit (TCLSDB)
- winding-up lump sum (WULS)
- winding-up lump sum death benefit (WULSDB)

Note: For further consideration of lump sum payments, see **Section 7** below.

(c) As with the First Newsletter, the Second Newsletter expressly doesn't apply to GMP conversion and goes further, stating:

"The position regarding conversion is complex and its effects within the pension tax rules may have wider impacts. For example, there may be implications when testing against the annual allowance, or whether the deferred member carve out applies, or where an individual has a lifetime allowance protection.

HMRC is unable to provide supplemental guidance on conversion, as more detailed work needs to be done on the wider issues associated with that methodology. Any schemes wishing to use the conversion method should consider any tax implications that may arise in accordance with the existing legislation and guidance within the PTM and seek advice as appropriate."

Note: With regard to GMP conversion, see **Section 8** below.

2.3 Latitude in application of HMRC Guidance to benefit adjustments: "Where the reason for the adjustment is solely for GMP equalisation"

As noted above, the First Newsletter and the Second Newsletter both state they apply where the "reason for the adjustment is solely for GMP equalisation".

Key message

The GMP Equalisation Working Group considers that there is latitude to apply the HMRC Guidance to reasonable adjustments 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 each case where such adjustments are made solely for GMP equalisation.

Example

For all or part of the period from 17 May 1990 to 05 April 1997, the scheme may not hold the data required in order to implement GMP equalisation (for example historical salary data). Therefore, in order to implement GMP equalisation, the scheme would need to make certain assumptions.

Even though the adjustments made based on those assumptions may vary slightly from those which would have been made if the trustee had access to full data, the 'reason' for these adjustments is solely for GMP equalisation, and therefore the HMRC Guidance would apply.

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.

2.4 Consideration of certain individuals on a "case by case" basis when applying HMRC Guidance

(a) As noted in 2.1(e) above, the First Newsletter flagged some individuals "*may also need to be considered on a case by case basis depending on their circumstances*".

(b) The above statement:

- suggests caution (and professional advice) may be required when dealing with complex circumstances in which the HMRC Guidance might not apply;
- leaves open the possibility of trustees adopting a different approach to that set out in the HMRC Guidance where trustees reasonably think this is appropriate in the circumstances; and
- indicates the HMRC Guidance doesn't address all possible circumstances and isn't intended to be exhaustive in nature

3. Reviewing benefits generally

3.1 Requirement to review past payments

Key message

It's now clear schemes need to make corrective adjustments to achieve GMP Equality in respect of benefits earned on and from 17 May 1990 — the date of the judgment of the European Court of Justice in the Barber⁹ case — and that this has been a requirement since 17 May 1990.

Past payments in respect of any benefits attributable to contracted out pensionable service between 17 May 1990 and 05 April 1997 will need to be reviewed and underpayments corrected as necessary.

Prior to the Lloyds Bank judgment very few schemes adjusted benefits to achieve GMP Equality. This was mainly because, until the judgment, schemes weren't certain whether GMP Equality was required and, if it was, how it should be achieved. Schemes winding up would sometimes make adjustments to address GMP inequalities, although much would depend on the funding position and status of the sponsor.

3.2 How could GMPs have produced inequalities?

- (a) The extent to which GMPs produce unequal pension benefits depends on a number of factors, including the specific benefit design of the scheme and the individual circumstances of each member:

Example

Scenario A: A scheme's rules provide for the same rate of increases to pensions in payment for each element of the pension (both GMP and pension in excess of GMP)

If the member left pensionable service prior to retirement (resulting in a period of deferment before the member's pension came into payment), the way in which GMP is accrued and revalued¹⁰ is likely to mean that inequalities emerge prior to age 65 (ultimately resulting in different starting pensions for male and female members), even in a scheme which applies the same rate of increase to the whole pension once in payment.

For a member retiring from pensionable service at age 60, there may not be any inequality prior to a member reaching age 65 (i.e. male GMP age).

Scenario B: A scheme's rules provide for a different rate of increases to be applied to GMP and pension in excess of GMP, once the pension is in payment

Even for a member retiring from pensionable service at age 60, there may be inequality prior to the member reaching age 65.

⁹ Barber v Guardian Royal Exchange Assurance Group (C-262/88) [1991] 1 QB 344

¹⁰ This Guidance Note doesn't address anti-franking considerations (broadly, considerations relating to the statutory provisions disallowing the offsetting of GMP revaluation against pension in excess of GMP). The GMP Equalisation Working Group's guidance notes on data considerations and methodology do address antifranking.

- (b) When establishing whether any corrective adjustments are required (including in relation to past payments), it will be necessary to consider any period of deferment (see **Section 4**) and any period during which benefits are in payment (see **Section 5**).

3.3 Dual record keeping approach

Key message

The review of past payments requires a dual record keeping (also known as a 'year-on-year') approach to be adopted¹¹ for equalisation.

If a member's comparator¹² would have received a higher benefit¹³, then a correction payment, with interest, will be due (i.e. an arrears payment in respect of past underpaid instalments).

To maintain GMP Equality, the dual record keeping approach would then be used when determining future instalments of pension (unless and until GMP conversion is implemented).

¹¹ It's not possible to equalise past underpayments using the statutory GMP conversion legislation.

¹² i.e. a member of the opposite sex with (among other things) the same date of birth, joining/leaving dates and earnings history.

¹³ In the case of Method C, taking into account the accumulated pension paid to date.

4. Reviewing periods of deferment

4.1 Introduction

(a) Why do inequalities emerge during a period of deferment?

Key message

Inequalities can occur during deferment because:

- the split between GMP and excess is different between men and women (because men and women accrued GMP at different rates); and
- the rate of revaluation applied under the scheme's rules may be different for GMPs and excess

(i) This means, where there's been a period of deferment:

- in the absence of appropriate action, the starting pensions for male and female members may differ because of the different revaluation in deferment; and
- implementing GMP Equality will therefore mean uplifting the starting pension for the disadvantaged sex, effectively by way of adjusting the revaluation which applied over the deferment period.

(ii) In many cases, revaluation calculations will only be undertaken when the member's benefits are to be put into payment. Legislation and/or the scheme rules may provide for calculations of cumulative revaluation by reference to key dates such as the member's retirement date, or the date upon which the member achieves Normal Pension Age or GMP age (i.e. 60 for women and 65 for men).

(b) Does the equalisation methodology selected by the scheme affect how benefits are adjusted for periods of deferment?

Methods B and C (two of the dual record keeping approaches referred to in the Lloyds Bank judgment) are the same in respect of periods of deferment. The change to the starting pension will therefore be the same regardless of which of those methods is used.

(c) Does implementing GMP Equality have implications for annual allowance purposes?

Key message

Yes, there are implications for annual allowance.

The First Newsletter states the GMP equalisation benefit adjustments should simply reflect the benefit the member had already accrued. However, this accrued benefit may not have been taken into account in previous calculations of pension input amounts.

In other words, from April 2006 onwards (i.e. from the first tax year in which the annual allowance regime applied) the annual allowance calculations for each year of deferment (to the extent that such a calculation was necessary) may not have been properly calculated.

However:

- this is only relevant where the deferred member carve-out doesn't apply (see **4.2(c)** below); and
- HMRC considers there's no need to revisit pension input amount calculations done in the past, for changes made to implement GMP equalisation (see **4.2(d)** below).

4.2 How do adjustments for GMP Equality interact with a member's annual allowance during deferment?

(a) How is the annual allowance tested during deferment?

Key message

Broadly, the calculation of a pension input amount in a pension input period under a defined benefits arrangement requires a comparison of the "opening value" and "closing value" of the member's benefits, both being notional 'capital' values¹⁴ (with an adjustment to the opening value in line with CPI).

If the pension input amount exceeds the member's annual allowance, a tax charge may be payable. Therefore, there's a question as to how changes to implement GMP equalisation affect these calculations.

However:

- many deferred pensioners will have become a deferred member before 06 April 2006 (i.e. before the annual allowance provisions were introduced) and will have remained outside the annual allowance provisions since that date (see **(b)** below); and
- many other deferred members will benefit from the 'deferred member carve-out' (see **(c)** below).

Even where an individual doesn't fall into one of these two categories, the HMRC Guidance includes a helpful easement regarding pension input calculations undertaken in the past (see **(d)** below).

¹⁴ Equal to 16 times the amount of pension

(i) Broadly:

- for an annual allowance calculation in the pension input period of retirement, the closing value reflects the pension put into payment (as if the member hadn't commuted any pension for a lump sum);
- in earlier pension input periods, annual allowance calculations involve assigning an element of the overall revaluation artificially between tax years, by notionally calculating the revaluation due at any particular date as if the date were the member's Normal Pension Date (these calculations will also affect the opening value for the pension input period of retirement);
- the requirement for the actual retirement pension to be equal changes the calculation of the notional revaluation (and means from April 2006 onwards the annual allowance calculations for each year of deferment may not have been properly calculated (where such a calculation is necessary, i.e. where an individual doesn't fall into one of the two categories set out in the bullet points in the key message above)

(ii) Where a pension input amount does have to be calculated, an adjustment for GMP Equality may change the opening and closing values and therefore impact the pension input amount for each tax year (resulting in a greater or smaller pension input amount than if no adjustment had been made). However, the HMRC Guidance includes a helpful easement regarding pension input calculations undertaken in the past (see (d) below).

(b) Members who became deferred members before 6 April 2006

(i) Section 3.1 of the First Newsletter states:

"An individual who became a deferred member before 6 April 2006 under an arrangement, and who has remained outside the annual allowance provisions since that date in relation to that arrangement, should still remain outside of those provisions for that arrangement."

Key message

Adjustments for the sole reason of achieving GMP Equality should have no impact for annual allowance purposes on a member who became a deferred member under an arrangement before 6 April 2006 and has remained a deferred member under that arrangement¹⁵ since that date. Therefore, there is no need to carry out annual allowance calculations for such members.

(ii) HMRC's Pensions Tax Manual states (at PTM053910¹⁶):

"The annual allowance provisions do not apply to an arrangement where the member became a deferred member (as defined for the purpose of the tax rules) under that arrangement prior to 6 April 2006, and has remained so from then on."

¹⁵ Additional consideration will be required where, for example, the member has transferred to the relevant arrangement from a different arrangement as a deferred member (e.g. as part of a bulk transfer exercise) on or after 6 April 2006 (see (iv) below).

¹⁶ For more detail, please see PTM053910, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm053910>

(iii) PTM053910 goes on to say the following don't constitute benefits beginning to accrue for these purposes:

- *"Where there is a change to the rate at which benefits are revalued in the deferred period, for example moving to a rate that includes as part of its mechanism an index based on RPI from an index based on CPI (so long as, where relevant, the change is not linked to continuing employment)"; or*
- *"The member exercising on or after 6 April 2006 a retirement option granted (by letter or in the scheme rules) before 6 April 2006."*

(iv) Impact of a transfer of deferred benefits

Broadly:

- PTM053910 considers the scenario in which a deferred member's benefits are transferred, by way of a recognised transfer, so the same benefit rights are held under a different pension scheme in replacement of the benefit rights that had been held under the transferring pension scheme
- HMRC states the grant of the replacement rights *"would be an accrual of benefits to or in respect of the individual, even though there is no increase in benefit rights between those given up in the transferring scheme and those granted in the receiving scheme"*
- However, PTM053910 states where *"but for the grant of the replacement benefit rights as a result of the transfer, the individual would otherwise qualify as deferred member in relation to the benefits rights under the receiving scheme arrangement"*, the individual can remain a deferred member
- PTM053910 states, with effect from 28 January 2015, in the case of a block transfer, the test for whether an individual is a deferred member but for the grant of the replacement benefit rights as a result of the transfer is conditional on *"the increase in value of the benefits in the receiving arrangement in relation to the transfer" being "equal (or virtually equal to) the decrease in value of the benefits in the transferring arrangement"*

(v) Impact of an adjustment to achieve GMP Equality

An adjustment to achieve GMP Equality shouldn't count as accrual for the purposes of treating such a member as having accrued benefits after 6 April 2006; the benefits were accrued between 17 May 1990 and 5 April 1997. A correction is simply being made now to reflect the correct entitlement accrued during this period. This is confirmed in Section 3.1 of the First Newsletter which states that the GMP equalisation benefit adjustments *"should simply reflect the benefit the member had accrued before 6 April 2006"*.

(c) Deferred member carve-out (DMCO)

(i) Section 3.2 of the First Newsletter states:

"An individual who is otherwise within the annual allowance deferred member carve out (DMCO) in relation to an arrangement should remain within the DMCO for that arrangement. GMP equalisation benefit adjustments are a series of percentage increases that are attributable solely to the application of section 67 of the Equality Act 2010 and so within the relevant statutory increase percentage aspect of the annual allowance DMCO. This is the case regardless of whether a sex equality rule has been incorporated into the rules of the pension scheme under which the arrangement is held."

