The big three

John Towner considers the top three questions for schemes considering a buyout, buy-in or longevity insurance

We are often asked what the single most important factor is behind a scheme successfully implementing an insurance de-risking arrangement and the answer is almost always preparation. Establishing a buyout, buy-in or longevity insurance is not an insignificant undertaking. Timelines are tight. The data requirements are significant. Integrated coordination is essential. However with the right preparation, the process is manageable.

Preparation means that the trustees and sponsoring company are able to answer these three questions:

1) How do you get the best arrangement for your scheme?
2) How do you pay for it?
3) What do you need to do to make it happen?

1) How do you get the best arrangement?

The key to obtaining the best arrangement for your scheme is engaging early with your advisers and insurance partners to understand the factors that will underpin your quote, so that you can look to get the most cost-effective arrangement for your scheme.

The more complete and accurate your data is, the better the insurance company will understand your scheme and this will come through in the pricing offered.

The new pensions freedoms have put liability management exercises back on the agenda for many pension schemes. These kinds of exercises will potentially impact insurance pricing so we encourage close coordination with the insurance company at an early stage. As recent transactions have demonstrated, running these initiatives in conjunction with an insurance exercise can help the trustees and the sponsoring company achieve their objectives, while giving members the freedom and choice to shape their pensions.

Market conditions can impact the price of the insurance quote relative to your scheme assets by several percentage points within a short period of time; building monitoring into your journey plan can help the scheme execute when market conditions and insurer pricing are favourable.

2) How do you pay for it?

Paying for your buyout or buy-in involves understanding what cash and investments are available and ensuring an efficient and cost-effective transfer of assets from your scheme to the insurer.

Both trustees and sponsoring company should understand what each is prepared to contribute and their constraints. For example, is the company willing to make additional cash available?

The cost of your insurance arrangement may be able to be reduced if the scheme pays for the insurance with assets rather than cash, as transition costs are minimised and pricing certainty is increased. Trustees and sponsors will therefore want to understand which scheme assets the insurer would be willing to accept as part of your arrangement.

3) How do you make it happen?

Making it happen is all about establishing the right governance to manage the process.

All stakeholders will want to understand at the outset what each would like to achieve and the risks involved. For example, do the trustees want to reduce reliance on the sponsor covenant, is the sponsor concerned with its shareholders' requirements? Increasing the level of understanding among all stakeholders will align interests and increase the probability of reaching a successful outcome.

A number of work streams will need to be pulled together simultaneously to achieve the desired outcome. All parties will want to agree roles, responsibilities and timescales in advance and understand who will own the process.

Unless the trustees have undertaken a full buyout, the scheme will need to continue to be managed on an ongoing basis and there may need to be adjustments made to the investment and risk management strategy with respect to the remaining liabilities not insured.

In conclusion

The racing driver, Bobby Unser, once said that success is where preparation and opportunity meet. Nothing could be more true in the pension buyout market. If stakeholders put the work in upfront to prepare, they will be well positioned to capture the best opportunity to secure their members' benefits with an insurance company.

If you would like to discuss your de-risking strategy, please contact John Towner on 020 3124 2963 or email john.towner@landg.com.

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