GMP equalisation – employers required to reflect cost now

A chance to avoid overestimates and remove complexity for good

At a glance

It has taken 28 years and the judgment in the Lloyds case to confirm that overall pension benefits must be improved to remove Guaranteed Minimum Pension (GMP) inequalities between men and women.

This means higher benefits for some members and therefore higher costs.

Companies and trustees now need to work together to allow for this. Suitable methods differ in terms of cost and complexity. Helpfully these include one method to simplify benefits by removing GMPs – but employer consent is needed.

This cost will need to be allowed for in the next accounts and is likely to be charged to P&L. It will be important to avoid overestimates.

Pragmatism is needed for funding valuations – for most schemes the impact will be manageable.

What is the cost?

Not all GMP equalisation methods are equal

The case looked at a number of methods (called methods A to D). The D methods provide equivalent actuarial value. D2 removes GMPs altogether and employer consent is needed. This will prevent unnecessary future costs.

Possible accounting treatment

Broad estimates commonly put equalisation costs at 1% to 3% of total pension liabilities. But in practice we have seen schemes where the impact is lower than 1%.

<table>
<thead>
<tr>
<th>Possible accounting treatment</th>
<th>Charge</th>
<th>Likelihood</th>
</tr>
</thead>
<tbody>
<tr>
<td>Past service cost</td>
<td>Through P&amp;L with adjustments in later years charged to OCI Risk that future judgments impact P&amp;L</td>
<td>More likely – unless schemes have made an explicit allowance in the past</td>
</tr>
<tr>
<td>Re-measurement/assumption change</td>
<td>Through OCI</td>
<td>Less likely unless previous allowance made in accounts. Evidence of approach and best estimate calculation is expected to be required</td>
</tr>
</tbody>
</table>

Actions employers can take

For those schemes with GMPs there are three short-term actions you can take.

1. Engage with your trustees to set out your initial thoughts on equalisation method in order to minimise cost and ensure you obtain the best outcome.
2. Obtain the high-level data required to calculate a robust estimate of your accounting charge quickly.
3. Armed with the above, agree treatment with your auditor.
A silver lining?

Exploring the opportunity to remove your GMPs once and for all can create the opportunity to simplify benefits and reduce future administration and long-term exit costs.

Whilst clearly unwelcome news for employers from a cost perspective, is the silver lining the opportunity to embrace the change and remove GMPs once and for all?

GMP conversion and benefit simplification will allow employers and trustees to avoid unnecessary ongoing administration burdens and cost.

Act Now

We are working with our clients using our XPS GMP Cost Calculator, a model we have developed to provide initial pragmatic accounting estimates so please get in touch with us as we can help you understand and manage this now.

For further information, please get in touch with Louisa Taylor or Helen Ross or speak to your usual XPS Pensions contact.

© XPS Pensions 2018. XPS Pensions is the trading name of Xafinity Consulting Ltd and Punter Southall Ltd. Registration: Xafinity Consulting Ltd, Registered No. 2459442. Registered office: Phoenix House, 1 Station Hill, Reading RG1 1NB. Punter Southall Ltd, Registered No. 03842603. Registered office: 11 Strand, London WC2N 5HR. All companies registered in England and Wales. This communication is based on our understanding of the position as at the date shown. It should not be relied upon for detailed advice or taken as an authoritative statement of the law. Part of XPS Pensions Group