Key message

Members who would otherwise benefit from the DMCO in respect of a pension input period, and are therefore treated as having a nil pension input amount, will not lose the DMCO as a result of adjustments to achieve GMP Equality.

Comment: This won't apply if the equalisation exercise goes beyond what is legally required (e.g. if a scheme chose to equalise benefits attributable to service prior to 17 May 1990).

- (ii) PTM053910¹⁷ provides that a person who's a deferred member for the whole of the pension input period is treated as having no pension input amount provided any increase in relevant rights under the arrangement isn't more than:
- the "relevant percentage"; plus
 - the "relevant statutory increase percentage"

(in this guidance note the aggregate is referred to as the "permitted percentage").

Note: A member's relevant rights for this purpose exclude GMP.

- (iii) The test to identify whether a member benefits from the annual allowance DMCO in respect of an arrangement is a two-part test:
- is the member a "deferred member" in relation to the arrangement for the purposes of tax legislation (see (iv) below); and, if so,
 - have the member's "relevant rights" increased during a pension input period by more than the "permitted percentage" (see (v) below)
- (iv) Is the member a deferred member for the purposes of tax legislation?
- A person is a deferred member for these purposes if they're not an active member or a pensioner. A person is an active member if there are "currently arrangements made under the pension scheme for the accrual of benefits to or in respect of the person".

¹⁷ For more detail, please see PTM053910, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm053910>

The following aren't "deferred members" for these purposes:

- members who aren't accruing pensionable service but who have retained a salary to link to their past service benefits
- members who have continued to benefit from life assurance under the scheme, unless the life assurance is in a separate "arrangement" (we would expect life assurance to be regarded as in a separate arrangement in most schemes, so remaining entitlement to life assurance should not normally be a problem); and
- members who have continued to benefit from ill health cover (with a contingent right to unreduced accrued benefits or possibly even additional pensionable service in the event of ill health early retirement) under the scheme, unless the benefit is in a separate "arrangement" (again, we would expect these benefits to be regarded as in a separate arrangement in most schemes, so remaining entitled to enhanced early payment of benefits should not normally be a problem).

The implementation of an adjustment solely for the "reason" of GMP Equality doesn't constitute accrual of benefits. Therefore, a member who would otherwise benefit from the DMCO for annual allowance purposes will not lose the DMCO for annual allowance purposes as a result of adjustments for the reason of achieving GMP Equality.

- (v) Have non-GMP benefits increased during a pension input period by more than the "permitted percentage"

As noted above, a person who is a deferred member for the whole of a pension input period is treated as having no pension input amount provided any increase in relevant rights under the arrangement doesn't exceed the permitted percentage.

As noted above, the "permitted percentage" is:

- the "relevant percentage"; plus
- the "relevant statutory increase percentage"

The "relevant percentage" is the amount required under the rules of the scheme provided:

- where it's an 'RPI based' increase, it was in the rules on 6 April 2012; or
- otherwise, where it was in the rules on 14 October 2010; or
- if the rules don't specify the "relevant percentage", it's the increase in CPI over a 12-month period ending with a month which falls within the pension input period (the month having been chosen by the scheme administrator).

The "relevant statutory increase percentage" is the part (which may be all) of the percentage increase in a member's rights under an arrangement which occurs during the pension input period which is

attributable solely to certain statutory provisions. One of those statutory provisions is Section 67 of the Equality Act 2010.

Therefore, an adjustment implementing GMP equalisation (i.e. attributable solely to the application of Section 67 of the Equality Act 2010) can't exceed the permitted percentage, because it forms part of the relevant statutory increase percentage and therefore is part of the permitted percentage.

Therefore, again, a member who would otherwise benefit from the DMCO for annual allowance purposes won't lose the DMCO for annual allowance purposes as a result of increases for the reason of achieving GMP Equality (again, provided the increases are restricted to those legally required).

(d) What happens in a pension input period in which the member is covered by neither the DMCO nor the exemption above relating to pre-06 April 2006 leavers?

(i) In **(b)** and **(c)** above we've addressed two scenarios in which a member's pension input amount for a specific pension input period would, in the absence of a GMP Equality Adjustment, ordinarily be treated as being zero. One scenario is where a member became a deferred member under an arrangement before 06 April 2006 and has remained a deferred member under the arrangement since this date; and the second scenario is where the member benefits from the DMCO. We've noted the HMRC Guidance confirms, in such scenarios, an increase for the reason of achieving GMP Equality covered by the HMRC Guidance (i.e. using a dual record keeping approach) would still result in a pension input amount being treated as zero. But what about pension input periods for which neither of these scenarios apply? There are two points to consider in this regard, namely past pension input periods and future pension input periods.

(ii) Section 3.3 of the First Newsletter states:

"HMRC considers that there is no need to revisit pension input amount calculations done in the past, for changes to implement GMP equalisation. Calculations for the pension input amount in the tax year of implementing GMP equalisation and tax years thereafter will need to take into account the revised amount of the benefit entitlement in both the opening and closing benefit calculations."

Key message

This appears to be an easement being granted by HMRC. For the reasons set out below, pension input amount calculations undertaken in the past could be wrong (and it is possible that pension input amounts should have been higher or lower). However, HMRC considers that there is no need to revisit these calculations.

(iii) In the absence of such an easement, there may have been a requirement to revisit the pension input amount calculations for pension input periods during deferment where a member was not covered by either the DMCO or the exemption relating to pre-06 April 2006 leavers described in **(b)** above.

Examples of pension input periods during deferment where a member's pension input amount was not covered either by the exemption relating to pre-April 2006 leavers or the DMCO

In respect of members who left pensionable service on or after 06 April 2006

This could include certain pension input periods where the DMCO did not apply perhaps because:

- the rules relating to revaluation in the relevant scheme:
 - have changed since 14 October 2010 (or, where the previous rules set out an 'RPI based' increase, since 06 April 2012)¹⁸; or
 - include a discretionary element¹⁹; or
- (arguably) the pension input period in which the member exercised an option that resulted in a one-off increase to the prospective starting pension at retirement, such as a pension increase exchange (or the exchange of part of a whole life pension for a bridging pension),
- as well as the pension input period when the member left pensionable service (as they were not a deferred member for the whole of the pension input period)

In respect of members who left pensionable service before 06 April 2006

As noted above, an individual who became a deferred member before 06 April 2006 under an arrangement and hasn't had any "accrual" since that time should remain outside the annual allowance regime.

However, such members can be brought within the annual allowance regime if they have "accrual" on or after 06 April 2006 (see **(b)** above). "Accrual" for these purposes isn't a defined term and will be a matter for the scheme trustees to determine with their lawyers. Exchange options such as cost-neutral pension increase exchanges or bridging options would typically not constitute accrual.

- (iv) Theoretically for such pension input periods, the pension input amount calculation should have taken into account the existence of GMP Equality. Although any adjustment to achieve GMP Equality should lead only to an uplift overall for retirement pension, the way the opening and closing values are calculated for the purposes of determining the pension input amount (including the adjustment made to the opening value in line with CPI) means the pension input amount in a particular pension input period may have been greater or smaller once the GMP Equality adjustment is taken into consideration.
- (v) The easement set out in **(ii)** above is helpful in reducing disruption and administrative burden. As HMRC considers there's no need to revisit pension input amount calculations done in the past, our view is that this indicates HMRC doesn't consider it necessary for schemes to provide members with corrected annual allowance information for tax years prior to the tax year in which an adjustment is made to achieve GMP Equality (or to revisit the calculation, or existence, of annual allowance charges attributable to those years).

¹⁸ This is because the statutory "relevant percentage" will cease to be the annual amount of increase specified by the pension scheme rules and will become the increase in the CPI over a 12-month period. The increase required by the new rules may be greater than CPI (and therefore greater than the "relevant percentage").

¹⁹ This is because, broadly, unless there is an annual rate "specified in the rules of the pension scheme", the "relevant percentage" will be the increase in the CPI over a 12-month period, and a discretionary provision may not be considered to "specify" a particular rate. However, the increase provided under the rules may be greater than CPI (and therefore greater than the "relevant percentage").

(vi) However, there are certain practical questions which arise here. For example, the HMRC Guidance states HMRC considers there's no need to revisit pension input amount calculations done "*in the past*". What does "*in the past*" mean in this context? Given the statement that calculations "*for the pension input amount in the tax year of implementing GMP equalisation and tax years thereafter*" will need to take into account the revised amount of the benefit entitlement, the most obvious interpretation is likely to be that "*in the past*" means 'in tax years prior to the implementation of GMP equalisation'. But what about a scenario in which implementation is delayed (potentially until the relevant member retires)? For how long can the pension input amount calculations be undertaken without taking into account the adjustment to achieve GMP Equality?

(vii) As noted above, Section 3.3 of the First Newsletter states:

"Calculations for the pension input amount in the tax year of implementing GMP equalisation and tax years thereafter will need to take into account the revised amount of the benefit entitlement in both the opening and closing benefit calculations."

Taking into account the revised amount of the benefit entitlement during a period of deferment may, in practice, require an annual GMP assessment on a notional benefit as if the member were retiring having reached Normal Pension Date²⁰.

4.3 How do adjustments interact with tax protections during deferment?

Please see **Appendix 1** for details as to how adjustments interact with fixed protection, enhanced protection, primary protection and individual protections during periods of deferment.

²⁰ Pursuant to the "valuation assumptions" set out in Section 277 of the Finance Act 2004

5. Reviewing periods where benefits are in payment

5.1 Introduction

Where a correction for the purposes of achieving GMP Equality results in an increase to what should have been the individual's starting pension at retirement, trustees should consider:

- how the benefit adjustment interacts with the lifetime allowance (LTA) legislation generally (see 5.2 below) and the trustees' disclosure obligations, as well as:
 - the approach for testing an individual's benefits under the scheme against the LTA (see 5.3 below)²¹
 - whether the benefit adjustment has any implications for members with:
 - fixed protection (see **Section 1 of Appendix 1**); or
 - enhanced protection (see **Section 2 of Appendix 1**); and/or
 - issues in relation to the (rare case of) payment of any new or increased LTA charge (see 5.3 below)²²
- how any arrears payment is to be treated from a tax perspective (see **Section 6** below); and
- in what circumstances a member who has experienced a *subsequent* benefit crystallisation event (BCE) in a different scheme should be informed about the requirement to notify such a scheme of any change in the LTA available at the time of the subsequent BCE (see **Appendix 2**)

5.2 How do adjustments interact with a member's LTA when benefits are in payment?

(a) LTA

- (i) The tax regime places no limit on the amount which can be saved within registered pension schemes but does place a limit on the amount of savings which receive tax relief, beyond which extra tax applies.

The LTA is the overall limit of tax-privileged pension savings a member can accrue across all of their registered pension arrangements, both occupational and personal (and any other tax-advantaged pension arrangements such as overseas schemes), before a tax charge known as the lifetime allowance charge (LTA charge) applies.

- (ii) There are three key LTA measures to remember:
- the **standard LTA (SLTA)**, which is set each tax year on a universal basis (it's £1,073,100 for the tax year 2020/21 and is expected to rise in line with inflation at the beginning of the next tax year)
 - an **individual's personal LTA**, which may be higher than the SLTA due to various enhancements and/or protections; and
 - an **individual's available LTA**, which is the individual's personal LTA as reduced through BCEs.

²¹ This is important in keeping the administration burden on schemes proportionate.

²² Or the treatment of (presumably very rare) cases of historical LTA charges that shouldn't have arisen once the adjustment to achieve GMP Equality is taken into account, for example, where a BCE₃ would not have arisen if the pension had, prior to the relevant increase which triggered the BCE₃, been adjusted to achieve GMP Equality.

- (iii) When an entitlement to benefit arises which is a BCE²³, the amount crystallised is measured against the individual's available LTA. If the amount crystallised under a BCE exceeds an individual's available LTA, an LTA charge²⁴ will be due.
- (iv) Broadly speaking, for each BCE, a calculation is undertaken of the percentage of the standard LTA (applying at the time of the BCE for the individual) used by the BCE. Despite the fact the standard LTA varies over time, the use of percentages in this manner provides an automatic form of indexation/normalisation between BCE dates.

(b) How does the adjustment interact with the LTA legislation?

- (i) For a pension already in payment, certain questions arise as to how the GMP Equality Adjustment interacts with current LTA legislation.
- (ii) In benefit correction exercises more generally, there's a question as to whether the benefit correction should be treated as:
- an upward adjustment to the BCE²⁵ which occurred when the individual originally became entitled to the payment of the pension;
 - a new pension entitlement (separate to the original pension), giving rise to a second BCE₂, with outstanding arrears due back to original retirement date; or
 - something else (for example, an increase to a pension in payment, potentially giving rise to a BCE₃)?

The approach taken may have an impact on how the GMP Equality Adjustment interacts with the individual's personal LTA.

