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By James Mirza-Davies

Guaranteed Minimum Pension increases

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Contents

Summary

The State Pension and contracting-out

For people who reached State Pension age before 6 April 2016, the State Pension has two tiers:

- The basic State Pension – which is a contributory flat-rate benefit.
- The additional State Pension – which depends on someone's earnings during their working life since 1978.

When the additional State Pension was introduced, it was possible to contract-out. This meant that both the employer and employee paid a reduced rate of National Insurance and instead receive a workplace pension meeting certain requirements.

Contracting-out ended when the new single-tier State Pension replaced the basic and additional State Pensions in April 2016 as there was no longer an additional State Pension to contract-out from.

What is a Guaranteed Minimum Pension?

A Guaranteed Minimum Pension (GMP) is a minimum pension normally provided through a workplace pension scheme to people who contracted-out of the additional State Pension between 6 April 1978 and 5 April 1997.

Guaranteed Minimum Pensions Increase Order

Schemes providing GMP are required to annually increase GMP entitlement built up (accrued) between 6 April 1988 and 5 April 1997 in line with prices. This increase is capped at 3%.

The Guaranteed Minimum Pensions Increase Order 2024 would specify that the minimum rate for GMPs is to be increased by the maximum amount permitted under the 3% cap. The increase in Consumer Prices Index (CPI) for the appropriate review period is 6.7% (the 12 months to September 2023).

How do Guaranteed Minimum Pensions interact with the State Pension?

Someone's GMP entitlement is deducted from the State Pension they receive. This calculation differs for the old and the new State Pensions:

- Under the additional State Pension someone's GMP entitlement is deducted from the amount they would have accrued had they not contracted-out. The person is entitled to the remaining amount of the additional State Pension.
- When the new State Pension was introduced in April 2016 a check was done by comparing State Pension entitlement under both the pre-2016 and post-2016 systems after making adjustments for contracting out (PDF). The higher amount became that person's "starting amount" – their entitlement in April 2016. After this their GMP entitlement continued to be increased and they will also be able to increase their new State Pension up to the full level.

Parliamentary and Health Service Ombudsman report

In 2019, the Parliamentary and Health Service Ombudsman (PHSO) published a report on its investigation of complaints by two individuals who said that the Department for Work and Pensions had failed to communicate that its State Pension reforms could have a negative long-term impact.

In response in August 2021, DWP published a factsheet on GMP and the effect of the new State Pension.

Public service schemes

There are specific legislative requirements applying to public service pensions – which must be annually increased in line with prices – measured according to the Consumer Prices Index (CPI).

1 Background

1.1 The State Pension and contracting-out

For people who reached State Pension age before 6 April 2016, the State Pension has two tiers:

- The basic State Pension (BSP) – which is a contributory flat-rate benefit.
- The additional State Pension – which depends on someone's earnings during their working life since 1978.[1]

The basic and additional State Pensions were replaced by the new State Pension on 6 April 2016.[2] This means that men born on or after 6 April 1951, and women born on or after 6 April 1953 are eligible to claim the new State Pension and people born before are eligible to claim the basic and additional State Pension.[3]

The basic State Pension

The basic State Pension is a contributory flat rate benefit. Eligible people reaching the state pension age before 6 April 2016 needed 30 qualifying years of National Insurance contributions or credits to receive the full basic State Pension.

In 2023/24 the full basic State Pension is £156.20 a week and will increase to £169.50 from April 2024.[4]

The additional State Pension

The additional State Pension is an earnings-related entitlement. Between 1978 and 2002 this was provided by the State Earnings-Related Pension Scheme and by the State Second Pension after that.[5]

When the additional State Pension was introduced in 1978, employers could contract-out their employees.[6] This meant that both the employer and

1 Social Security Contributions and Benefits Act 1992
2 Pensions Act 2014
3 Gov.uk, State Pension [accessed 26 January 2024]
4 Further detail is available in the Commons Library briefing CBP-09872, Benefits uprating 2024/25
5 Social Security Pensions Act 1975 and Welfare Reform and Pensions Act 1999
6 Social Security Pensions Act 1975

employee paid a reduced rate of National Insurance and instead receive a workplace pension meeting certain requirements.

