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# Sixty second summary

## GMP equalisation: tax effects of transfer top-ups & conversion

Her Majesty's Revenue and Customs (HMRC) has published a new *Guaranteed Minimum Pension (GMP) Equalisation Newsletter*, covering issues that arise when scheme administrators take corrective action in connection with historical transfers, and providing an update and guidance for those who convert GMPs into ordinary scheme benefits after equalisation.[1]

## Historical transfers

### Transfer top-ups

Most top-up transfer payments will be 'recognised transfers' and therefore authorised member payments for tax purposes. It is notable, however, that the receiving scheme must be a registered pension scheme or a qualifying recognised overseas pension scheme (QROPS) *when the top-up is paid*.

### Lump-sum payments

A lump-sum payment made to the member in lieu of a transfer top-up may also be an authorised member payment, if the necessary conditions are met. The *Newsletter* discusses several of the small lump sums, and winding up lump sums.

#### Payment following 'relevant accretion'

A commutation payment not exceeding £10,000 could be paid after a '*relevant accretion*' (the calculation of the GMP-equalisation uplift), provided that the historical transfer was to a registered pension scheme or QROPS. Unfortunately, this means that pre-A-day (6 April 2006) transfers are excluded, as there were no RPSs or QROPSs then. The scheme administrator must not have been aware (or reasonably expected to have been aware) of the member's entitlement to an additional benefit at the time of the original transfer. The *Newsletter* indicates that this condition will be satisfied if the administrator did not then know the specifics of the transferring member's GMP-equalisation uplift entitlement. Whilst the lump sum must be paid within six months of the 'relevant accretion', HMRC does not regard that period to have begun until the lump-sum amount, member's whereabouts, and other details such as banking information have been established.

#### Other small lump sums

Occupational pension schemes can pay other small lump sums of up to £10,000. Notably, though, it is a condition of such payments that there cannot have been a recognised transfer from the scheme (or, in some cases, any other scheme related to the same employment) in respect of the member during the three years preceding the date of the lump-sum payment.

#### Taxation

If lump sum payments are made directly to members, or to their estates after their deaths, to extinguish their rights to top-up transfer payments, they will be considered to be payments in respect of uncrystallised rights, so that 25 per cent of the lump sum will be tax-free. Where an authorised lump sum is payable to another individual following the member's death (rather than being owed to the member and payable to the estate), the lump sum will be wholly taxable. Tax is due in the tax year in which the lump sum is paid, and PAYE should be operated on the lump sum.

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[1] *Guaranteed Minimum Pension Equalisation Newsletter—April 2022* <www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-april-2022/guaranteed-minimum-pension-equalisation-newsletter-april-2022>.

There should be no additional annual allowance consequences of making a top-up transfer payment or paying a lump sum in lieu.[2] Nor should a top-up or lump sum endanger the 'block transfer' status of the original transfer, for transitional-protection purposes. However, an additional transfer payment could result in a loss of fixed or enhanced protection if it is not a '*permitted transfer*': transfers to money-purchase schemes will be safe in most cases, but there are limited circumstances in which transfers to DB schemes are *'permitted*'.

## GMP Conversion

### Pre-retirement

When conversion occurs pre-retirement, the *Newsletter* says that there can be annual-allowance effects both in the tax year of conversion and in all subsequent years up to and including the year of retirement. In particular, there is a risk that early leavers will lose the benefit of the ‘deferred member carve out’ that usually means that they are treated as though their pension rights did not increase in value during the tax year. Members may also lose fixed protection from the lifetime allowance. Further work—and possibly legislative change—is required.

### Pensioners

There are no annual-allowance consequences if conversion occurs after the tax year of retirement. Fixed protection is not endangered by conversion of a pension in payment provided the member’s rights in the arrangement have been fully crystallised. The lifetime allowance test for benefit crystallisation event (BCE) 3—which applies when pensions in payment increase beyond certain levels—should be done as though the member was always entitled to the equalised benefits.

### Recent retirees

Conversion after, but in the same tax year as retirement does not constitute benefit accrual for AA purposes, and does not affect the deferred member carve-out determination, even if the resulting increase in pension triggers a BCE3 tax charge. Again, the BCE3 test should be done as though the member was always entitled to the equalised benefits.

### Pre-A-day leavers

Members who left service before 6 April 2006 should remain outside of the scope of the annual allowance so long as conversion does not increase the actuarial value of their benefits.

The court judgment on the implications for historical transfers has created new tangles that have to be carefully teased out, especially when a top-up transfer payment cannot be made. The ability to pay lump sums (and have part of it tax-free) in suitable circumstances will be helpful.

There was doubt until very recently that guidance on the tax implications of GMP conversion would be forthcoming, so we are pleased to see the *Newsletter* and to learn that additional guidance can be expected. The message is, unsurprisingly, that the issues involved are complex. It seems likely that legislation will be needed to resolve some of the complications, such as the potential for loss of valuable protections. The indications are that HMRC wants to work with industry bodies to achieve appropriate outcomes, and for that it should be applauded.

[2] The annual allowance implications of GMP equalisation benefit adjustments were discussed in *Guaranteed Minimum Pension (GMP) Equalisation Newsletter—February 2020* <www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020>.