SEPTEMBER 2008

news

sackers extra

Options for managing pensions risk

With so many defined benefit (DB) pension schemes in long-term run-off, managing risk is a hot topic for scheme sponsors. And the emergence of a new buy-out (and buy-in) market has widened the de-risking options available to pension schemes. Combined with more competitive pricing, this has made buy-outs / buy-ins a genuine option for trustees and employers contemplating laying off risk.

Options Available

- Broadly, the choices now available to ongoing schemes include:
  - buy-outs;
  - buy-ins; and
  - an array of "alternative" de-risking solutions.

Buy-outs

Transfer of liabilities

- A conventional route for schemes in wind-up, a buy-out usually consists of an annuity purchase with an insurance company.
- The buy-out process on wind-up transfers all of the scheme's liabilities (i.e. for both pensioners and deferred members) to the insurance company in the members' names.

Buy-outs

Some issues for ongoing schemes

- Ongoing schemes may consider buying-out a particular class of members, such as pensioners.
- But funding is likely to be the main barrier, as the benefits to be bought out will need to be fully funded.
- A history of poor record keeping can also pose problems; as can having to cater for contracted-out benefits.
- And schemes will need to make sure that the members left behind are not prejudiced by a buy-out.

SACKER & PARTNERS

The buy-out provider

Some issues

- Schemes looking to buy-out need to scrutinise both the provider and the terms it is offering.
- For example, how might the buy-out price move before the process is finalised?
- Choosing an insurance company with a strong "covenant" and a long-term commitment to the market are also likely to be key considerations for trustees.
- A good administration track record will likewise be important.

Buy-ins

In brief

- Potential impediments which can arise in relation to buy-outs have led to the increased use of the buy-in model.
- A buy-in is a bulk annuity purchased in the trustees' name.
- Unlike a buy-out, the annuity remains a scheme asset, albeit one which matches the relevant liabilities.
- For more on buy-ins, please see our separate newsletter: "Buy-ins – the name of the 'legal' game" dated September 2008.[1]

The alternatives

- In addition to the traditional buy-out and buy-in models, insurance companies and banks have been devising new solutions for schemes seeking to de-risk.
- The possibilities include:
  - mortality hedging / survivor swaps;
  - longevity insurance;
  - employer covenant insurance; or
  - company purchase.

The future

- Analysts are predicting that the buy-out market could be worth up to £10 billion in 2008.
- This figure still only represents about 1% of all liabilities in UK occupational pension schemes.
- But it remains to be seen how current turbulence and changes in the financial markets will impact on the buy-out markets.

[1] Available from the client area of our website at: www.sackers.com

SACKER & PARTNERS

Solicitors specialising in pensions law

Sacker & Partners LLP
29 Ludgate Hill
London EC4M 7NX
Tel 020 7329 6699
Fax 020 7248 0552

enquiries@sackers.com
www.sackers.com