

General Information

Transvas Profiler: Franking

Date Logged: 11 March 2014

What is Franking?

In occupational final salary pensions, there are circumstances where one tranche, or slice of benefits can be offset against increases in another. This is known as franking.

Full Franking

The most widely known example of Full Franking is for members who left their pension scheme prior to 1 January 1985 with some GMP.

Schemes were permitted to let any increases on the GMP before retirement effectively be absorbed by the non GMP pension. For leavers after 31 December 1984, this practice was prohibited by the Anti-Franking legislation; however there are still common scenarios where Full Franking is permitted for post 85 leavers. These are discussed below.

Partial Franking

The Anti-Franking Legislation, together with various Social Security Acts provide for a minimum level of pension that must be paid, depending on the benefits that the member has accrued.

In simple terms, there are three main scenarios:

- 1) For a member retiring **at the scheme's Normal Retirement Age** on or after GMP Age
The minimum pension **at Retirement** is the sum of:
 - i) Excess pension revalued in line with Statutory Orders* to Normal Retirement Age.
 - ii) GMP revalued to GMP Age

- 2) For a member retiring **at the scheme's Normal Retirement Age** but before GMP Age
The minimum pension **at Retirement** is:
 - i) Excess pension revalued in line with Statutory Orders* to Normal Retirement Age.Then, on reaching **GMP Age** the minimum pension is the sum of:
 - ii) Excess pension revalued in line with Statutory Orders* to Normal Retirement Age.
 - iii) GMP revalued to GMP Age

- 3) For a member retiring **Before the scheme's Normal Retirement Age**
There is no minimum pension until the member reaches GMP Age
The minimum pension **at GMP Age** is:
 - i) GMP revalued to GMP Age

*Statutory Orders here is taken to mean the minimum rate appropriate to the excess slice, so 0% for pre 85 pension for pre 86 leavers, RPI/CPI capped at 5% for post 85 pension for pre 91 leavers...etc

Summary

Normal Retirement Style Franking

Any member who retires at Normal Retirement Age, will at least receive their excess revalue to NRA plus their GMP at GMP age; however if there is any escalation in payment on the excess pension between retirement and GMP age, the scheme is perfectly able to frank these increases against the GMP revaluation.

i.e. Franking is permitted on the escalation only

Early Retirement Style Franking

If a member retires early, then all bets are off as far as anti-franking is concerned. The scheme need only test that GMP is covered at GMP age and the entire excess pension can be franked to provide for this.

i.e. Full Franking of the excess pension is permitted

Public Sector Style Franking

There is a further scenario for Public Sector style schemes. If the scheme revalues the entire pension including the GMP at a single rate that is equal to RPI or CPI, then on retiring at the scheme's Normal Retirement age, the minimum pension on reaching GMP age will be the sum of:

- i) GMP revalued to GMP age (usually by Section 148 orders)
- ii) Excess at Date of Leaving

So the scheme can frank the *revaluation* of the excess pension, but not fully frank the *whole* excess.

An Example

Consider a male with £100 of GMP and £300 of excess pension at date of leaving. The scheme's Normal Retirement Age is 60. Let's say the GMP revalued to **GMP age** is £400; and the Excess revalued to **Scheme NRA** is £500. The scheme also pay £275 as a GMP bridge at age 60.

This would be as follows:

Benefit	Date of Leaving	NRA (60).....(with esc to 65)	GMP Age (Male 65)
GMP	£100	£275.....£350	£400
Excess	£300	£500.....£600	£600 £550
Total	£400	£775.....£950	£1000 £950

Between 60 and 65, the pension of £775 receives escalation in payment so at age 65 the excess is £600 and the GMP bridge is £350. A total of £950.

The scheme could simply replace the GMP bridge of £350 with GMP, so the total is £400 + £600. There would be a step-up at age 65 of £50 to take the pension from £950 to £1000. Some schemes do apply these rules.

However most schemes would simply reallocate the pension at GMP age to ensure they pay at least the GMP (£400) plus the Excess at normal retirement age (£500). In this case the £950 is more than the minimum and they would continue to pay £950, by reallocating £50 from the excess pension to pay the GMP.

This is an example of franking the escalation on the excess pension.