Targeting security

Matt Kohler-Richards discusses how trustees targeting funding at buyout level are keeping their options open – and maximising member security



Deciding on a funding strategy for a defined benefit (DB) scheme can appear complicated as trustees and sponsors consider a growing range of endgame options. But every assessment should begin with one very simple question: how will the security of members' pensions be maintained?

DB schemes, after all, exist to provide members with their pensions. Member security should therefore always be ground zero for decisions around endgames. Those decisions start with funding.

There are, of course, different approaches to funding. But when member security is the starting point, the result is clarity around the decision-making process. Fundamentally, a scheme funded to buyout has the strongest set of options in front of it: It can insure, run on or consider releasing surplus in a controlled way. Funding at buyout level keeps those options available and gives trustees the ability to secure benefits if circumstances change. With many schemes having reached the position of being in surplus (often after a long and difficult journey), it is critical for members that surplus is protected. Buyout of course, fully secures that surplus.

Buyout remains the gold standard for member security because it replaces covenant, investment, governance and operational risks with a regulated, durable outcome. Alternative endgames may be appropriate in certain circumstances, but trustees should assess every option against the same question: does it improve or weaken member security? That means testing covenant, liquidity and investment risks under credible downside scenarios before pursuing an alternative endgame or releasing surplus.

From that foundation, trustees should define their objectives and consider how their chosen partner will deliver them. Price, insurer strength, covenant replacement, execution certainty and member experience should be assessed as a complete package.

In our experience, this process often demonstrates the power of buyout: A regulated, market-tested solution that secures members' benefits and provides clarity over the risks being transferred. However, price is only part of the decision. Trustees also need to partner with an insurer with the transition capability to deliver the agreed outcome and support members throughout the journey.

It is sometimes argued that targeting buyout-level funding somehow ties trustees' hands or limits their options. In fact, the opposite is true. A strong funding position allows trustees to make decisions from a position of strength, with a clear understanding of the cost of securing members' benefits.

Surplus release could then be considered by trustees. My concern is that allowing extraction at low-dependency funding could remove capital before members' benefits are adequately protected, especially in volatile market and economic conditions.

PIC's purpose is simply to pay the pensions of our current and future policyholders. That purpose keeps policyholders and the debate around endgame solutions grounded in the only outcome that matters: paying the right pension to the right person, at the right time, for life.

The security of members' pensions should always be paramount. By targeting buyout-level funding, trustees preserve the full range of options and create the strongest platform for their decisions. Alternative solutions may suit particular circumstances, but when trustees put members first and test those alternatives against the objective benchmark of buyout, the combination of security, certainty and service offered by the insurance sector remains the gold standard for most schemes.



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