²³ For a brief summary of BCEs, see PTM088100, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm088100#IDAF15K>

²⁴ HMRC guidance in relation to the lifetime allowance charge can be found in PTM 081000, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm081000>. An LTA charge of 55% applies to the value of any excess above the individual's available lifetime allowance that is taken as a lump sum. A charge of 25% applies to the value of any excess taken as a pension or designated to drawdown and is payable up front; this is in addition to any income tax payable in relation to the pension at the individual's marginal rate as payments are made.

²⁵ A 'BCE₂' arises where an individual becomes 'entitled' to a scheme pension. HMRC's Pensions Tax Manual (PTM088200, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm088200>) explains that, for the purposes of the tax legislation, the member only becomes 'entitled' to a pension benefit at the point when they first obtain an 'actual right' to receive it (as opposed to a 'prospective right'). HMRC state that a member has an 'actual right' when the member "has the right to a benefit without having to fulfil any further conditions or take any further actions".

(iii) Section 5.2 of the First Newsletter states:

"Where GMP equalisation implementation results in an increase to what should have been the individual's starting pension at retirement, the original BCE2 that occurred at retirement requires correction by reference to the revised starting pension with the test for any lifetime allowance charge (or any additional lifetime allowance charge) being by reference to the individual's remaining lifetime allowance at the time of the original BCE2 date[...]"

Any increase solely for GMP equalisation will be a correction of an entitlement that has already arisen and does not create a new entitlement for tax purposes. If the reason for the increase is as a mixture of GMP equalisation and other adjustments this could be a new entitlement for tax purposes."

Key message

HMRC's position is that:

- the GMP Equality Adjustment (if it impacts the starting rate of pension) should be treated as an upward adjustment to the BCE2 that occurred when the individual originally became entitled to the payment of the pension;
- the BCE2 that occurred when the individual originally became entitled to the payment of the pension should be recalculated; and
- the recalculated BCE2 should be tested against the individual's available LTA at the point the individual originally became entitled to the payment of the pension (and not, for example, the individual's available LTA at the date the adjustment is implemented)

(iv) HMRC's position appears reconcilable with an argument that:

- where a pension was put into payment after 17 May 1990, from the date the pension was put into payment the member had a right to a pension adjusted to achieve GMP Equality²⁶; and
- the entitlement which arose at the date of the original BCE2 was actually an entitlement to the "equalised" pension, which has, in practice, been underpaid (**Section 6** below deals with payment of arrears). **Section 7.3(d)** explains that an additional pension commencement lump sum can't be paid when GMP Equality is implemented (unless the GMP Equality Adjustment is implemented within 12 months of the original BCE2).

(v) As noted in **Section 1.4** above, this Guidance Note is focused on the HMRC Guidance. However, this shouldn't be interpreted as an endorsement of HMRC's approach or a suggestion that other approaches aren't legitimate in appropriate circumstances. Furthermore, a GMP Equality Adjustment

²⁶ There were no further conditions to fulfil or further actions for the member to take in order to become entitled to an equalised pension. The delay in implementing the correction did not arise from the member's inaction and an actual right had arisen

may differ from other benefit correction exercises where for various reasons the trustees may have decided the correction should be treated as a new pension entitlement (separate to the original pension), giving rise to a second BCE2, with arrears paid back to the original retirement date²⁷.

- (vi) Clearly, when considering the interaction between adjustments to achieve GMP Equality and tax legislation, trustees will need to take appropriate advice. Where trustees choose to adopt an approach which differs from that set out in the HMRC Guidance, professional advice to identify any potential tax consequences will be especially important²⁸.

(c) LTA charges arising directly from the recalculation of the BCE2

- (i) In the vast majority of cases, the original BCE2 won't have given rise to an LTA charge, and the increase in original BCE2 won't result in the member exceeding their available LTA at the date of the BCE2.

However:

- establishing no LTA charge is payable may involve significant work; and
 - an increase to the original BCE2 may have an impact on BCEs occurring after the date of the BCE2 (both under the same arrangement (see **(d)(iv)** below) and in other arrangements see **(d)(v)** below)).
- (ii) Where the original BCE2 had already resulted in an LTA charge, any upward recalculation of the BCE2 will result in a greater LTA charge.
- (iii) Where the original BCE2 didn't result in an LTA charge but the recalculated BCE2 results in the individual exceeding their available LTA at the point the individual originally became entitled to the payment of the pension, an LTA charge will be due.

Note: The LTA at the date of the original BCE2 may have been higher than the current LTA.

- (iv) Where a recalculated BCE results in a member exceeding their available LTA (or exceeding their available LTA to a greater extent), then an LTA charge will be due. Scheme administrators should consider what process is appropriate to adopt to identify whether any GMP equalisation adjustment to the member's benefit in their scheme is likely to have resulted in an LTA charge.
- (v) The HMRC Guidance notes, where the pension in question started before 06 April 2006, the adjustment to achieve GMP Equality won't trigger a BCE2 in the scheme (but see **(d)(iv)(G)** below in relation to notional BCEs).

²⁷ With the trustees having decided, for example, that the payment of arrears is an authorised payment pursuant to Regulation 2 of the Registered Pension Scheme (Authorised Payments — Arrears of Pension) Regulations 2006 and Section 164 of the Finance Act 2004.

²⁸ Such advice may need to consider, amongst other things, whether the resulting benefits are authorised payments and the ability to pay arrears.

- (vi) Further considerations relating to the retesting of members' benefits against the individual's available LTA are addressed in 5.3 below.

(d) Impact on events occurring after the date of the BCE2

- (i) Section 5.2 of the First Newsletter states:

"The recalculated BCE2 will affect any BCEs a member may have had after becoming entitled to the scheme pension that is being adjusted for GMP equalisation. Members will need to consider the tax effects of the recalculated BCE2 on later benefit crystallisations. This may include the member becoming liable to an lifetime allowance charge, or to a greater lifetime allowance charge."

Key message

Under HMRC's approach of recalculating the original BCE2, any reduction to the individual's available LTA as a result of the recalculated BCE2 could have an impact on crystallisations after the date of the BCE2 (including benefit crystallisations which have already occurred at the time of implementation of the GMP Equality Adjustment).

- (ii) These subsequent benefit crystallisations could have occurred in the same arrangement (including, for example, in relation to pension increases or step-ups, see (iv) below) and/or in other schemes or arrangements (see (v) below).

- (iii) Section 5.2 of the First Newsletter states trustees:

"should consider what process is appropriate to adopt to identify whether any GMP equalisation adjustment to the member's benefit in their scheme is likely to have resulted in an lifetime allowance charge".

Considerations relating to the retesting of members' benefits against the individual's available LTA are addressed in 5.3 below.

- (iv) Events in relation to the same arrangement (including in relation to the same adjusted benefit)

- (A) If (after 06 April 2006) a scheme pension in payment is increased to the extent that both the "threshold annual rate"²⁹ and "permitted margin" are exceeded, a "BCE3" will occur³⁰.

²⁹ Broadly speaking, in determining whether the "threshold annual rate" is exceeded, a comparison is undertaken of the rate of the scheme pension in payment a year before the increase and the rate of the pension after the increase. If the difference is more than the greatest of (a) RPI, (b) 5% of the rate of the scheme pension a year before the increase, and (c) £250, the threshold annual rate is exceeded.

³⁰ HMRC guidance on BCE3s can be found in PTM088630, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm088630>

- (B) Whilst the focus of the HMRC Guidance is on amendments to the starting rate of pension (i.e. a recalculation of the original BCE2), trustees will also need to consider the extent to which they need to review the period while the pension was in payment to identify:
- whether there are any 'new' BCE3s (i.e. whether a BCE3 arose but hadn't been identified until GMP Equality was implemented)
 - whether any 'old' BCE3s did not, in fact, arise (i.e. whether a BCE3 turns out not to have occurred once GMP Equality was implemented); and
 - with regard to any BCE3s which have occurred, whether the timing and amount crystallised was correct³¹
- (C) An adjustment to the starting level of pension and/or the dual record keeping approach to correcting pensions in payment may mean:
- an increase to the pension in payment previously understood to have occurred at a particular time (e.g. at age 65) didn't occur (or didn't occur to the same extent) and therefore a BCE3 did not arise³² (or did arise, but with a different amount being crystallised); and/or
 - a year-on-year increase to a pension in payment triggered a BCE3 not previously identified.
- (D) All correct BCE3s will need to be tested against the member's available LTA at the time of the BCE3.
- (E) The recalculation of the original BCE2 (and any BCE which occurred between the original BCE2 and when GMP Equality is implemented) means the individual's available LTA when a BCE3 occurred may have changed since any previous calculation.
- (F) The Trustee will need to consider whether:
- any LTA charge is due as a result of any newly identified BCE3s; and
 - whether any LTA charge previously treated as having arisen as a result of a BCE3 should have been different.
- (G) Impact on notional BCEs
- As noted above, the HMRC Guidance states, where a pension commenced before 06 April 2006, the adjustment to achieve GMP Equality will not trigger a BCE2 in the scheme.

³¹ One effect of a recalculated BCE2 (and higher starting pension) may be that a historical BCE3 (and any associated LTA charge) in relation to the same pension shouldn't have arisen.

³² i.e. the test was previously undertaken using unequalised (lower) benefits, which may have resulted in an undervaluing of the benefits pre-increase. Therefore, it is theoretically possible that an increase thought to have exceeded the threshold annual rate when tested against the unequalised pension would not have exceeded the annual threshold rate if tested against the (higher) equalised pension (i.e. a BCE3 should never have occurred).

However, if and when the member experiences their first actual BCE on or after 06 April 2006, a 'notional' BCE occurs³³ reflecting the value of any pension in payment on 05 April 2006. This is only a notional BCE, and won't itself generate a tax charge, however, it will reduce the amount of LTA available at the first actual BCE (and any subsequent BCEs).

An adjustment to achieve GMP Equality may mean the notional BCE should have been different and therefore has implications for the first actual BCE and any subsequent BCEs. For example, if the pension in payment before 06 April 2006 should have been greater, it's possible the individual's available LTA should have been further reduced as a result of a notional BCE, and the individual would have had less available LTA than previously understood at the point of their first actual BCE.

(H) Process for corrections where a new or additional LTA charge arises

Where a correction is required to an LTA charge in relation to a BCE which has occurred under the scheme, Section 6 of the First Newsletter states:

- the Accounting for Tax return in which the original BCE was reported should be amended to reflect the updated amount; and
- any Event Report will need to be amended if the value of events reported have changed or the revision to benefits results in further reportable events.

(v) Events in relation to a different arrangement

(A) A recalculation of the LTA used by an individual in one arrangement may be relevant for the trustees and managers of other arrangements under which a subsequent BCE has arisen.

(B) Even if a recalculated BCE₂ (or a new or recalculated subsequent BCE) doesn't result in an LTA charge in the scheme under which the "equalised" pension is paid, the recalculation could mean an LTA charge (or a greater LTA charge) is payable in relation to the relevant member's benefits crystallised under other schemes (or arrangements).

(C) It's most likely the trustees or managers of those other schemes will be unaware of the recalculation of a previous BCE (and any change in historical LTA usage) unless notified by the affected member.

³³ As explained in PTM088300, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm088300>

(vi) Member notifying other arrangements of revised LTA usage

(A) Section 5.2 of the First Newsletter states members:

"will need to consider the tax effects of the recalculated BCE2 on later benefit crystallisations".

(B) Where a member becomes aware of revised LTA usage in relation to a BCE in one scheme ("Scheme A"), the member may need to notify the trustee of a different scheme ("Scheme B") under which the member experienced a subsequent BCE.

(C) **Appendix 2** contains a template communication from the trustees of a Scheme A to members:

- informing members of this possible requirement; and
- including a schedule of key information which could be used by members when communicating with a Scheme B.

The purpose of this template wording is both to pre-empt the member asking the administration team of Scheme A for assistance in (or information for the purposes of) communicating with Scheme B, and to provide the information in a standard form for Scheme B, thereby reducing the burden on administration teams of both schemes.

(D) In practice:

- the member is only likely to provide information to Scheme B where the member considers a benefit adjustment in Scheme A may have an impact on whether and to what extent an LTA charge arose in Scheme B (and a communication with information to assist the member with such considerations may help reduce individual member requests for assistance); and
- Scheme A is unlikely to need to send such a communication to any member who experienced an LTA charge in relation to the original BCE (as the benefit adjustment in Scheme A is unlikely to have any impact on the LTA charge which arose in Scheme B)

5.3 Practical approach for retesting members' benefits against LTA

(a) Adopting a process to identify whether any GMP equalisation adjustment resulted in an LTA charge

Section 5.2 of the First Newsletter states that scheme administrators:

"should consider what process is appropriate to adopt to identify whether any GMP equalisation adjustment to the member's benefit in their scheme is likely to have resulted in an lifetime allowance charge".

