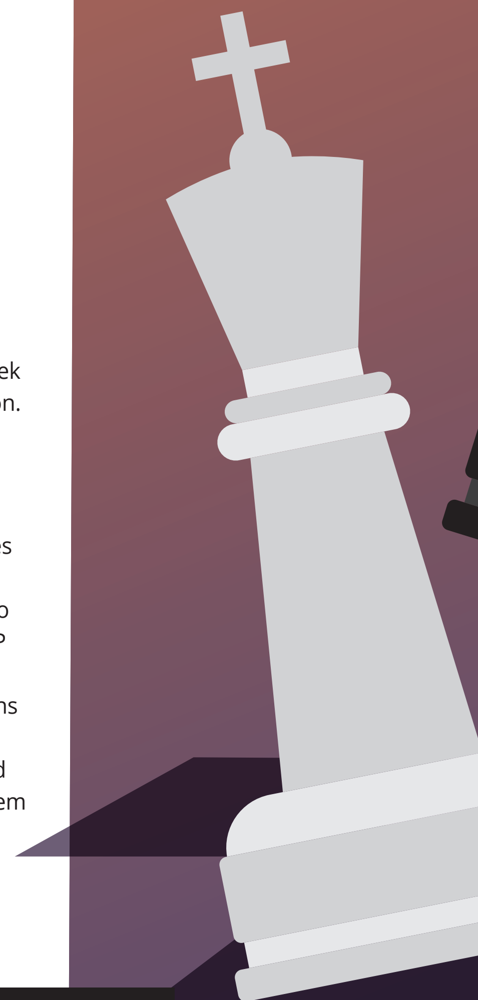
DB trustees – much to ponder in 2018

2018 looks set to be another busy year for DB scheme trustees.

Ideally, trustees should aim to be ahead of the game. Most schemes aim to secure at least some of their liabilities in time, but relatively few are "buy-out ready".

On top of the "business as usual" agenda items for DB schemes, trustees this year have until late May to put into place the necessary updates to their documentation and procedures to comply with the General Data Protection Regulation. More significant work could arise for DB trustees, however, depending on the particular circumstances of the scheme and its sponsor.



Scheme funding issues

For the majority of schemes, the impact of the financial crisis is still very much in evidence. Many trustees are faced with a significant deficit (often driven by continued low gilt yields) and a weak employer covenant. In these situations, the need for contributions to repair the deficit has to be balanced against the imperative not to jeopardise the long-term interests of the scheme by pushing the sponsor into insolvency.

In the current regulatory environment, schemes with a weak employer covenant are expected to de-risk their investments. This is intended to minimise the likelihood that the [funding position] will get worse, but it also increases the extent to which the scheme will have to rely on contributions from the sponsor if things are to improve.

De-risking schemes

De-risking the scheme's investment strategy, if it hasn't happened already, should be high on the agenda. Trustees of well-funded schemes may seek to lock in a favourable position.

Ideally, trustees should aim to be ahead of the game. Most schemes aim to secure at least some of their liabilities in time, but relatively few are "buy-out ready". Trustees who can address matters like GMP reconciliation, data cleansing and even benefit specifications in advance are far better placed to transact quickly and effectively. This may allow them to take advantage of pricing opportunities which would otherwise be missed.

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Liability management

Liability management exercises such as pension increase exchanges and enhanced transfer value exercises have been popular in recent years, and that trend looks set to continue. These are typically instigated by scheme sponsors but, as with insurance transactions, trustees who have anticipated the issues and started preparatory work will put themselves in a more comfortable position.

Most private sector DB schemes are now closed to new members, so although some will be around for decades to come, from the sponsor's perspective they are fundamentally a legacy issue which needs to be managed. 2018 will therefore continue the trend of sponsor-led proposals including changes to the basis of future accrual, closure to accrual or switching revaluation and/or pension increases from RPI to CPI.

For the time being, the legislative framework which is designed to protect members means that there are very few options available to restructure pension liabilities in a material way, even if doing so is manifestly necessary for the survival of the sponsor. However, 2018 might mark the start of change on this front: having consulted on the security and sustainability of private sector DB pensions in its Green Paper back in February 2017, the follow-up White Paper is due this spring. Its spotlight is likely to fall on scheme consolidation, benefit simplification and TPR's powers. But while these could be big news for DB in the long term, the DWP has already suggested that legislative changes are unlikely to come into effect before 2020.

By Tom Jackman, Associate Director, Sackers