The amount of this reduction – the “contracted-out rebate” – was set by the Government on the advice of the Government Actuary’s Department and was designed to reflect the cost of providing the benefits foregone.[7] In 2015/16, the rebate was 1.4% for employees and 3.4% for employers.[8]

The new State Pension

The new State Pension was introduced for people reaching the State Pension age on or after 6 April 2016.[9] Unlike the previous system, the new State Pension is single-tiered, and people need 35 qualifying years of National Insurance contributions or credits to receive the full amount.[10] It is not possible to contract-out of the new State Pension.

The full new State Pension is £203.85 a week in 2023/24 and will increase to £221.20 from April 2024.[11]

1.2 What is a Guaranteed Minimum Pension?

A Guaranteed Minimum Pension (GMP) is a minimum pension normally provided through a workplace pension scheme to people who contracted-out of the additional state pension between 6 April 1978 and 5 April 1997.[12]

Until April 1988, members of contracted-out schemes had to be provided with an individually calculated GMP.[13] Schemes that provide GMP usually needed to be defined benefit schemes which provide specified pension benefits based on factors such as salary and length of service. However, defined contribution schemes, which provide a pension pot that can increase or decrease in value, could also contract-out if a GMP was provided through a defined benefit underpin.[14] In a scheme with a defined benefit underpin the member receives the better of the pension from the defined contribution scheme or the defined benefit scheme.

The Pensions Act 1995 abolished the future accrual of GMPs with effect from 6 April 1997.[15] The existing rights to GMPs accrued until that date though were

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7 Pensions Commission, “Pensions: Challenges and Choices: The First Report of the Pensions Commission”, October 2004, Appendix F, p158

8 HMRC, Rates and allowances: National Insurance contributions, 6 April 2015

9 Pensions Act 2014

10 Pensions Act 2014

11 Further detail is available in the Commons Library briefing CBP-09872, Benefits uprating 2024/25

12 Pensions Act 1995

13 Pension Schemes Act 1993, s109

14 Social Security Act 1986

15 Pensions Act 1995

fully protected.[16] After 1997 there were still minimum pension benefits which employers needed to provide in order to contract out, but these were met through a reference scheme test instead of GMP.[17]

The Pensions Act 2007 included provision to allow pension schemes to convert GMPs to scheme benefits, from 6 April 2009.[18]

1.3 How do Guaranteed Minimum Pensions interact with the State Pension?

Someone's GMP entitlement is deducted from the State Pension they receive. This calculation differs for the old and the new State Pensions.

The additional State Pension

Schemes providing GMP are required to annually increase GMP entitlement built up (accrued) between 6 April 1988 and 5 April 1997 in line with prices. This increase is capped at 3%.[19]

At the same time the GMP entitlement is deducted from the additional State Pension they would have accrued had they not contracted-out.[20] The person is entitled to the remaining amount of the additional State Pension. The effect of these arrangements is that, although schemes are not required to provide increases on the GMP on rights accrued between 1978 and 1988 (or in excess of 3% on rights accrued between 1988 and 1997), the additional State Pension that would have been built up during that period still increases.

The new State Pension

When the new State Pension was introduced in April 2016, a check was done by comparing State Pension entitlement under both the pre-2016 and post-2016 systems after making adjustments for contracting out.[21] The higher amount became that person's "starting amount" – their State Pension entitlement in April 2016. After this their GMP entitlement continued to be increased and they will also be able to increase their new State Pension up to the full level, at the rate of 1/35th of the full rate for each additional qualifying year they gain before reaching State Pension age.[22]

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16 Pensions Act 1995

17 Pensions Act 1995

18 Pensions Act 2007, section 14; Pensions Act 2007 (Commencement No. 3) Order 2009 (SI 2009/406); Pensions Bill Deb, 1 February 2007, c234

19 Pension Schemes Act 1993, s109

20 Pension Schemes Act 1993, s46

21 Department for Work and Pensions, Single-tier Impact Assessment (PDF), October 2013

22 Department for Work and Pensions, The single-tier transition and contracting out (PDF), 2013

2 State Pension reforms

2.1 Treatment of periods of contracting out

Contracting-out ended when the new single-tier State Pension was introduced from April 2016 as there was no longer an additional State Pension to contract-out from.[23]

Employees who were contracted-out on 6 April 2016 ceased to be so and became no longer eligible for a contracted-out rebate on their National Insurance (NI), meaning that their National Insurance contributions (NICs) increased to the standard rate.[24] In return, they started to accrue State Pension rights on the same basis as other employees.