In considering potential processes, trustees are likely to split members up into two groups, namely:

- those for whom an LTA charge was already treated as having arisen when the individual originally became entitled to the payment of the pension (see (b)); and
- those for whom no LTA charge was treated as having arisen when the individual originally became entitled to the payment of the pension (see (c)) — a scenario which is expected to be far more common

(b) Members for whom an LTA charge was treated as having arisen at the time of the original BCE2

- (i) Any increase in the original BCE2 would create an additional LTA charge related to the original BCE2.

Comment: To put the likely scale of this issue into context:

- we understand the total number of LTA charges paid by schemes through Accounting for Tax returns for tax years 2006/07 to 2017/18 was, in total, only 18,900³⁴;
 - we've no record of how many crystallisations happened over the same period (so can't estimate with accuracy the proportion of members likely to be affected); however, taking the 2017/2018 tax year as an example, the statistics show:
 - 4,550 LTA charges were paid by schemes through Accounting for Tax returns; while
 - over 590,000 pension plans were accessed for the first time in the same period (to buy an annuity, move into drawdown or take a first cash withdrawal)³⁵, on top of which there would have been a large number of individuals whose pensions from occupational defined benefit pension schemes commenced.
- (ii) Scheme administrators and the member have "joint and several" liability for the LTA charge. When pensions come into payment, trustees can pay the LTA charge and reduce the member's benefits by an actuarially equivalent amount.
- (iii) One approach would therefore be for the scheme to:
- calculate the increase in the BCE2 arising from the adjustment to be made to the member's starting pension to achieve GMP Equality (i.e. 20 x the increase in starting rate of the pension)
 - calculate the LTA charge (or additional LTA charge) that should have arisen when the individual originally became entitled to the payment of the pension and pay any LTA charge (or additional LTA charge) ("New Charge") to HMRC
 - calculate the reduction which would have been applied to the member's equalised pension, had a reduction been made from the date of the BCE2 to take account of the New Charge; and
 - take such a reduction into account when paying arrears to the member and, if that is not sufficient, making an adjustment to the pension put into payment to implement GMP Equality³⁶.

³⁴ See the September 2019 Table of Lifetime Allowance Statistics, <https://www.gov.uk/government/statistics/personal-pensions-pensions-lifetime-allowance-statistics>.

³⁵ see the FCA's "Retirement income market data 2018/19", <https://www.fca.org.uk/data/retirement-income-market-data-2018-19>.

³⁶ For some members, where lifetime allowance had been fully used up, any benefit entitlement crystallising beyond that point, may have been paid as a "lifetime allowance excess lump sum". HMRC have not yet provided guidance as to whether this approach could be used to address the New Charge.

(iv) In some cases, due to the interaction between:

- the way in which the LTA charge is calculated (i.e. based on the member's starting pension); and
- adjustments for GMP Equality being made on a year-on-year basis,

the New Charge may be greater in amount than the actuarial value of the adjustment for GMP Equality.

(v) For example, in an extreme case, the member may find:

- a higher starting pension results in a New Charge; but
- there's little or no change to the level of the ongoing gross pension (and the amount of any arrears may be small)

meaning neither using the arrears nor making an adjustment to the pension put into payment to implement GMP Equality would be sufficient to address the New Charge.

(vi) Given the joint and several liability, the trustees may find themselves with an obligation to pay a tax charge without an appropriate way of recovering the cost from the member³⁷. In such cases careful consideration will be required by the Trustees and appropriate advice obtained. It's not possible to apply a reduction to a member's pension once it's in payment. A scheme pension must ordinarily be payable for life at a rate not less than the initial rate³⁸. Whilst there are exceptions, those exceptions don't include a reduction to pay an LTA charge.

(vii) However, depending on the circumstances, it may be possible to reach agreement with the member that the scheme will 'redirect' an appropriate amount of the member's pension to HMRC for the member, to pay the charge for which the member is liable³⁹. This would need to be carefully documented.

(c) Members for whom no LTA charge was previously treated as having arisen

(i) In order to ascertain whether an LTA charge should have arisen for such members, trustees would need information about the member's available LTA at the time of the original BCE2. The information obtained at the time of the original BCE2 may have been the exact amount of available LTA (as understood by the member at the time) or, more usually, information which was otherwise sufficient for the Trustee to conclude the member had sufficient available LTA to mean no LTA charge was payable.

³⁷ Where the scheme funds the charge (or part of it) without correspondingly reducing the rights of the member, the level of the charge may be higher (see PTM085000, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm085000>)

³⁸ See PTM62340, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm62340>

³⁹ The intention being that the *member* pays the tax from their pension. However, it may be necessary to consider Section 254 of the Finance Act 2004 which sets out certain reporting obligations for the purposes of the scheme return and payment obligations.

(ii) Depending on the approach taken by the trustees in the past, reliable data for determining whether the member has sufficient available LTA to accommodate the increase in the BCE2 without triggering an LTA charge may not be readily available. For example, the data may be very expensive to recall from archives etc., may no longer be correct because of adjustments made to benefits under other arrangements, may no longer exist, or may no longer be sufficient to determine the member had sufficient available LTA to mean no LTA charge was payable or would be payable once GMP Equality is implemented).

(iii) Where reliable data isn't readily available:

- depending on the scheme's circumstances (including, for example, the number of members and the earliest dates upon which a BCE2 may have occurred) trustees may consider it impractical to ask every member in respect of whom an adjustment is to be applied to confirm their available LTA usage at the date of the BCE2; and
- trustees may consider it disproportionate to simply assume the member has already used up all of their LTA and treat the member as subject to an LTA charge⁴⁰.

(iv) Trustees will likely need to take advice on the approach to be taken in such circumstances. Depending on the scheme's circumstances, we think it would be appropriate for trustees to adopt the following approach (which seems reasonable and proportionate):

- to assume members had sufficient available LTA at the time of the original BCE2 for the equalised pension to be put into payment without an LTA charge becoming payable (unless the trustees have information which is incompatible with this assumption, for example, where the revised BCE2 is more than 100% of the member's standard/protected LTA at the time of the original BCE2)
- to issue a communication to the member (see **Appendix 2** for template wording):
 - informing them of the revised LTA usage and the fact this affects the LTA they had available from the point of the BCE2
 - notifying them that, as a result of the adjustment to achieve GMP Equality, an LTA charge may be payable (under the scheme and/or under the member's other pension arrangements)
 - explaining how the member might easily establish whether an LTA charge is clearly not payable in relation to the BCE2 (or an LTA charge might be payable)
 - requesting prompt confirmation from the member if they consider an LTA charge might be payable in relation to the original BCE2
 - notifying the member that, unless the member informs the trustee within a specified period (for example, within four weeks of the communication to the member) that an LTA charge might be payable in relation to the original BCE2, the member's

⁴⁰ Although this approach may be considered appropriate in certain cases, see for example PTM086000, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm086000>

pension will be adjusted (and an arrears payment will be made) on the assumption no LTA charge is payable (but the member will remain liable for any tax due)

- (v) As noted above, scheme administrators and the member have "joint and several" liability for the LTA charge. If, contrary to the assumption made by the trustees, an LTA charge is payable (but hasn't been recovered from the member at the point at which the GMP Equality Adjustment was made), the approach set out in **(b)(iii)** above can't be adopted: the arrears can't be used to meet the LTA charge because they've already been paid to the member, nor can an adjustment be made to the pension put into payment to implement GMP Equality, as it's already in payment (as stated above, it's not possible to apply a reduction to a member's pension once it's in payment). However, depending on the circumstances, the Trustees may consider the approach set out in **(b)(vii)** above (i.e. reaching an agreement with the member to 'redirect' an appropriate amount of the member's pension to HMRC for the member, to pay the charge for which the member is liable).
- (vi) As noted in the HMRC Guidance, in certain situations⁴¹ a scheme administrator can apply in writing to HMRC to have all or part of their liability to the LTA charge discharged. Subject to taking appropriate advice, schemes might conclude:
- in the event any new LTA charge emerges, they will apply to HMRC for a discharge to address the risk set out in **(v)** above (if such an application was appropriate in the circumstances)⁴²; and
 - the sums at risk if HMRC were to reject an application to discharge the scheme from liability are unlikely to be material in the context of scheme funding.

⁴¹ See PTM158000, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm158000>. Time limits for making such an application apply and may mean that an application is not possible in the circumstances.

⁴² This would not discharge the member from liability.

6. Tax treatment of arrears payments

6.1 Obligation to pay arrears

- (a) As noted above, the Lloyds Bank judgment confirmed there's an obligation to adjust the benefits payable under an occupational pension scheme in excess of GMP in order that the total benefits (for service on and after 17 May 1990) received by male and female members are equal — and this obligation has existed since 17 May 1990.
- (b) In the Lloyds Bank case:
- it was accepted that, to the extent members have in the past been paid lower benefits than would have been paid had GMP Equality been implemented from 17 May 1990, the trustee was obliged to make back-payments to members
 - it was decided the period of time which was relevant for the purpose of calculating the amount of back-payments is determined by the governing provisions of the scheme (see 6.4 below); and
 - the parties agreed the trustee should pay interest on the arrears in relation to the period during which each instalment was due and unpaid (i.e. in relation to each instalment where the member has been paid lower benefits than would have been paid had GMP Equality been implemented from 17 May 1990)

6.2 Approach to payment of arrears and deduction of tax

- (a) Section 6 of the First Newsletter states:

"Arrears of pension may be paid to scheme members as a lump sum as part of the GMP equalisation exercise. The pension payer is required to operate PAYE on the lump sum. However, the amount of pension income charged to tax is the amount of pension the member is entitled to in the tax year (the accruals basis).

The amount of tax deducted under PAYE may be more than the tax due under the accruals basis. Members can contact HMRC to claim the correct tax treatment (see EIM74103)."

- (b) In other words:
- each instalment of pension income is chargeable to tax in the tax year in which the individual became entitled to the instalment (even where the pension paid was less than the full instalment to which the individual was entitled) which won't necessarily be the tax year in which the aggregated arrears payment is received; however
 - trustees are required to operate PAYE on the aggregated arrears payment; consequently
 - where an individual is usually a basic rate taxpayer, the operation of PAYE on the aggregated arrears payment may result in a greater level of tax being deducted than would have been the case if tax had been deducted as and when the individual became entitled to each instalment⁴³

⁴³ This is the case irrespective of whether a "single BCE2" approach is adopted.

(c) HMRC's Employment Income Manual (EIM74103) states:

"The pensioner should contact the tax office and supply a schedule showing the years to which underpayments are attributable. HMRC will spread the payments back over the relevant years and recalculate liability. Underpayments in the earlier years may be set-off against the resulting over-payment in the year of the lump-sum payment."

(d) Where a pensioner wishes to submit to the tax office a schedule showing the years to which underpayments are attributable ('Arrears Schedule'), it's likely they'll request such information from the trustee.

(e) A template 'Arrears Schedule' (as part of a template letter from the member to HMRC) is set out in **Appendix 3**.

6.3 Payment of interest on arrears and taxation of such a payment

(a) The HMRC Guidance states pension schemes may pay interest on arrears of pension and refers to HMRC's Pensions Tax Manual (PTM143100) for an explanation as to how such interest will be taxed.

(b) PTM143100 deals with the taxation of 'scheme administration member payments'. To qualify as a scheme administration member payment (under Section 171 of the Finance Act 2004), any interest paid should be made on an arm's length, commercial basis (for example, a rate comparable to what the member might have obtained if he or she had received the money and deposited it in the bank). PTM143100 warns *"any excess will be an unauthorised member payment and taxed accordingly"*.

(c) Our conclusion is if interest is paid on arrears at the same rate as set out in the Lloyds Bank judgment⁴⁴:

- it would qualify as a scheme administration payment; and
- it's subject to income tax in the year in which it is eventually paid⁴⁵

(d) Schemes may wish to consider more generous rates of interest, for example where arrears are being backdated for more than six years, or where a scheme prefers to pay compound rather than simple interest, or where a scheme's rules prescribes an interest rate for such payments.

⁴⁴ *Lloyds Banking Group Pensions Trustees Limited v Lloyds Bank Plc* [2018] EWHC 2839 (Ch) (26 October 2018), <https://www.bailii.org/ew/cases/EWHC/Ch/2018/2839.html>.

⁴⁵ PTM143100, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm143100>, includes an example of a monthly instalment of a benefit paid to a member later than he was entitled to receive it, with the scheme administrator paying interest in respect of the delay. In the example, HMRC state that the *"normal rules for determining whether the interest is 'yearly' or 'short' will apply"*. In the example (which deals with a payment of one late monthly instalment made within one year of when it was due), HMRC go on to state that *"there is no doubt that the interest is short, and there is no requirement for the scheme administrator to deduct income tax from it"*. However, PTM143100 does not say that the scheme administrator should not deduct income tax. The authors understand it would be common for administrators to deduct income tax from interest payments relating to arrears and that to do so may often be administratively easier for both the member and the scheme.

