

REPORT OF THE GROUP DIRECTOR, FINANCE & CORPORATE RESOURCES

Guaranteed Minimum Pensions (GMP) Reconciliations Update	Classification PUBLIC	Enclosures One (Exempt)
	Ward(s) affected ALL	AGENDA ITEM NO.
Pensions Committee 29th March 2017		

1. INTRODUCTION

- 1.1 This report provides the Pensions Committee with an update on the Fund's GMP reconciliation (Guaranteed Minimum Pensions) exercise, which is being undertaken to ensure that scheme member records for periods spent contracted out of the second state pension are properly accounted for. The report provides an update on the progress of Phase 1 of the reconciliation exercise and outlines factors for consideration before the Fund embarks on Phase 2

2. RECOMMENDATIONS

- 2.1 **The Pension Board is recommended to consider granting formal approval for the commencement of Phase 2, subject to the regular review of estimated costs as set out in Appendix 1 to this report.**

3. RELATED DECISIONS

- Pension Board 20th March 2017 – GMP Reconciliations
- Pension Board 26th January 2016 – GMP Reconciliations – Update and Training
- Pensions Committee 21st September 2015 – Pensions Update

4. COMMENTS OF THE GROUP DIRECTOR, FINANCE AND CORPORATE RESOURCES

- 4.1 This report sets out for the Pensions Committee the issues faced by the Fund as it tries to reconcile historical data for its scheme members for periods during which they were contracted out of the second state pension.
- 4.2 At this time it is difficult to quantify the full financial impact of the GMP data reconciliation exercise, but the Fund has commenced initial phases, using the Fund's external administrators to match the data held on the pension administration system and that held by HMRC. The cost of the initial work has amounted to around £28,000, with estimated costs for Phase 2 and Phase 3 indicated at Appendix 1 to this report.
- 4.3 Whilst the cost of undertaking a GMP reconciliation exercise is likely to be significant, failure to undertake this work would result in the Fund being made responsible for the payment of any GMP liability that HMRC deems to be associated with it. Indications from Phase 1 of the project and from other funds' experiences are that the differences

between the Fund's administration data and HMRCs records are considerable, exposing the Fund to significant risk if no reconciliation exercise is undertaken.

- 4.3 The LGA in a letter to administering authorities provided an indication of the level of costs across LGPS for the GMP reconciliation exercise which suggested that total costs could be somewhere between £30m to £100m.

5. COMMENTS OF THE DIRECTOR, LEGAL

- 5.1 As quasi-trustees of the Pension Fund, the Pensions Committee have a fiduciary duty to ensure that the Fund is well managed. The end of contracting out and consequent requirement for pension funds to undertake GMP reconciliation exercises could have considerable implications for the Fund's liabilities. It therefore falls within the remit of the Committee to consider the requirement for the Fund to undertake such an exercise and how the costs of that exercise should be managed.
- 5.2 There are no immediate legal implications arising from this report.

6. GMP RECONCILIATION - BACKGROUND

- 6.1 From 6th April 2016 the government introduced the new State Pension (nSP). This was designed to radically simplify pension provision, removing layers of complexity whilst ensuring security in retirement. Amongst the provisions removed was the Additional State Pension (AP), an earnings-related element of the old system. Members of defined benefit occupational schemes such as the LGPS were able to 'contract out' of this element, permitting both employee and employer to pay lower National Insurance contributions as a result. In exchange, schemes guaranteed to provide members with a pension at least as high as they would have received had they not been contracted out. This guaranteed amount is the GMP; it applies to all those who were contracted out between 6 April 1978 and 5 April 1997.
- 6.2 Currently, HMRC offers a service whereby schemes can check their GMP records against those held by HMRC and resolve any differences. HMRC have announced that this will be scaled back considerably in April 2018. In December 2018, HMRC plans to write to all scheme members for whom its records indicate a GMP liability with details of the amount owing and the scheme responsible for payment. Following this, the Scheme Reconciliation Service (SRS) will be withdrawn altogether, with no further support offered for GMP queries. Where schemes have not undertaken a reconciliation of their contracted out liabilities, HMRC takes the stance that its own calculations are final; schemes will become responsible for any GMP liabilities which HMRC believe they hold.
- 6.3 A GMP reconciliation exercise lists all the members who have a GMP liability according to scheme records and compares this against a list of all members for whom HMRC holds a GMP record under that same scheme. The lists are rarely fully aligned at the start of the process, with discrepancies usually occurring both in terms of membership and GMP amounts. Where there is a discrepancy, this should be investigated and a decision taken on whether or not to accept the HMRC record as correct and adjust the individual's pension entitlements accordingly.

