Which GMP equalisation method should you choose?

At a glance

By now, most employers have accounted for GMP equalisation. But you remain at the forefront of decision making – your consent is needed for most equalisation methods.

Some methods may suit employers’ objectives better than others, for example methods that are lower cost or facilitate new member options.

However, the liability cost may not be that different between methods – our research shows very small differences for most schemes.

The small difference in cost means other factors may drive decisions, such as reducing complexity and supporting long term objectives.

If you might insure in the future, bear in mind some insurers have a strong preference for equalisation using conversion of benefits.

Comparison of liability cost

The table below compares GMP equalisation costs across the methods for affected pension only. For example the average C1 cost is 0.10% higher than D.

This is based on 250,000 scenarios covering most scheme circumstances. Cost as a percentage of total liability will be around a quarter of the figures below.

<table>
<thead>
<tr>
<th>Average extra liability compared with conversion (Method D)</th>
<th>Method B</th>
<th>Method C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Best of both worlds each year</td>
<td>0.55%</td>
<td>C1: 0.10%</td>
</tr>
<tr>
<td>Range of extra liability compared with conversion (Method D)</td>
<td>0% – 17%</td>
<td>C1: 0% – 6%</td>
</tr>
</tbody>
</table>

b) Total scheme liabilities will include pensions earned outside 17/5/1990 and 5/4/1997.

Recap of GMP equalisation methods

1. Adjustments to ongoing payments

   - Better than both worlds
     - Methods A1, A2 and A3 give each sex the higher of every payment and increase separately.
   - Best of both worlds each year
     - Method B gives each sex the higher total pension each year.
   - Best of both worlds overall
     - Methods C1 and C2 give each sex the same overall value of benefits.

   Given it seems unlikely that schemes will pursue Method A, focus is on Methods B, C1 and C2.

2. Conversion of GMP into non-GMP benefit (Method D)

   This could be a silver lining in the equalisation process, as conversion could be used to create a simpler future benefit structure and increase member engagement.

   For more information click here.

Actions employers can take

1. Engage with your trustees to get involved early in decisions on GMP equalisation.
2. Understand the difference in liability cost between equalisation methods for your scheme and see if this provides you with flexibility.
3. Identify other important factors to consider, e.g. future administration complexity.
4. Consider the opportunities offered by conversion to simplify benefits, offer new member options and increase engagement with members.
What other factors should you consider?

Where the difference in liability cost between equalisation methods is small, there are a number of other factors that become important. The table below compares the relative significance of these factors for each equalisation method.

<table>
<thead>
<tr>
<th></th>
<th>Method B: Best of both worlds each year</th>
<th>Method C: Best of both worlds overall</th>
<th>Method D: Conversion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liability cost</td>
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<td>Data requirements</td>
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<td>Complexity of equalisation project</td>
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<td>Complexity of ongoing administration</td>
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<td>Impact on member options and engagement</td>
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<td>Future retirement communications</td>
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<tr>
<td>Preferred for future insurance</td>
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<td>Employer consent required?</td>
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For further information, please get in touch with Vicky Mullins or Victoria Pullan or speak to your usual XPS Pensions contact.


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