6.4 Benefits which are subject to forfeiture provisions

- (a) The rules of many schemes provide for the forfeiture of unclaimed benefits after a certain period of time (this may, for example, be six years after an instalment has fallen due for payment). In some cases, a scheme's rules will provide the trustee with a discretionary power to prevent the forfeiture.

- (b) Where the trustee chooses to exercise such a discretionary power to prevent the forfeiture, we consider the best interpretation will generally be the trustee is preventing an existing entitlement from being extinguished (rather than the trustee creating a new benefit).

- (c) This distinction is important, because it would mean the exercise of discretion wouldn't result in a new entitlement to benefits which could, for example, have an impact on the way an individual's annual allowance LTA usage is calculated.

7. Lump sum payments

7.1 Second Newsletter

(a) On 16 July 2020, HMRC published the Second Newsletter⁴⁶, which states:

"If pension schemes have started to pay pensions and made lump sum payments, further payments may be due if schemes find that benefits have been underpaid due to GMP equalisation. This guidance covers tax issues in respect of lump sums previously paid and the payment of lump sums as a result of GMP equalisation."

(b) The Second Newsletter addresses:

- previous lump sum payments (see 7.2 below); and
- future lump sum payments (see 7.3 below)

(c) This chapter considers the content of the Second Newsletter; however, the GMP Equalisation Working Group intends to provide further guidance in relation to lump sum payments in the next iteration of this Guidance Note.

7.2 Previous lump sum payments

(a) The Second Newsletter states:

"Whether or not a lump sum payment is authorised depends on whether the payment conditions that applied at the time of the payment have been met."

Key message

The Second Newsletter directly addresses two payment conditions which apply to certain lump sum payments:

- the requirement to extinguish rights under the scheme (or arrangement) (see (b) below); and
- limits on the amount of the lump sum payment (see (c) below).

(b) Extinguishing rights

(i) For certain lump sum payments, one of the payment conditions is a requirement to extinguish the member's (or dependant's) rights under the scheme (or arrangement as appropriate). This includes a:

- serious ill health lump sum (SILS)
- trivial commutation lump sum (TCLS)
- small lump sum under Regulations 11 or 12 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (small lump sum)
- winding-up lump sum (WULS)

⁴⁶ <https://www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-july-2020>

- trivial commutation lump sum death benefit (TCLSDB)
- winding-up lump sum death benefit (WULSDB)

(ii) The Second Newsletter states (emphasis added):

"The reference to extinguishing the member's (or dependant's) entitlement to benefits is to all the benefits or rights that could reasonably have been known about at the time of the payment. The 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 of the lump sum payment. This reflects the exceptional circumstances associated with GMP and applies once the scheme administrator adopts their chosen GMP equalisation methodology."

(iii) This is a helpful statement from HMRC. However, a question arises as to what is meant by "could reasonably have been known about at the time of the payment". It appears lump sums paid before the trustees have determined how to implement GMP Equality won't stop being authorised payments, since the trustees won't "reasonably have known" about the additional entitlement before this time (in particular, until the GMP equalisation methodology has been chosen, the additional entitlement can't be calculated). It's not clear how this interacts with scenarios, for example, where a GMP equalisation methodology has been chosen, but scheme administrators haven't implemented a process to calculate the GMP Equality Adjustment (i.e. in this scenario, could the scheme administrator reasonably have known about the GMP Equality Adjustment to be applied to a particular member's benefits at the time of the payment?).

(iv) Similar considerations arise in relation to the statement that this "applies once the scheme administrator adopts their chosen GMP equalisation methodology". It's unclear whether the reference to the 'adoption' of a chosen GMP equalisation methodology is intended to be a separate step to the selection of a GMP equalisation methodology (as opposed to implementation).

(v) We note the Second Newsletter, when providing guidance in relation to specific lump sums, simply states that when schemes *"have chosen their method of equalising GMP"*⁴⁷ this will need to be taken into account in calculating and paying the lump sum (i.e. there's no reference to the 'adoption' of a methodology).

(vi) Taking advice, trustees may decide to avoid this ambiguity by not definitively selecting a GMP equalisation methodology until the scheme is in a position to implement payments on the basis of such a methodology. In practice, many schemes have suspended payment of these lump sums and a prudent approach would be to continue such suspension until the scheme is ready to implement GMP Equality or at least is in a position to pay an equalised lump sum in respect of the particular member.

⁴⁷ See the Second Newsletter's guidance in relation to serious ill health lump sums, trivial commutation lump sums, and small lump sums under regulations 11 or 12

(c) Payment limits

(i) For certain lump sum payments, one payment condition is a limit on the amount of the payment. This includes a:

- small lump sum under Regulations 11 or 12 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (small lump sum)
- winding-up lump sum (WULS)
- trivial commutation lump sum death benefit (TCLSDB)
- winding-up lump sum death benefit (WULSDB)

Note: This isn't the case in relation to trivial commutation lump sums, in relation to which the limit is the value (using an HMRC basis) of all pensions under authorised schemes, not the amount of the payment, see (iii) below.

(ii) The Second Newsletter states:

"As long as the previous lump sum payment was not more than the relevant payment limit, that lump sum will not stop being an authorised payment purely because, due to GMP equalisation, further entitlement is later identified."

(iii) Past payment of a trivial commutation lump sum (TCLS)

(A) The Second Newsletter highlights the fact that for TCLS payments the situation is different (emphasis added):

*"Instead of a limit on the amount of the lump sum payment, the limit is based on the value for the member's pension rights under all registered pension schemes on the 'nominated date'."*⁴⁸

(B) The limit on the value for the member's rights is as set out below:

Nominated date	Limit
On or after 06 April 2006 but before 06 April 2012	1% of the SLTA
On or after 06 April 2012 (where the first trivial commutation lump sum payment from any registered pension scheme was paid before 27 March 2014)	£18,000
Not relevant, whenever the first trivial commutation lump sum payment from any registered pension scheme was made on or after 27 March 2014	£30,000

Note: As GMP rights were accrued before 6 April 1997, HMRC's position is that the value of the member's pension rights on the nominated date includes the equalised GMP rights.

⁴⁸ The approach to valuing the member's pension rights for these purposes is set out in legislation. In other words, it's not the amount paid by the scheme that matters. For example, when valuing uncrystallised rights in a defined benefits arrangement on the nominated date, the value is likely to be (i) 20 times the annual rate of pension the member would be entitled to if they became entitled to the actual payment of benefits on the nominated date, plus (ii) the amount of any separate lump sum (see PTM063000 and PTM134500).

(C) The Second Newsletter states:

"It may be that as a result of equalising GMP rights the value of the member's rights on the nominated date is found to be more than the relevant limit. If this is the case the original lump sum payment cannot be a trivial commutation lump sum. Unless the lump sum can meet the payment conditions for another type of authorised payment, for example a small lump sum, the payment will be unauthorised."

Key message

- There is a risk that, as a result of implementing GMP Equality, trivial commutation lump sums previously paid are “found” not to meet the conditions of a trivial commutation lump sum payment (because the value of the member's pension rights under all registered pension schemes, including GMP Equality Adjustment, exceeded the limit that applied when the trivial commutation lump sum was paid (i.e. the time of the original BCE6), in which case they would be unauthorised payments⁴⁹).

(D) The HMRC Guidance doesn't provide any guidance to schemes finding themselves in this position. The GMP Equalisation Working Group is aware this may be an issue for some schemes and is giving further consideration to this point.

(E) Assumptions in relation to past payments

In a similar approach to the one set out at 5.3(c)(iv) above, depending on the scheme's circumstances, trustees may consider (upon taking advice) it to be reasonable and appropriate to assume the value of the member's pension rights (under all registered pension schemes) on the nominated date was within the relevant limit unless the trustees have information which is incompatible with this assumption (for example, where the revised value of the member's rights following adjustment for GMP Equality within the arrangement in question is more than the relevant limit).

(F) Trivial commutation lump sum payments made before 06 April 2006

- As noted above, the Second Newsletter states that, as GMP rights were accrued before 06 April 1997, the value of the member's pension rights on the 'nominated date' includes the equalised GMP rights.
- The principle underpinning HMRC's position would appear to apply equally to the tax regime in place prior to 06 April 2006 (in relation to trivial commutation lump sum payments made after 17 May 1990).

⁴⁹ One of the conditions of a small lump sum payment under Regulation 11 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 is that the commutation value of the benefits under the scheme and any related scheme must not exceed £10,000 in total. In theory, this could give rise to the same problems identified here for TCLS payments. However, the Second Newsletter does not address this point. In practice, we understand that small lump sum payments under Regulation 11 are less common than those under Regulation 12. This issue doesn't arise for small lump sum payments under Regulation 12.

- Therefore, it appears there's a risk certain trivial commutation lump sum payments made on or after 17 May 1990 but before 06 April 2006 didn't meet the conditions in place at the time (e.g. because the member was in fact entitled to a pension value of more than £260 per annum, which was the limit under the tax regime which applied immediately before 06 April 2006⁵⁰).
- The authors believe the original payment wouldn't result in an unauthorised payments charge under the current authorised payments regime. Further, we believe it wouldn't be proportionate for the schemes to seek to identify whether or not the GMP Equality Adjustment for any member would have increased the pension so that it was more than £260 per annum⁵¹ such that the lump sum shouldn't have been paid. Any top-up payment made as a result of implementing GMP Equality would be subject to the authorised payments regime (as a new lump sum payment, see 7.3 below).

7.3 Future lump sum payments

(a) Payment conditions

- (i) The Second Newsletter states (emphasis added):

"Where benefits have previously been paid, depending on the circumstance, a further lump sum payment may be an authorised payment. Any payment, including 'top-up' payments to previous lump sums, must satisfy the payment conditions in force at the time the payment is made."

- (ii) HMRC then clarifies this further by stating:

"Where a scheme is considering making a 'top-up payment' this means the payment conditions in force at the time the 'top-up' payment is made, not the date of the original lump sum payment. This may mean that a top-up lump sum payment cannot be an authorised payment, or it is another form of authorised payment."

- (iii) To further develop an example given by HMRC in relation to trivial commutation lump sums:

Example

In May 2015, a trivial commutation lump sum payment was made to a member. In order to implement GMP Equality, a 'top-up' payment is now to be paid to the member.

The 'top-up' payment can't be a trivial commutation lump sum payment because the individual had a one-off 12-month period to commute trivial funds across all their schemes, which will have expired. Any commuted lump sum paid after the 12-month period has ended won't qualify as a trivial commutation lump sum.

⁵⁰ The allowable value of trivial benefits for full commutation may have been lower, depending on when the payment was made prior to 06 April 2006.

⁵¹ Or the allowable value that applied at the relevant time (see footnote above).

However, it may qualify as a 'small lump sum' if the relevant payment conditions⁵² (including the size of the payment) are satisfied.

(b) Relevant tax year for 'top-up' payments

The Second Newsletter clearly states:

"Authorised lump sums that are taxable are subject to tax in the tax year that the lump sum is actually paid. For the avoidance of doubt, where the payment is a top-up payment this is the date the top-up payment is made, not the date of the original payment."

(c) Payments following the member's death

The Second Newsletter notes certain types of lump sum payments must be paid to the member (and can't be authorised payments if they're paid following the member's death):

- pension commencement lump sum (PCLS)
- serious ill health lump sum (SILS)
- trivial commutation lump sum (TCLS)
- winding-up lump sum (WULS)

(d) Pension commencement lump sum (PCLS)

(i) The Second Newsletter states:

"Pension commencement lump sums (PCLS) can be paid in stages, that is, a PCLS does not need to be a single payment. However, one of the conditions for a payment to be a PCLS is that the payment must be made within the period beginning 6 months before and ending one year after the member becomes entitled to it."

Key message

The payment of a further PCLS may be possible if it's paid within 12 months of the member becoming entitled to their scheme pension, i.e. the date of the original BCE2.

If the member became entitled to their scheme pension more than 12 months ago, because the top up is an increase to the original BCE2, the pension scheme can't pay a further PCLS.

(ii) The Second Newsletter also states:

"Where payment of a further PCLS is possible the BCE 6 will need to be recalculated, and a revised benefit crystallisation event (BCE) statement given to the member."

⁵² 52 see PTM063700, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm063700>

(e) Serious ill health lump sum (SILS)

- (i) The Second Newsletter states (emphasis added):

"Scheme administrators should be aware of the requirement to equalise GMPs and which members are potentially affected by this requirement.

When schemes have chosen their method of equalising GMP, this will need to be taken into account in calculating and paying the lump sum. Scheme administrators should note the requirement is to extinguish rights under an arrangement not under the whole scheme.

A member may have a number of different arrangements under a scheme, as the scheme may use different arrangements to provide different types or tranches of benefit. It is up to scheme administrators how they structure their scheme."