In addition, the new State Pension needed to deal with previous periods of contracting out. If someone has spent a period in a contracted-out scheme a deduction is applied to their State Pension to reflect the fact that they paid a lower rate of NI.

2.2 Starting amount

When the new State Pension was introduced in April 2016 a check was done to make sure individuals did not receive less than they would have done under the pre-2016 system. People's National Insurance record was calculated under the old and new scheme rules and the higher amount became that person's "starting amount" – their entitlement in April 2016.[25]

The calculation for both amounts took full account of people's contracting-out record. For the old State Pension system contracted-out deductions are made from the additional State Pension someone would have accrued had they not contracted-out.[26] A person who spent many years contracted-out may, therefore, find that their starting amount is less than the full amount of the new State Pension even where they had 35 qualifying years. However, they will be able to increase their new State Pension up to the full level, at the rate

23 Pensions Act 2014, Part 1
24 Department for Work and Pensions, Single-tier Impact Assessment (PDF), October 2013, section 5.2
25 Department for Work and Pensions, The single-tier transition and contracting out (PDF), 2013
26 As above (PDF)

of 1/35th of the full rate for each additional qualifying year they gain before reaching State Pension age.[27]

This led some commentators to note that gainers from the introduction of the single-tier State Pension will include some people who have been contracted-out. The Institute for Fiscal Studies, said:

> Overall, 35% of men and 61% of women (43% of individuals) would see their pension income at SPA increased as a result of the proposed reform. Many of these individuals will be benefiting from the ability to 'work off' previous periods of contracting out.[28]

2.3 Impact of ending contracting out for people with Guaranteed Minimum Pensions

The statutory requirements for pension schemes to increase GMPs did not change after the single tier reforms. However, the way in which the GMP affects State Pension entitlement did change.

Under the pre-2016 system, an annual calculation was made which deducted the amount of any GMP from an individual's additional State Pension entitlement. Under the new State Pension this was done once at implementation. However, an individual who was contracted-out on that date will cease to be so and will start to build up rights to the State Pension in the same way as other people.[29]

In response to a question on the issue in January 2014, the then Pensions Minister Steve Webb said that the design of the transition to the single-tier would benefit many people who had been contracted out and 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."[30]

In March 2016, the National Audit Office (NAO) produced a report on the impact of state pension reforms on people with Guaranteed Minimum Pensions.[31] It explained that for people retiring after 6 April 2016, the Government would no longer take account of inflation increases to GMPs when uprating their new State Pension.[32] This meant that any GMP accrued between 1978 and 1988 would not be uprated, and the scheme provider would only uprate GMPs built up between 1988 and 1997 to a maximum of 3% each

27 Department for Work and Pensions, The single-tier transition and contracting out (PDF), 2013
28 Institute for Fiscal Studies, A single-tier pension: what does it really mean? (PDF), July 2013
29 Department for Work and Pensions, The single-tier transition and contracting out (PDF), 2013
30 HC Deb 6 January 2014 c51W
31 NAO, DWP – the impact of state pension reforms in people with Guaranteed Minimum Pensions (PDF), HC 907, 24 March 2016
32 As above (PDF)

year.[33] In addition, increases in the State Pension age meant GMPs could lose more value before people started to draw their State Pension. Some people would be able to offset some of the loss in value of their GMP by building additional entitlement to the new State Pension between April 2016 and reaching State Pension age.[34] Overall, the amount by which individuals would be affected would "depend on the time they were in a contracted-out scheme, the value of their new state pension, how the government decides to uprate the state pension and future inflation rates.[35]

The NAO concluded that the impact of the new State Pension reforms on people with GMPs would vary widely:

> The impact of new state pension reforms on people with Guaranteed Minimum Pensions will vary widely. The type of person who will do comparatively worse under the reforms is someone who has spent long periods in a contracted-out pension scheme and is close to retirement on 6 April 2016, so has little time to build up additional entitlement to new state pension. The Department estimates that 180,000 people who will reach state pension age in 2016-17 will have Guaranteed Minimum Pensions from before 1988. The amount by which people will be affected depends on their specific employment history. The Department's modelling forecasts that 50,000 of these people will be worse off in 2017-18 as a result of the introduction of new state pension.[36]

Some people were likely to lose out and had not been able to find the information they needed:

> The uprating of Guaranteed Minimum Pensions is a complicated area. The impact of reforms on individuals will depend on a number of factors including their age, employment history, earnings and future inflation. Some people are likely to lose out and they have not been able to find the information they need.
>
> We are concerned that the Department has limited information about who is affected by the impact of pension reforms on Guaranteed Minimum Pensions. It is now seeking to improve how it communicates the impact of pension reforms, and will need to help people identify how they are affected and provide them with accurate and more complete information so that they can make informed decisions about their future pension arrangements.[37]

Parliamentary and Health Service Ombudsman report

On 30 August 2019, the Parliamentary and Health Service Ombudsman (PHSO) published a report on its investigation of complaints by two individuals who said DWP had failed to communicate that its State Pension reforms could have a negative long-term impact.[38] The PHSO said that DWP had failed to provide clear and accurate information on the issue, despite being warned,

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33 NAO, DWP – the impact of state pension reforms in people with Guaranteed Minimum Pensions (PDF), HC 907, 24 March 2016

34 As above (PDF)

35 As above (PDF)

36 As above (PDF)

37 As above (PDF)

38 Parliamentary and Health Service Ombudsman, Communication of changes to inflation of State Pensions, 30 August 2019

with the result that some individuals were not aware that they might need to make alternative provision for their retirement.[39] The Ombudsman recommended that DWP should "review and report back its learning from our investigations." In particular, it should improve its communications on this issue.[40]

In response in August 2021, DWP published a factsheet on "GMP and the effect of the new State Pension", saying it would review usage data after six-months.[41] In June 2022, the then Minister for Pensions and Financial Inclusion told the Work and Pensions Committee that it had only had one comment on the factsheet and would "review this when more information is available."[42]

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39 Parliamentary and Health Service Ombudsman, Communication of changes to inflation of State Pensions, 30 August 2019

40 As above

41 Department for Work and Pensions, Guaranteed Minimum Pension and the effect of the new State Pension, August 2021

42 Work and Pensions Committee, Letter from the Minister for Pensions to Chair re Review of GMP Factsheet (PDF), 29 June 2022

3 Public service schemes

There are specific legislative requirements applying to public service pensions – which must be annually increased in line with prices – measured according to the Consumer Prices Index (CPI).[43]

Previous governments made commitments to ensure the GMPs of public servants were increased. For example, on 20 May 1975, Mr Alec Jones, the then Minister for Social Security gave assurances to the House of Commons that the GMP of public service schemes will receive price increases, and on 14 December 1978, Mr Eric Deakins, the then Minister in the Department for Health and Social Security, said that the Pensions Act 1975 was intended to take account of increases and that "those increases will normally be sufficient to cover inflation proofing of the GMP".[44]

3.1 The old State Pension

The arrangements in place before 6 April 2016 ensured that public servants received indexation on their GMP while preventing duplication.[45] In cases where this system did not deliver full indexation (for example, if the pensioner was resident in an overseas country where the UK State Pension was not uprated), their full public service pension was increased, including the GMP.[46]

3.2 The new State Pension

As explained in section 2 above, the mechanism in the old State Pension for providing full indexation of GMPs, is not part of the new State Pension. HM Treasury has explained the new State Pension removed the mechanism to give public service schemes fully indexed pension and said that this impacted schemes in two ways:

[43] Pensions Increase Act 1971 and sections 59 and 59A of the Social Security Pensions Act 1975 as amended

[44] HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, November 2016

[45] HM Treasury, Guidance on the operation of pensions increase legislation for public service pension schemes, April 2016

[46] HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, November 2016, para 2.3

