

Sixty second summary

HMRC pragmatic (so far) on GMP-equalization tax issues

Her Majesty's Revenue and Customs (HMRC) has published a first instalment of guidance on the tax issues arising from equalization of pension rights for the discriminatory effects of guaranteed minimum pensions ('GMP equalization').¹ Equalization-driven increases will not be treated as 'accrual', and so will not need to be tested for annual allowance purposes, or cause loss of lifetime allowance protections. Nevertheless, there are complications to be managed, and issues - most glaringly concerning GMP conversion - that are yet to be addressed.

HMRC's general approach

The broad message is that, for tax purposes, a pension increase resulting from GMP equalization is attributable to membership between 17 May 1990 (the date of the Barber judgment) and 5 April 1997 (when GMP accrual stopped, across the board), rather than an entirely new entitlement to benefits. HMRC has therefore concluded that an equalization increase will not by itself constitute fresh accrual for annual or lifetime allowance purposes. That means that it should not generate annual allowance charges or trigger loss of lifetime allowance protections; it will, however, affect the amounts crystallized for lifetime allowance purposes by past and future benefit crystallization events.

Annual allowance

increases that are purely the result of GMP-equalization adjustments will not

- bring those who were deferred members at the inception of the current tax regime (on 6 April 2006) and have remained so ever since within range of the annual allowance system;
- mean that members who became deferred on or after 6 April 2006 lose the benefit of the 'deferred member carve-out'; or
- necessitate the recalculation of historical pension input amounts for other members.

The opening and closing values for the tax year in which benefits are adjusted (and subsequent tax years) will have to reflect the member's equalized pension. The two values will effectively cancel each other out, so that no-one will be subject to an annual allowance charge purely as a result of GMP equalization.

Lifetime allowance

Protections

Similarly, GMP equalization adjustments ought not to invalidate the various flavours of lifetime allowance protection. However, the value of the rights protected will have to be revisited if a member has primary, individual or (in some cases) enhanced protection. For primary and individual protection, where HMRC has been provided with a figure for the protected amount, the member will need to update the value of the pension savings at the relevant date to take account of any increase. Some members (the newsletter suggests the category is restricted to those with 'individual protection 2016') will be able to do so via their online personal tax accounts; others will need to write to HMRC.

¹ *Guaranteed Minimum Pension (GMP) equalization newsletter - February 2020* <www.gov.uk/government/publications/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020/guaranteed-minimum-pension-gmp-equalisation-newsletter-february-2020>.

Broadly speaking, enhanced protection is lost, in a DB arrangement, when the value of the benefits paid or transferred exceeds that of the benefits on 5 April 2006, but with an allowance for indexation or salary increases since that date. Equalization increases will affect both values. Calculations for members who have accrued benefits since 5 April 2006 will need to be reconsidered in light of equalization (those who have not should be unaffected).

Where the result of equalization increases is such that a member would, with hindsight, have qualified for some form of lifetime allowance protection, HMRC will in some circumstances accept a late claim.²

Benefit crystallization events (BCEs)

Equalization increases will inflate the amounts crystallized in, and therefore the running total of the member's lifetime allowance used up by, past and future BCEs. A member who has already had a BCE may in retrospect be found to have incurred a lifetime allowance charge (LAC), or a higher LAC. Some members who previously expected to be able to take their benefits without incurring charges may now find that that is no longer true.

The annual lifetime-allowance statements provided to pensioner members will, following equalization increases, have to be revised to show the (higher) percentage of the lifetime allowance used up by the equalized pension.

Scheme administrators will need to amend historical Accounting for Tax returns and Event Reports if equalization increases mean that—in hindsight—the amounts reported were too low, or that reports that should have been made were not. They can apply to be discharged of their liability to a LAC where they reasonably believed that none was due (or thought that the LAC was lower than it turned out to be), and it would not be just and reasonable in the circumstances for them to be liable. The newsletter says that it is not possible for HMRC to say in advance whether the application for discharge will be successful.

Scheme members may need to update past self-assessment tax returns to reflect the correct LAC position.

Pensioner payroll operators will need to deduct income tax, in accordance with the PAYE rules from any arrears of pension paid as a lump sum. This may result in overpayment of tax, in which case the pensioner will need to contact HMRC and supply details of the historical underpayments and the tax years to which were attributable, in order to have their tax corrected. Interest on the arrears will be a scheme administration member payment, which is an authorized member payment; the newsletter appears to suggest that such interest should be paid net of tax.

Still awaited

The guidance in the newsletter is concerned only with increases that are made directly to equalize for GMP differences. It does not cover any other benefit adjustments that might be made in association with an equalization exercise, for example where GMP is converted into other benefits of equal value following equalization. Work on the tax implications of conversion, as well as on payments such as trivial commutation lump sums and death benefits, is ongoing.

The Revenue's general position on GMP equalization increases is sensible and reflects the legal view that members have been entitled to equalized benefits for service since 17 May 1990. It appears that there should be no adverse annual-allowance consequences or invalidation of lifetime allowance protections. However, the administrative demands of revisiting BCEs and ensuring that the correct tax has been paid should not be underestimated. Note that there is no suggestion of the possibility of members applying to be discharged of their LAC liabilities, where these arise or are increased.

Note also that this newsletter deals only with cases in which a 'year-on-year' ('dual-records') approach to equalization is taken. Many schemes are leaning instead toward using GMP conversion to resolve the issue. Her Majesty's Revenue and Customs has yet to advise on the tax repercussions of that route.

² Readers are directed to the *Pensions Tax Manual* <www.gov.uk/hmrc-internal-manuals/pensions-tax-manual/ptm098000> for details.