- 6.4 The reconciliation of GMP values is not a mandatory regulatory requirement; however the Fund faces significant risks if its GMP liabilities are not reconciled before the withdrawal of support for queries by HMRC in December 2018. These include:
- Incorrect calculation of GMPs by HMRC, potentially increasing the fund's overall liabilities
 - Assumed liability for GMPs if HMRC holds records for a fund that are not the fund's responsibility
 - Unexpected increase in liabilities if the Fund does not hold records of all the liabilities it is responsible for
 - Breach of The Pensions Regulator's (TPR) code of practice regarding record keeping
 - Over and underpayment of pension benefits to individual scheme members
 - Queries following HMRC notifications to scheme members in 2018
 - Reputational issues
- 6.5 In considering its approach to GMP reconciliation, the Fund should not only have regard to the risks above but also to the outcome of the government consultation on GMP indexation and equalisation. The removal of the Additional State Pension not only resulted in the need for large scale reconciliation exercises but also removed the link between public service and state pension systems that ensured that GMPs were fully indexed and equalised. If the government does not act, there will be no mechanism in place to fully index pension payments for members with contracted out service between April 1978 and April 1997 who reach State Pension age (SPa) after December 2018. Additionally, an inequality in the payment of public service pensions between men and women may also be introduced.
- 6.6 The consultation closed in February 2017 and the outcome is still pending. The Government has proposed three possible options: case by case comparison, full indexation and 1:1 conversion. All will require some degree of reconciliation of a scheme's GMP liabilities.

7. LB HACKNEY GMP RECONCILIATION PROJECT

- 7.1 Officers have been working with the pension administrators, Equiniti and the Fund's benefits consultant, AON on a phased reconciliation project. The project is being undertaken by a specialist team within Equiniti's discontinuance department, and is separate from the main administration service provided to the Fund. Equiniti is carrying out GMP reconciliations for a number of funds and this project forms part of their Contracted-Out Liabilities Reconciliations Programme, It is run on a phased basis, with the scope and estimate costings being agreed for each phase prior to approval.
- 7.2 To date Phase 1 has been completed at a cost of £28,000. This has involved requesting and receiving data from both HMRC and the Fund's administrator, and bulk analysis to identify sets of defined queries e.g. records that appear on Compendia, the administration system but not on HMRC's NICO database and vice versa, plus records for which the NICO data is insufficient, incorrect or missing. These initial queries have been submitted in bulk to HMRC for analysis.
- 7.3 Equiniti have now put together a proposal for Phase 2, the scope of which includes:

- Finalising the 'in scope membership' for the project by resolving queries over disputed membership (i.e. those records which appear on one database but not the other)
- Agreeing GMP amounts and State Scheme Premiums for records already matched (i.e. members definitively in scope as records appear) on both databases
- Identifying corrections to data anomalies or populating missing data items in either data set

7.4 Phase 3 of the project includes the certification and rectification of the Fund's administration data. Certification records on the administration system that reconciliation has been carried out, and what changes have been made. Rectification involves physical changes being made to the administration data held.

7.5 The provision of accurate cost information for the project as a whole is a particular challenge associated with GMP reconciliation. The work is time intensive, and until the details of the number of records in scope and the extent of the discrepancies are known, the Fund is reliant on estimated costings. Prior to formal commencement of Phase 2, the Fund has sought an estimate of the costs of Phase 3 relative to Phase 2, to give an early indication of the likely costs of the overall project.

7.6 The estimated costs for Phase 2 and Phase 3 are shown at Appendix 1 to this report. Whilst the costs are likely to be significant, failure to undertake this work would leave the Fund exposed to the risks described in the previous section. The Committee is therefore asked to consider formal approval for the commencement of Phase 2, with regular review of costs by Officers of the Fund. Officers will receive a monthly progress from Equiniti detailing progress made and costs incurred; summaries of these reports can be provided to the Committee as required. Additionally, Equiniti have proposed a series of cost notification caps, which are set out in Appendix 1. As each notification cap is reached, Equiniti will review and refine cost estimates with Officers, to ensure that the costs of the project are well managed.

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Exempt Appendices 1(parts a,b & c) – Estimated costs Phases 2 & 3