- they will no longer receive, in effect, indexation of their GMP through the indexation received on the AP
- the previous mechanism designed to avoid unequal payments on account of gender will no longer apply[47]

In March 2016, the Government announced that those reaching State Pension age between 6 April 2016 and 6 December 2018 would receive a fully-indexed public service pension for life:

> In response to the introduction of the new State Pension in April 2016, the government will continue to price protect the Guaranteed Minimum Pension of public sector workers.
>
> This means that those who reach State Pension Age on or after the 6th April 2016 and before the 6th December 2018 – when the State Pension Age equalises – will receive a fully indexed public service pension for their whole life.
>
> This will ensure public service pension payments to these individuals continue to be equal between men and women.[48]

In November 2016, HM Treasury launched a consultation on how to address this issue in the longer term.[49] It explained that "an estimated two million members of the public service schemes with GMPs who reach their State Pension age up until 2040 may be affected" by the State Pension reforms. The impact would vary. In extreme cases, cumulative losses could have an estimated value of £18,000. However, for the majority of those who lose, the government expected the impact to be lower. The consultation aimed to consider two issues:

- How best to avoid the introduction of unequal payments to men and women in the public service schemes that will result from the abolition of the additional State Pension.
- Whether public service pension schemes should pay full indexation on GMPs rights for people reaching [State Pension age] after 5 December 2018.[50]

The aim was to address these two "complex and closely linked" issues in a single policy solution. The Government asked for views on three options: a

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47 HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, 28 November 2016, para 2.4

48 HM Treasury, Government one step closer to introducing new State Pension this year, 1 March 2016; HM Treasury, Guidance on the operation of pensions increase legislation for public service pension schemes, April 2016

49 HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, November 2016

50 As above

case-by-case approach; continuing the full indexation policy introduced in 2016; and conversion of GMP rights into scheme benefits.[51]

On 22 January 2018, it said it had decided to extend the interim solution for a further two years, while investigating the possibility of conversion.[52]

In March 2021, following a further consultation, the Government said it would make full GMP indexation the permanent solution.[53]

This is discussed in the Library briefing on Public service pension increases.

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51 HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, 28 November 2016

52 HM Treasury, Consultation on indexation and equalisation of GMP in public service pension schemes, 22 January 2018

53 HM Treasury, GMP indexation consultation, March 2021

4 Debate on GMP Increase Orders

The Secretary of State is required to review the general level of prices in Great Britain annually and lay a draft Order before Parliament specifying the percentage by which GMPs are to be increased. This must be in line with the general level of prices, capped at 3%.[54] Annual increases in the State Pension are provided for in the Social Security Benefits (Uprating) Order for that year.[55]

The GMP Increase Order and Social Security Benefits Uprating Order are generally debated together. The Benefits Uprating Order is generally the focus of discussions, while, as Ministers have often said, the GMP increase order is an "entirely technical matter."[56]

There was more significant debate of the Guaranteed Minimum Pensions Increase Order 2022 in February 2022. Stephen Timms (Labour) raised concerns that the Government's factsheet about the Parliamentary and Health Service Ombudsman's findings (section 2.3 of this paper) was difficult to find and did not tell people they could apply for compensation.[57] Beth Winter (Labour) and Alan Brown (SNP) expressed concerns that GMP increases were capped at 3% when inflation may have been much higher when the increases were enacted in April 2022.[58] According to the Office for National Statistics inflation as measured by CPI was 9.0% in April 2022.[59]

The Guaranteed Minimum Pensions Increase Order 2024 would specify that the minimum rate for GMPs is to be increased by the maximum amount permitted under the 3% cap. The increase in CPI for the appropriate review period is 6.7% (the 12 months to September 2023).[60]

54 Pension Schemes Act 1993, section 109
55 See Library Briefing Paper CBP 5649, State Pension Uprating
56 For example HC Deb 9 February 2015 c569 [Steve Webb] and HC Deb 5 February 2018 c1257 [Kit Malthouse]
57 HC Deb 7 February 2022 c727
58 HC Deb 7 February 2022c732-740
59 Office for National Statistics, Consumer price inflation, 18 January 2023
60 The Guaranteed Minimum Pensions Increase Order 2024 - Draft Explanatory Memorandum

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