- (ii) As noted above, this raises the question as to what is meant by a scheme 'choosing its method of equalising GMP'. As stated in **7.2(b)(vi)**, taking advice, trustees may decide to avoid this ambiguity by not definitively selecting a GMP equalisation methodology until the scheme is in a position to implement payments on the basis of such a methodology.
- (iii) In relation to SILS, HMRC has previously stated that where *"because of contracting-out requirements, dependants' benefits have to be retained under the scheme, then either before or at the time a serious ill-health lump sum is paid, the dependants' benefits might be moved to a separate arrangement"*⁵³.

(f) Trivial commutation lump sum (TCLS)

- (i) The Second Newsletter notes one of the payment conditions for a trivial commutation lump sum is the payment extinguishes the member rights under the scheme. In this regard, it's stated (emphasis added):

"scheme administrators should be aware of the requirement to equalise GMPs and which members are potentially affected by this requirement – when schemes have chosen their method of equalising GMP, this will need to be taken into account in calculating and paying the lump sum"

Note: The considerations set out in **(e)(ii)** above also apply here.

- (ii) As noted above, a further payment condition is that it's to be paid within 'the commutation period' (a period of 12 months beginning with the day the member is first paid a trivial commutation lump sum by any registered pension scheme)⁵⁴:

⁵³ For further details, see PTM063400, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm063400>

⁵⁴ As noted above, whilst a 'top-up' payment may not qualify as a trivial commutation lump sum, it may qualify as some other type of authorised payment (e.g. a 'small lump sum') if the relevant payment conditions are satisfied.

"This means that if any registered pension scheme has paid a trivial commutation lump sum to a member and the first such payment was more than 12 months ago no further payment of a trivial commutation lump sum to that member is possible."

(g) Small lump sum under Regulations 11 or 12 of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (Small Lump Sum) ⁵⁵

(i) With regard to the conditions of such a payment, the Second Newsletter states:

"From a tax perspective, there's no requirement for the lump sum to be paid to a member. These provisions may be used to pay a lump sum following the death of a member. Neither is there a time-frame in which the payment must be made."

(ii) The Second Newsletter states:

"Scheme administrators may consider using regulation 12 to pay a further lump sum to extinguish the members rights where:

- *further benefits have been identified as payable to a member*
- *the value of their total rights under the scheme is not more than £10,000."*

Comment: The authors presume that HMRC's reference to "the value" of the total rights under the scheme being not more than £10,000 is intended to be a reference to the payment not exceeding £10,000⁵⁶.

(iii) More generally, the Second Newsletter states (emphasis added):

"When schemes have chosen their method of equalising GMP, this will need to be taken into account in calculating and paying the lump sum."

Note: The considerations set out in **(e)(ii)** above also apply here.

(h) Defined benefits lump sum death benefit (DBLSDB)

One relevant factor here will be whether the DBLSDB is to be paid within two years of the earlier of:

- the date the scheme administrator first knew of the member's death, or
- the date the scheme administrator could reasonably have been expected to know of the member's death⁵⁷.

⁵⁵ For further details, see PTM063700, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm063700>

⁵⁶ i.e. the condition set out in Regulation 12(1)(e) of the Registered Pension Schemes (Authorised Payments) Regulations 2009

⁵⁷ See PTM073100, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm073100>

If it's paid within the two-year period (and the member was aged under 75 when they died), it will trigger a BCE7. If it's paid outside the two-year period (or if the member was aged 75 or older when they died), no BCE 7 will be triggered but the lump sum will be taxable⁵⁸.

(i) Trivial commutation lump sum death benefit (TCLSDB)

The Second Newsletter states:

"There is no time limit for paying this type of lump sum. Where further dependants' scheme pension is identified for a dependant, the scheme administrator may consider commuting that pension within the payment terms for this type of lump sum."

⁵⁸ See PTM073100, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm073100>

8. GMP conversion

8.1 HMRC Guidance

As noted above, in the Second Newsletter, HMRC stated:

"The position regarding conversion is complex and its effects within the pension tax rules may have wider impacts. For example, there may be implications when testing against the annual allowance, or whether the deferred member carve out applies, or where an individual has a lifetime allowance protection.

HMRC is unable to provide supplemental guidance on conversion, as more detailed work needs to be done on the wider issues associated with that methodology. Any schemes wishing to use the conversion method should consider any tax implications that may arise in accordance with the existing legislation and guidance within the PTM and seek advice as appropriate."

8.2 This Guidance Note

- (a) Because of the ongoing uncertainty around the tax implications of conversion, and our understanding that no further guidance is expected from HMRC at this time, this version of the Guidance Note doesn't cover GMP conversion in detail.
- (b) The GMP Equalisation Working Group intends to publish separate guidance on GMP conversion (including tax considerations) in due course.

8.3 Current activity

- (a) We appreciate certain schemes will have already undertaken a GMP conversion project and others may follow, if and when conversion is confirmed as their preferred methodology to implement GMP Equality.
- (b) It's imperative the trustees of schemes considering GMP conversion receive scheme-specific advice on the potential tax consequences and any options for negating or mitigating adverse tax consequences such as the loss of LTA protections or deferred member carve outs.
- (c) It's the authors' understanding the approaches listed below are being considered by certain schemes as ways to potentially help address adverse tax consequences which may arise for some members when GMP conversion is adopted as a methodology to implement GMP Equality. The issues relating to each of these approaches are currently being considered by the GMP conversion subgroup:
 - (i) an "at crystallisation" approach to conversion where GMP isn't converted to scheme benefits until members retire;
 - (ii) a "constrained initial pension" approach, whereby the intention is:

- revaluation in deferment is set at a level such that it doesn't create annual allowance issues, which typically might mean lower future revaluation in deferment (perhaps CPI); and
- the value foregone as a result of a lower revaluation is instead provided by way of higher indexation once the pension is in payment,

with the overall design intended to deliver benefits with an actuarial value equal to the greater of the member and comparator benefits; and

- (iii) “internal transfers” between arrangements in the same pension scheme (pursuant to guidance in the Pensions Tax Manual at PTM053710⁵⁹). This is because, where the annual allowance transfer provisions apply, a change in rate of pension can, in certain specific circumstances, operate on a basis which is neutral from an annual allowance perspective.

Comment: We are not recommending any specific course(s) of action and aren’t currently commenting on whether these approaches would work (and, if so, in which circumstances). Approaches would have to be considered on a scheme by scheme basis with appropriate advice.

- (d) Despite outstanding questions regarding the tax treatment of the conversion method, there may still be scope for schemes to progress certain elements of their GMP equalisation projects (for example, addressing data considerations and correction of past payments using a dual record keeping approach), where trustees consider that it's appropriate to do so. Subject to appropriate advice, schemes may in fact decide to proceed with implementing GMP Equality using conversion. For schemes contemplating ‘buy-out’ after GMP Equality, providers may insist on a particular method.

⁵⁹ See PTM053710, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm053710>

APPENDIX 1 – TAX PROTECTIONS (FIXED PROTECTION, ENHANCED PROTECTION, PRIMARY PROTECTION AND INDIVIDUAL PROTECTIONS)

1. Fixed protection 2012, fixed protection 2014 and fixed protection 2016 (together referred to in this Guidance Note as "fixed protection")

1.1 Fixed protection generally

(a) Background⁶⁰

(i) Fixed protection 2012

- With effect from 06 April 2012 the SLTA was reduced from £1.8 million to £1.5 million. If an individual has fixed protection 2012, their LTA is the greater of the SLTA from time to time and £1.8 million
- Individuals wishing to rely on fixed protection 2012 had to notify HMRC by 05 April 2012

(ii) Fixed protection 2014

- With effect from 06 April 2014 the SLTA was reduced from £1.5 million to £1.25 million. If an individual has fixed protection 2014, their LTA is the greater of the SLTA from time to time and £1.5 million.
- Individuals wishing to rely on fixed protection 2014 had to notify HMRC by 05 April 2014

(iii) Fixed protection 2016

- With effect from 06 April 2016 the SLTA was reduced from £1.25 million to £1 million. If an individual has fixed protection 2016, their LTA is the greater of the SLTA from time to time and £1.25 million
- There is no deadline for individuals wishing to rely on fixed protection 2016 to notify HMRC

(b) Loss of fixed protection

There are certain conditions to retaining fixed protection. For example, benefit accrual (as defined under legislation, see 1.3(a) below) can cause an individual to lose fixed protection.

1.2 Could fixed protection be lost as a result of an adjustment to achieve GMP Equality?

The First Newsletter includes the following statements:

- *"An individual who otherwise has a fixed protection should retain that protection"*
- *"Any increase solely for GMP equalisation will not be 'benefit accrual' and so should not result in loss of fixed protection"*

⁶⁰ For more detail, please see PTM093100, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm093100>

HMRC's reading of the legislation is helpful and will provide reassurance to many schemes. However, trustees may want to understand whether there are exceptional circumstances in which fixed protections could be lost (see 1.3 below), taking legal advice as appropriate.

1.3 How do adjustments interact with fixed protection during a period of deferment?

(a) Loss of fixed protection as a result of benefit accrual⁶¹

Fixed protection 2012 will be lost if at any time there is an increase in the value of a member's defined benefit rights under an arrangement, occurring after the date when the fixed protection became effective and before the member's benefits come into payment, which exceeds the "relevant percentage".

Note:

- this isn't tested annually but is an "any point in time" test
- this is a test on prospective rights, so the testing ceases once the benefits come into payment (PTM093700⁶²); and
- parallel provisions apply for fixed protection 2014 and fixed protection 2016

(b) What is the "relevant percentage"?

The relevant percentage is defined, for the purposes of fixed protection 2012, in paragraph 14(13) of Schedule 18 of the Finance Act 2011. Broadly, in relation to a tax year, it means:

- (i) where the scheme rules provide for the value of the rights of the individual to increase at an annual rate specified in the scheme rules as they stood on 9 December 2010:
 - the percentage specified (**FP scheme rules limb**); plus
 - the "relevant statutory increase percentage"
- (ii) where the scheme rules provide for the value of the rights of the individual to increase at an annual rate specified by reference to the retail prices index in the scheme rules as they stood on 06 April 2012:
 - the percentage specified (**FP RPI scheme rules limb**); plus
 - the "relevant statutory increase percentage"⁶³
- (iii) if neither (i) nor (ii) apply:
 - the increase in the consumer prices index (**FP CPI limb**); or if higher
 - the "relevant statutory increase percentage"

Note: These limbs are alternatives, the relevant statutory increase percentage is not added to the FP CPI limb).

⁶¹ For more information on 'benefit accrual' under fixed protection, please see PTM093500, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm093500>

⁶² For more detail, please see PTM093700, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm093700>

⁶³ This applies to fixed protection 2012 only

(c) What is the "relevant statutory increase percentage"?

As explained in PTM093600⁶⁴, this is a "percentage increase in a member's rights under an arrangement which occurs during a tax year solely as a result of the application of certain statutory provisions". One of those statutory provisions is Section 67 of the Equality Act 2010.

(d) Will the adjustment to achieve GMP Equality exceed the "relevant statutory increase percentage"?

An adjustment implementing GMP equalisation (i.e. attributable solely to the application of Section 67 of the Equality Act 2010) can't exceed the relevant statutory increase percentage, because it forms part of the relevant statutory increase percentage.

This is the case regardless of whether a sex equality rule has been incorporated into the rules of the pension scheme under which the arrangement is held.

(e) Will the adjustment to achieve GMP Equality exceed the "relevant percentage"?

(i) Where at the relevant time either the "FP scheme rules limb" or the "FP RPI scheme rules limb"⁶⁵ applied (see **(b)** above):

- the definition of "relevant percentage" would include the relevant statutory increase percentage;
- as noted above, an adjustment implementing GMP equalisation would form part of the relevant statutory increase percentage; therefore
- an adjustment to achieve GMP Equality couldn't exceed the relevant percentage (and an individual who otherwise has fixed protection for a tax year should retain this protection).

(ii) Where at the relevant time the "FP CPI limb" applied, the adjustment to achieve GMP Equality could theoretically exceed the relevant percentage (and fixed protection could be lost). This is because (as noted in **(b)** above) the definition of "relevant percentage" doesn't provide for the "relevant statutory increase percentage" to be added on to the CPI measure in these circumstances.

1.4 How do adjustments interact with fixed protection when benefits are in payment?

(a) As noted at 1.3(a) above, the test for benefit accrual is a test on *prospective* rights, so the testing ceases once the benefits come into payment⁶⁶.

(b) Trustees may want to consider whether fixed protection had been lost *prior* to the original BCE2 (as a result of benefit accrual resulting from the implementation of the GMP Equality Adjustment); however, for the reasons set out at 1.3 above, such scenarios are expected to be rare.

