FAQs on the calculation of PPF compensation for the effect of Guaranteed Minimum Pensions (GMPs)

1. What's GMP?

Guaranteed Minimum Pensions (GMPs) are a defined benefit underpin broadly equal to SERPS (the State Earnings-Related Pension Scheme) which must be provided by schemes if they contracted out of SERPS.

They were introduced with contracting out in 1978, and could accrue up to 5 April 1997 when contracting out arrangements were changed.

Both defined benefit (DB) and (otherwise) defined contribution (DC) schemes could contract out and commit to pay GMPs.

Our Statement only relates to the calculation of PPF compensation for DB pension schemes that have entered PPF assessment and for the calculation of FAS assistance for affected FAS eligible schemes. It is not intended for schemes that remain outside of the PPF.

2. So, what are you doing?

The Board has for some time been looking at the treatment of GMP for PPF compensation. Since becoming FAS Scheme Manager in July 2009 the Board has also been considering how the statutory requirements in relation to equality also apply to FAS assistance payments.

The latest consultation response and technical Statement set out the Board's method for making this calculation for PPF/ FAS.

3. What's the underpin method?

The underpin method is the way in which the PPF will calculate compensation and assistance to take account of the effect of GMPs on member benefits. It works by testing when the GMP element of a member's benefits met the minimum statutory requirements. For example: adjusting the calculation of those benefits payable for a man at age 60 depending on whether the minimum has been met already or if it will be covered in future (e.g. at age 65).

4. How much difference will this make to members' benefits?

For nearly all members the change will have a very small impact on their overall compensation or assistance; the exact amounts will of course depend on their individual circumstances. For example, some PPF members could see some parts of their compensation coming into payment earlier than it would otherwise have done.

5. **Will anyone see their compensation reduced as a result?**

   Nobody will receive less than the PPF compensation they are entitled to.

6. **If the impact is small why are you doing this?**

   We are legally obliged to do this – we have no choice.

7. **Will people who will benefit receive retrospective payments?**

   Yes. (We will make payments to members of Transferred schemes as soon as practicable.)

8. **Is using PPF resources on this a good use of levy payers' money? Is this a good use of tax-payers' money for FAS schemes?**

   It is something we (and all schemes) have to address by law.

9. **Why has it taken so long to come up with a solution?**

   It is a very complex area. The issue first arose 18 years ago and to date there has still been no industry consensus.

   We have devised a solution for the calculation of PPF and FAS compensation/assistance. We appreciate that schemes outside of our processes may choose to take alternative approaches.

10. **Will it mean that schemes will spend longer in assessment while they adjust calculations for GMP for their members?**

    Trustees of schemes in a PPF assessment period that are expected to transfer to the PPF before the end of the pilot study are not expected to calculate compensation taking account of equalisation for GMPs and the Statutory Minimum prior to transfer. The PPF will adjust compensation for members of such schemes following transfer to the PPF using the approach set out in the Statement. This will avoid any delay in transferring such schemes to the PPF that would otherwise result from undertaking such calculations late in the assessment process.

We are undertaking a six month pilot study in order to determine the most effective way to implement the approach on a wider basis. Once the pilot study is completed we will issue guidance to all schemes about our plans for wider implementation; Minimising any delay in the assessment period will be a key factor in determining our approach.

11. Do you now expect other UK pension schemes to follow your lead?

This proposal only relates to pension schemes in a PPF assessment or affected FAS schemes in wind-up. We are not seeking to set an industry standard. It is up to schemes to decide how they calculate their benefits for the effect of GMPs.

12. Why aren't UK pension schemes equalising for GMPs in the same way?

That is a matter for the trustees and employers.

13. If it increases scheme liabilities does it mean less money coming into the PPF once schemes transfer?

The obligation exists for schemes in assessment and those that transfer. There is, of course, a cost for performing any adjustments but this is a legal requirement which we (and schemes) are obliged to fulfil.

14. Could it prevent a scheme being rescued or being wound-up outside the PPF as it can no longer pay benefits greater than PPF levels of compensation?

We do not expect this change to have an impact on rescues or on schemes' ability to wind-up outside of the PPF. Schemes with section 143 valuations with funding levels greater than PPF levels of benefits will be expected to confirm that if GMPs had been equalised the scheme would still be overfunded on a PPF basis.

15. If it is such a complex process, will trustees be equipped to do this work successfully?

We believe that our approach can be carried out successfully. To ensure that we adopt the most effective approach we are running a pilot study to test whether there are any practical issues that we will need to address before applying it more widely.

16. Why are you running a pilot study?

We have always recognised that carrying out calculations for GMP equalisation is complicated, and will have practical challenges (i.e. around data etc). We are therefore testing some of these issues with a pilot study before the approach is implemented more widely.

For clarity, we are not re-opening our Statutory Underpin calculation method for consultation. The pilot study relates to the practicalities of its implementation.

17. Who is in the pilot study? Can I become a pilot study member?

We have selected a mix of schemes in assessment to take part in the pilot study. If your scheme has been selected your trustee will have already been informed.

18. How long will the pilot study be? What about other schemes in PPF assessment? What are the schemes in the pilot study doing?

It is expected that the pilot study will run for six months. Following its conclusion we will publish guidance for all schemes setting out how we expect them to implement the calculation methodology.

Schemes that are not in the pilot study should continue to progress their scheme through assessment as normal.

Pilot schemes are testing whether there are any practical challenges applying the methodology we have set out in our Statement.

19. Will the levy increase as a result of this proposal?

The Board has recently confirmed the levy for 2011/12 at £600m and (separately) set out its plans for the future of the levy. The adoption of the GMP proposals – in itself – will not affect this position.

20. When will DWP's revised equalisation guidance be issued?

This is a matter for DWP.

22. Have DWP approved your guidance?

We have developed our proposals taking account of Government statements on the requirement to equalise and we have notified Government of the methodology we intend to use. We are confident that any amendments to legislation will not alter our approach.

23. Your consultation finished in March – why did it take so long to issue this statement.

In response to our consultation we received a number of highly technical queries – some of which have required further investigation. To aid stakeholders we have sought to address all of these queries in our response and technical Statement.