



Department  
for Work &  
Pensions

**From the Permanent Secretary**

Peter Schofield CB  
Caxton House  
Tothill Street  
London  
SW1H 9DA

Rt Hon Stephen Timms MP  
Chair  
Work and Pensions Select Committee  
House of Commons  
London  
SW1A 0AA

28 August 2020

*Dear Stephen*

### **Guaranteed Minimum Pension (GMP) Indexation**

Thank you for your letter of 11 August regarding the investigation by the Parliamentary and Health Service Ombudsman (PHSO) into complaints by two individuals into how the Department communicated information to them regarding changes to the policy on GMP indexation. You asked for an update on the work the Department has undertaken in light of the PHSO's findings.

By way of background, the PHSO partially upheld the complaints and the Department has apologised to the complainants and paid them compensation of £500 and £750, as recommended by the PHSO.

As part of its decision, PHSO also recommended that we provide clearer information about how people could suffer notional losses through the change, and that we invite others who believe they have suffered a similar injustice as the two individuals to come forward to have their cases considered.

We propose to respond to these recommendations by publishing a factsheet on GOV.UK and I attach a draft. We are currently awaiting the PHSO's comments on this.

In addition, the PHSO recommended that their reports into the matter were shared with the Select Committee and we have sent your office copies of these documents today.

You asked us to outline the extent to which the Department was aware of the negative impact of the policy on individuals, and how this was communicated to Parliament and others involved in the policy decision making.

As was clear from publication of the Government's White Paper in January 2013, it was an intrinsic feature of the new State Pension that the old regime of additional State Pension and contracting out, along with its various forms over the years, would be replaced by a new, simpler single-tier system. It was a fundamental feature of the changes that the withdrawal of additional State Pension meant also the withdrawal of

GMP indexation. A detailed account of the change was provided in a response to a PQ on 6 January 2014 and is attached for reference at Annex A.

More generally, the policy, and how it was communicated, was examined by the Work and Pensions Select Committee in its investigation into *Understanding the new State Pension* in 2016. In addition, the NAO reported on the policy in the same year.

Handwritten signature in black ink, appearing to read 'Peter Schofield'.

Peter Schofield CB

## Annex A

### GMP Indexation PQ 6 January 2014

#### Guaranteed Minimum Pensions

**Teresa Pearce:** To ask the Secretary of State for Work and Pensions (1) what estimate his Department has made of the number of people affected by ending the payment of guaranteed minimum pension increases; [181793]

(2) what impact assessment his Department has conducted of ending the payment of guaranteed minimum pension increases; [181794]

(3) what estimate he has made of the average loss to persons affected by ending the payment of guaranteed minimum pension increases; [181795]

(4) what estimate his Department has made of the total saving to the public purse as a result of ending the payment of guaranteed minimum pension increases. [181860]

**Steve Webb:** The Department for Work and Pensions does not pay increases on guaranteed minimum pensions (GMPs). GMPs are occupational pension scheme benefits

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which were accrued between 1978 and 1997. Pension schemes are liable for any statutory indexation of GMPs, and this liability will not change as a result of the single tier reforms. The Department for Work and Pensions pays state pension benefits and their indexation, including additional state pension (SERPS and S2P) and basic state pension.

Additional state pension and GMPs are linked in that when a person reaches pensionable age, the total amount of GMP is subtracted from the total amount of additional state pension built up between 1978 and 1997, and any net amount is paid. This subtraction of the total GMP amount is called a ‘contracted-out deduction’, and reflects that reduced national insurance was paid during the period of contracting out in return for meeting legislative requirements. This calculation is performed each year that the pension is payable.

There is no statutory obligation on schemes to pay increases on GMPs accrued between 1978 and 1988. However, additional state pension built up during that period is subject to increases. When the contracted-out deduction is subtracted from the additional state pension, the remaining additional state pension includes an increase linked to prices. In this way, an amount broadly equivalent to the GMP, but which is in fact additional state pension, is subject to an increase. Schemes are under an obligation to pay increases on GMPs accrued between 1988 and 1997, subject to a cap of 3%.

With the introduction of single tier, the additional state pension will close, as will the facility to contract out. For those reaching state pension age from April 2016, we will value their national insurance record to that point. We will compare what state pension the single-tier rules would give them with what they have built up as at April 2016 under the current system. The higher of these two valuations will become the individual’s ‘foundation amount’.

As set out in the White Paper, the design of the transition will benefit many people with a history of contracting out. In effect, these individuals may be able to offset their contracted-

out deduction with further qualifying years until they reach the full amount of single tier. This means that many individuals who have previously been contracted-out may receive more state pension than they would have under the current system.

The Department estimates that over 2 million people will reach state pension age in the five years after the introduction of single tier, of whom around 40% to 45% will have been contracted out of private and public sector defined benefit schemes between 1978 and 1988. From 1988 onwards, the facility to contract out was extended to people in defined contribution schemes. By the mid 2030s over 80% of people reaching state pension age will have had a deduction for being contracted out factored into their transitional calculations and many will be able to benefit from the transition described above, as well as from the indexation arrangements for single tier compared to the current arrangements for additional pension and basic state pension.

The single tier reforms will cost no more than the existing system, and expenditure is projected to be within 1% of current spending until the late 2030s. The impacts of the single tier reforms have been captured in the impact assessment for single tier, which is published

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online. We estimate that those who hold GMPs are no more likely to have a lower outcome as a result of the reforms overall than the rest of the population.



## Work and Pensions Committee

House of Commons, London, SW1A 0AA  
Tel 020 7219 8976 Email [workpencom@parliament.uk](mailto:workpencom@parliament.uk)

From the Chair

11 August 2020

Dear Peter

Last year it was reported that the Government was found guilty by the Parliamentary and Health Service Ombudsman of maladministration over the impact of state pension reforms on those with a Guaranteed Minimum Pension (GMP). I understand that the Department is considering how it informs individuals how they may have been negatively affected by changes in policy on GMP indexation. Might you please provide the Committee with an update on this work?

Please could you also outline the extent to which the Department was aware of the negative impact of the policy on individuals, and how this was communicated to Parliament and others involved in the policy decision making?

With best wishes,

**Rt Hon Stephen Timms MP**  
Chair, Work and Pensions Committee