⁶⁴ PTM093600, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm093600>

⁶⁵ This applies to fixed protection 2012 only

⁶⁶ For more detail on enhanced protection please see PTM093700, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm093700>

2. Enhanced protection

2.1 Enhanced protection generally

(a) Background⁶⁷

- (i) When the LTA was introduced with effect from 06 April 2006, individuals who had uncrystallised rights at 05 April 2006 could apply to HMRC for "enhanced protection" to protect them from the LTA charge when those rights come into payment after 05 April 2006.
- (ii) Enhanced protection is potentially very valuable. In principle, it protects all of a member's pre-06 April 2006 pension rights under tax approved pension schemes from an LTA charge but, in practice, the protection is more complex and — importantly — it can be lost in various ways.
- (iii) Under HMRC's approach of a "single BCE2", it's possible GMP equalisation has consequences for members with enhanced protection⁶⁸.

(b) Loss of enhanced protection

- (i) One of the ways in which enhanced protection can be lost is where the member has "relevant benefit accrual"⁶⁹ in any arrangement.
- (ii) Implementing adjustments to achieve GMP Equality won't necessarily result in relevant benefit accrual.
- (iii) For these purposes, there's relevant benefit accrual if the benefit value exceeds the "appropriate limit"⁷⁰ (which is broadly the value of benefit rights (as calculated under enhanced protection legislation) as at 5 April 2006, appropriately indexed).
- (iv) Whether there's been "relevant benefit accrual" is tested when there is a BCE or when there's a transfer out to an "other money purchase arrangement".
- (v) In particular, it's possible a benefit which was assessed to be within the "appropriate limit" when the original BCE2 occurred (prior to the equalisation of the benefit) is now assessed to have exceeded the "appropriate limit" once the effect of the equalisation is also allowed for.
- (vi) This would result in the loss of enhanced protection with effect from the date of the original single BCE2 (including for the purposes of the BCE).

⁶⁷ For more detail on enhanced protection please see PTM092410, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092410>

⁶⁸ Other approaches may also have an impact on enhanced protection.

⁶⁹ For more detail on 'relevant benefit accrual' please see PTM092430, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092420>, and PTM092430, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092430>

⁷⁰ For more detail on the appropriate limit please see PTM092430, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092430>

- (vii) The good news is, in many cases, there may have been sufficient 'headroom' to avoid an upward adjustment to the benefit value at the time of the original BCE2 resulting in the appropriate limit being exceeded.

Note: As stated in the First Newsletter, for these purposes, the value of a member's benefit rights under an arrangement as at 05 April 2006 needs to include the GMP Equality Adjustment valued at this date (which will likely add to the available headroom).

(c) Individuals who have been deferred members since before 06 April 2006

- (i) Section 4.3 of the First Newsletter states:

"For individuals who have been deferred members since before 6 April 2006 then any GMP equalisation benefit adjustments should not be 'relevant benefit accrual'.

- (ii) We would interpret this as helpful guidance suggesting that, if the indexation used in the test relies on the Registered Pension Schemes (Uprating Percentages for Defined Benefits Arrangements and Enhanced Protection Limits) Regulations 2006 (SI2006/130), any GMP equalisation benefit adjustments shouldn't be 'relevant benefit accrual'.
- (iii) However, if the administrator is using some other form of indexation for testing enhanced protection (e.g. the 5% p.a. margin) the exact number work will need to be considered.

(d) Individuals who have not been deferred members since before 06 April 2006

- (i) Section 4.3 of the First Newsletter states:

"Individuals who have not been deferred members since 6 April 2006 will have accrued benefits that with any GMP adjustments may result in relevant benefit accrual. When carrying out the relevant accrual calculations, the value of the member's rights under the arrangement as at 5 April 2006 needs to include the adjustment for GMP equalisation valued at that date."

- (ii) As noted in **(b)(iii)** above, there's relevant benefit accrual (and therefore a potential loss of enhanced protection) if the benefit value exceeds the "appropriate limit" (which is broadly the value of benefit rights (as calculated under enhanced protection legislation) as at 05 April 2006, appropriately indexed). Whether there's been relevant benefit accrual is tested when there's a BCE or when there is a transfer out to an "other money purchase arrangement".
- (iii) We expect it to be relatively rare that a GMP Equality Adjustment *alone* could result in the benefit value at the point of testing exceeding the appropriate limit. However, depending on the benefits accrued by the member since 06 April 2006, when considered as part of the wider calculation, the GMP Equality

Adjustment could result in the benefit value at the point of testing exceeding the appropriate limit. If so, enhanced protection would be lost.

3. Primary protection and individual protections

3.1 Background

(a) Primary protection

- (i) Where the value of an individual's rights exceeded £1.5 million as at 05 April 2006, they could apply to HMRC for primary protection⁷¹.
- (ii) Broadly speaking, an individual with primary protection is given a higher personal LTA than the SLTA. This is achieved by applying a factor to the member's SLTA at the time of the relevant BCE. The factor is calculated based on the extent to which the value of the individual's rights exceeded £1.5 million as at 05 April 2006.

(b) Individual protections

- (i) Where an individual had built up pension savings of more than:
 - £1.25 million as at 05 April 2014, a member could apply for individual protection 2014 (IP 2014); or
 - £1 million by 05 April 2016, a member could apply for individual protection 2016 (IP 2016).
- (ii) Broadly speaking, where an individual has:
 - IP 2014, their LTA is the lower of the value of their pension savings on 05 April 2014 and £1.5 million; or
 - IP 2016, their LTA is the lower of the value of their pension savings on 05 April 2016 and £1.25 million.

3.2 Level of protection

- (a) Section 4.2 of the First Newsletter says:

"GMP equalisation benefit adjustment could mean the value of rights protected are higher than originally notified to HMRC."

- (b) An adjustment for GMP Equality could mean the value of a member's benefits as at the relevant date (i.e. 05 April 2006 for primary protection, 05 April 2014 for IP 2014 or 05 April 2016 for IP 2016) was higher than the member previously appreciated. This is most likely to apply if the member had left contracted-out service before the relevant date⁷².

⁷¹ For more detail on primary protection, please see PTM092300, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092300>

⁷² If the member was still in contracted-out service on the relevant date, GMP Equality would have had no impact at that time, so there would be no adjustment to be made to the protected value of the member's benefits.

- (c) Trustees no longer have a statutory obligation to assist members in ascertaining the value of the member's benefits on the relevant date for these purposes. The adjusted value of the member's benefits as at the relevant date may be easy to ascertain if the scheme pension was already crystallised at this date, but otherwise the value may be very difficult to ascertain (potentially requiring complex calculations and the consideration of various legislative provisions and tax rules for what may only be a small uplift in the notional value of the member's benefits at the relevant date).

3.3 Changing the level of protection

(a) HMRC Guidance

Section 4.2 of the First Newsletter says:

"Individuals should notify HMRC of the corrected figure without undue delay. If the individual used the online notification process to protect their pension savings (Individual Protection 2016 only) they can amend the protection by accessing their personal tax account. Otherwise, they will need to tell HMRC in writing."

(b) Impact of a change in the level of protection

If such a correction is made, it could mean any LTA charge incurred in the past was overcalculated. The adjustment to the individual's LTA may be small (and therefore unlikely to result in any significant reduction in an LTA charge), so members may derive very little benefit from correcting the value of their benefits as at the relevant date.

3.4 Qualification for protection

(a) As a separate issue to the above, Section 4.4 of the First Newsletter states:

"Where GMP equalisation benefit adjustments result in an increase in value of the member's benefits, meaning the individual would qualify for protection from the lifetime allowance charge, the individual can approach HMRC with evidence to support their late notification."

(b) In the very unlikely event the increase in the value of a member's benefits as a result of the GMP Equality Adjustment means, on the relevant date, the value of the member's benefits would have been sufficient to allow the individual to register for protection⁷³ where they previously thought they weren't able to do so, such an individual can now (if they wish) approach HMRC with evidence to consider their claim⁷⁴. The individual should do so without undue delay once the individual is aware of the possibility.

(c) Primary protection

⁷³ For example, for primary protection, if an adjustment for GMP Equality takes the known value of a member's benefits as at 05 April 2006 above £1.5 million.

⁷⁴ see PTM098000, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm098000>

Ordinarily, an application for primary protection had to be made before 5 April 2009. However, there is a process for an application after this date in certain circumstances⁷⁵.

(d) IP 2014

We understand that, ordinarily, applications for IP 2014 had to be received by 5 April 2017. There's no late application process but there's a process of appeal as described in PTM098000, which needs to be implemented by the member urgently once they become aware an appeal is possible — additional delay may increase the likelihood HMRC reject an appeal.

(e) IP 2016

There's currently no deadline for an application for IP 2016.

(f) Impact of retrospective protection

If a member retrospectively obtains protection, it could mean any LTA charge incurred in the past was overcalculated.

⁷⁵ see PTM092300, <https://www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm092300>

APPENDIX 2 – TEMPLATE COMMUNICATION TO A MEMBER REGARDING THE NEED TO CONSIDER THE TAX EFFECTS OF RECALCULATED BENEFIT CRYSTALLISATION EVENTS

Drafting Note: This template is intended to provide example wording only. It does not cover all circumstances and will need to be tailored to reflect the circumstances in which it's sent.

It's only intended to be sent to a member whose pension commenced on or after 06 April 2006. Different wording will be required where a member's pension commenced prior to this date. Additional wording will be required if an additional PCLS is also being paid (i.e. to communicate the revised BCE6).

The wording assumes the member has already been informed of the GMP Equalisation Adjustment, subject to any lifetime allowance charge payable. If the member has not previously been informed of the GMP Equalisation Adjustment, amendments and additional wording will be required.

Drafting Note: Drafting notes, set out in red boxes like this one, should be removed prior to sending the letter.

Private & Confidential

Member Reference: <<MEMBER REFERENCE>>

<<TITLE>> <<INITIALS>> <<SURNAME>>

<<ADDRESS>>

<<POSTCODE>>

<<COUNTRY>>

Date: <<DATE OF LETTER>>

Dear <<TITLE>> <<SURNAME>>,

Guaranteed minimum pension ("GMP") equalisation:

Adjustment to your benefits and your lifetime allowance usage

Purpose of this letter

Drafting Note: The introductory wording will depend on the context in which the communication is sent (e.g. prior communications with the member in relation to GMP equalisation).

We write following previous correspondence regarding the GMP equalisation exercise the trustees have recently undertaken on [the XYZ scheme].

As the starting level of your pension has been adjusted, we have recalculated the percentage of your lifetime allowance which was used when your pension came into payment. The purpose of this letter is to explain the actions you may need to take as a consequence.

What is the lifetime allowance?

There is no limit on the total amount of pension benefits you can receive. However, everyone has a 'lifetime allowance' in relation to the value of benefits they can draw from all pension schemes (ignoring State pensions and pensions payable following the death of a member) without incurring additional tax.

When is lifetime allowance used?

Lifetime allowance can be used up in a number of different ways. The most common way is where an individual starts to draw a pension. A 'benefit crystallisation event' (or 'BCE') is the term used to refer to a situation in which lifetime allowance is used up.

What do I need to know?

- [Following a recent GMP equalisation exercise, the starting level of your pension (i.e. the level at your retirement date) was increased.
- Because the value of your pension at your retirement date was increased, we needed to retest it against your available lifetime allowance at your retirement date.
- We have recalculated the percentage of your lifetime allowance that was used when your pension came into payment.
- This may have tax implications (as set out in this letter), both in relation to the benefits paid by [the XYZ scheme] and, in certain cases, other arrangements.]

Keeping track of your available lifetime allowance

Each time a BCE occurs, the pension scheme administrator provides you with a statement showing the percentage of the lifetime allowance used up by the BCE. This information helps you keep track of your available lifetime allowance.

The percentage of your lifetime allowance being used up by a BCE is added to any percentage used up by previous BCEs (whether under the same scheme or a different scheme).

Lifetime allowance charge

If your pension savings being tested as at the date of a BCE exceed your available lifetime allowance at that point, a tax charge known as a 'lifetime allowance tax charge' is due on the excess.

In general, a lifetime allowance charge would only arise where you have significant pension savings.

Your pension benefits in [the XYZ scheme]

When you originally became entitled to your scheme pension, you experienced a BCE. The amount of your available lifetime allowance used up by the BCE is calculated by reference to the starting level of your pension.

Following the recent GMP equalisation exercise, the starting level of your pension (i.e. the level at your retirement date) was increased [and you were informed that an arrears payment would be made as a result of this adjustment].

The increase to the starting level of your pension means the amount of your available lifetime allowance used up by that BCE had to be recalculated.

The attached **Schedule** sets out:

- the revised starting level of your pension at your retirement date; and
- a revised figure for the percentage of lifetime allowance which was used when putting your pension into payment.

What does this mean for me?

Drafting Note: Select one appropriate paragraph from 1A to 1C below which reflects the knowledge of the member's lifetime allowance position and delete the others:

Section 1A: Available lifetime allowance at retirement date is currently unknown and benefits in scheme following adjustment are under 100% of the standard (or member's protected) LTA at date of retirement;

Section 1B: An LTA charge was paid in connection with the original BCE², therefore an additional LTA charge is due as result of the adjustment – assumes a 25% LTA charge to be deducted;

Section 1C: Benefits in scheme did not exceed standard LTA at retirement date, but do so following adjustment (this section assumes a 25% LTA charge is to be deducted in relation to the excess).

[It depends on your available lifetime allowance at your retirement date. Your retirement date is set out at **Section 1(b)** of the **Schedule**.

If the percentage of lifetime allowance which was used when putting your pension into payment (as shown in **Section 2** of the **Schedule**) exceeded your available lifetime allowance at this point, a 'lifetime allowance tax charge' is due.

How do I know what my available lifetime allowance was at my retirement date?

Broadly speaking, your available lifetime allowance percentage is 100% minus the percentage(s) of lifetime allowance used up by any BCEs which happened before your retirement date.

For example, if you only had one BCE in a different scheme — prior to your retirement date as set out at **Section 1(b)** of the **Schedule** — which used up 63% of your lifetime allowance, your available lifetime allowance at your retirement date is 37% (i.e. 100% - 63%).

Note for those with lifetime allowance protection: If we are aware of any lifetime allowance protection which you had in place at your retirement date, we have set this out as **Section 3** of the **Schedule**. **If, at your retirement date, you had any lifetime allowance protection which is not set out in the Schedule, please let us know.**

Note for those who had a pension under a different arrangement which commenced before 6 April 2006: The tax rules for pensions changed in 2006 and pensions which commenced before 6 April 2006 weren't tested against lifetime allowance (so you won't have been given a statement showing the percentage of the lifetime allowance used up by that pension being put into payment). However, any such pension would have reduced the amount of your available lifetime allowance at your retirement date as set out at **Section 1(b)** of the **Schedule**.

[In general, unless your current total pension benefits in payment (across all schemes) are at least £ **[INDICATIVE FIGURE TO BE INSERTED BY SCHEME]** a year, you are unlikely to be affected].

What do I need to do?

If you believe the percentage figure in **Section 2** of the **Schedule** (i.e. the revised percentage of lifetime allowance used when putting your pension into payment at your retirement date) might exceed the lifetime allowance which you had available at your retirement date **please contact us before [dd/mm/yyyy]** with details of the lifetime allowance you had available at your retirement date (including the details of any pension which commenced before 6 April 2006).

We will then calculate any tax charge to be paid to HMRC and re-calculate the adjustment to your pension **[and the arrears due]**.

If we do not hear from you by [dd/mm/ccyy], we will assume you had enough available lifetime allowance at your retirement date and will pay your increased pension [and the arrears due] [ADD DETAILS OF EXPECTED DATES OF SUCH PAYMENTS].

Drafting Note: Section 1B

[As you know, at your retirement date, the value of your pension benefits was in excess of your available lifetime allowance and a lifetime allowance tax charge was paid to HMRC in respect of the excess.

Following the increase to the starting level of your pension, a further lifetime allowance charge of [£X.XX] is due in respect of your benefits in [the XYZ scheme].

We have made arrangements for the tax charge to be paid to HMRC and this has been taken into account in the revision to your benefits [and any arrears payable]. The details will be set out in a future communication.

The revised level of your starting pension set out at **Section 1(a)** of the **Schedule** reflects the adjustment made.]

Drafting Note: Section 1C

[Following the increase to the starting level of your pension, the recalculated value of your benefits at your retirement date (as set out at **Section 1(b)** of the **Schedule**) now exceeds your available lifetime allowance on your retirement date.

This means a lifetime allowance charge of <<£AMOUNT>> arises on the value of the benefits in excess of [the standard/your protected] lifetime allowance at your retirement date in respect of your benefits in [the XYZ scheme].

We have made arrangements for the tax charge to be paid to HMRC and this has been taken into account in the revision to your benefits [and any arrears payable]. The details will be set out in a future communication.

The revised level of your starting pension set out at **Section 1(a)** of the **Schedule** reflects the adjustment made.]

Drafting Note: The above text deals with the consequences of an adjustment to the starting pension. The following text relates to the impact the adjustments have had on the pension once it is in payment.

Section 2A addresses the scenario in which, once the GMP equalisation adjustments are taken into account, a BCE₃ previously treated as having arisen did not arise, or where the amount crystallised was less than previously identified.

Section 2B addresses the scenario in which, once the GMP equalisation adjustments are taken into account, a new BCE₃ has been identified.

[Impact of GMP equalisation adjustments on increases occurring after the pension commenced

We also want to address the impact of GMP equalisation adjustments on increases which have been applied to your pension after your pension commenced.

Where your pension, once in payment, increases by more than a permitted margin (broadly speaking, the greater of 5% a year and the increase in price inflation since your pension first became payable), a further BCE arises at that point.

The amount of your available lifetime allowance used up by the BCE is calculated by reference to the extent to which the increase exceeds the permitted margin.

If you don't have enough available lifetime allowance, a lifetime allowance charge becomes payable.

Drafting Note: Section 2A

[In <<YEAR>> you were informed that, as a result of increases applied to your pension, a BCE had arisen.

However, as part of the GMP equalisation exercise, we have recalculated all subsequent increases to your pension in payment.

[WHERE NO BCE₃ AROSE]

[This process has identified the increase to your pension in <<YEAR>> no longer exceeded the permitted margin, meaning no BCE arose as a result of the increase. [WHERE AN LTA CHARGE WAS PAID IN ERROR] This means no lifetime allowance charge should have been paid at the time. We will write to you separately in this regard. If, after <<YEAR>>, a lifetime allowance charge became payable in relation to another arrangement, you may want to advise the administrators of that arrangement of the revised percentage set out in **Section 4**, as it may reduce the lifetime allowance charge which arose under that arrangement.]

[WHERE A BCE₃ AROSE, BUT THE AMOUNT CRYSTALLISED WAS LOWER THAN PREVIOUSLY THOUGHT]

[This process has identified the increase to your pension in <<YEAR>> which resulted in the BCE was lower than previously thought and, as a result, the percentage of [the standard/your protected] lifetime allowance used up as a result of this BCE is lower than previously identified. The revised percentage is set out in **Section 4** of the **Schedule**. [WHERE AN LTA CHARGE WAS PAID/OVERPAID IN ERROR] Based on our understanding of your [the standard/your protected] lifetime allowance at that time, this means [no/a lower] lifetime allowance charge should have been paid at that time. We will write to you separately in this regard. [WHERE THERE IS UNDERSTOOD TO BE AVAILABLE LTA AFTER THE REVISED BCE₃] If, after <<YEAR>>, a lifetime allowance charge became payable in relation to another arrangement, you may want to advise the administrators of that arrangement of the revised percentage set out in **Section 4**, as it may reduce the lifetime allowance charge which arose under that arrangement.

Drafting Note: Section 2B

[Additional BCE after your retirement date

As part of the GMP equalisation exercise, we have recalculated all increases to your pension since it came into payment.

This has identified an increase beyond the permitted margin occurred as at <<DD/MM/CCYY>>, resulting in a BCE.

The percentage of [the standard/your protected] lifetime allowance used up as a result of this BCE is set out in **Section 4** of the **Schedule**.

If the percentage of the available lifetime allowance you had available at <<DD/MM/CCYY>> was less than the percentage figure set out in Section 4 of the Schedule, please contact us before [dd/mm/yyyy] with details of the lifetime allowance you had available at <<DD/MM/CCYY>>.

Broadly speaking, your available lifetime allowance at that time was 100% minus the percentage(s) of lifetime allowance used up by any BCEs which happened before that date.]]

Drafting Note: The section below is intended to make the member aware as to whether they should be contacting the administrators of other registered pension arrangements. Either Section 3A or Section 3B is to be used.

Section 3A is to be used where an LTA charge previously arose in relation to the original BCE2.

Section 3B is to be used where no LTA charge arose in relation to the original BCE2.

Your pension benefits in other registered pension schemes

As noted above, the lifetime allowance limits the value of benefits you can draw from all pension schemes (ignoring State pensions and pensions payable following the death of a member) without incurring additional tax. Therefore, an increase in the amount of lifetime allowance used up by BCEs under the [the XYZ Scheme] means there is less available lifetime allowance for subsequent BCEs which arise under any other pension schemes in which you participate.

Drafting Note: Section 3A

[As the value of your benefits in [the XYZ Scheme] at your retirement date was already in excess of your available lifetime allowance at that date, it will not be necessary to inform other schemes of the adjustment in your starting pension, as the adjustment would not result in additional tax to pay in respect of those schemes.]

Drafting Note: Section 3B

[If:

- your total pension and lump sum benefits crystallised to date might exceed your lifetime allowance;
- you have pension benefits in another pension scheme; and
- a BCE has occurred in that pension scheme after the retirement date set out in **Section 1(a)** of the **Schedule** (e.g. a pension was put into payment, in that scheme, after that date),

you may need to let that pension scheme know the revised percentage of the lifetime allowance used up at your retirement date (as set out in **Section 1(b)** of the **Schedule**) [and any changes in respect of BCEs occurring after the retirement date as set out in **Section 4** of the **Schedule**] so the scheme can check whether the changes have any impact on the benefits under that scheme.

You may wish to use the **Schedule** to inform another scheme of the changes in your lifetime allowance position.]

Amending your self-assessment tax return

For any year in which a lifetime allowance charge is payable (or there is an increase in the level of lifetime allowance charge payable), you will need to report this to (or update) HMRC on your self-assessment tax return for the relevant tax year(s).

Drafting Note: The following text is to be tailored according to other communications to be sent to the member.

[Arrears of pension from your retirement date

If, following the adjustment to your pension, you are entitled to a higher pension from your retirement date, we will provide details of any arrears you may be due in a separate letter.]

Kind regards

[Administrator name]

Schedule

1. Revised level of starting pension

- (a) The revised level of your pension as at your **retirement date** is <<£AMOUNT>> per annum.

(b) Your **retirement date** for these purposes is <<DD/MM/CCYY>>.

2. Revised lifetime allowance usage

As a result of the change in the level of your pension as at your retirement date, the percentage of lifetime allowance used when putting the pension into payment has also been revised.

The revised figure is <<X.XX%>> of [the standard/your protected] lifetime allowance for the <<CCYY/CCYY>> tax year (this is an increase from the figure of <<X.XX%>> that was previously communicated to you).

3. Lifetime allowance protections

[EITHER]

[The Trustee's records show that, at your retirement date, you had [INSERT KNOWN LIFETIME ALLOWANCE PROTECTIONS].

[OR]

[The Trustee is not aware that you had any lifetime allowance protections in place at your retirement date.]

Drafting Note: The following text is to be included if there has been a previous BCE₃ – and the adjustment to the starting level of the pension means the BCE₃ has changed (or is no longer applicable).

4. BCEs in the [XYZ scheme] following your retirement date

[EITHER (WHERE THERE IS AN AMENDMENT TO AN 'OLD' BCE₃)]

The revised figure for the percentage of [the standard/your protected] lifetime allowance used by the BCE which occurred on <<DATE OF INCREASE RESULTING IN A BCE>> is <<X.XX%>>.

[OR (WHERE THERE IS A NEW BCE₃)]

The percentage of [the standard/your protected] lifetime allowance used by the BCE which occurred on <<DATE OF INCREASE RESULTING IN A BCE>> is <<X.XX%>>.

APPENDIX 3 – TEMPLATE COMMUNICATION TO A MEMBER INCORPORATING AN ARREARS SCHEDULE (WHICH COULD BE FORWARDED, BY THE MEMBER, TO HMRC)

Private & Confidential

[Title] [Initials] [Surname]

[Address]

Postcode

Dear [Title] [Surname],

I write following previous correspondence regarding the GMP equalisation exercise the trustees have recently undertaken on [the XYZ scheme].

It has been determined you are due [£X.XX] (before tax and excluding interest) which represents the amount of pension you have been underpaid. The payment will be made as a one-off lump sum on [dd/mm/ccyy].

This payment may mean you are taxed at a higher rate than you would have been had the underpayments been paid in each of the tax years when they were due.

If this affects you then please send a copy of this letter to the following address:

Pay As You Earn and Self Assessment
HM Revenue and Customs
BX9 1AS
United Kingdom

HMRC will then be able to work out whether there has been an underpayment or overpayment of tax.

Tax year to which the payment relates	Additional amount which should have been paid (before tax and excluding interest)
20XX/YY	£X.XX
20XX/YY	£X.XX
20XX/YY	£X.XX
20XX/YY	£X.XX
20XX/YY	£X.XX
20XX/YY	£X.XX
Total	[£X.XX]

Note to HMRC: Section 6 of HMRC's Guaranteed Minimum Pension (GMP) equalisation newsletter published 20 February 2020 states members can contact HMRC to claim the correct tax treatment relating to an arrears payment (see EIM74103).

Kind regards

[Administrator name]



PASA 
assess | aspire | achieve

THE PENSIONS ADMINISTRATION STANDARDS ASSOCIATION

Get in touch:

info@pasa-uk.com

www.pasa-uk.com