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The Pension Insider is a monthly newsletter developed for Actuaries, Third Party Administrators, Attorneys and Consultants who work in the pension arena. The Pension Insider was created to share ideas, success stories, coming events and industry specific articles.

BCG Pension Risk Consultants and BCG Terminal Funding Company specialize in settling pension liability for terminating and ongoing pension plans.

Today's Solutions for Tomorrow's Needs.

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PSNC 2014: DB Plan De-Risking

From PLANADVISER

Jun 05, 2014 --- The effort to de-risk defined benefit (DB) pension plans is an immensely complex task that presents no shortage of challenges or opportunities to retirement plan sponsors and consultants.

De-risking is part art and part science, says Matthew Gnabasik, managing director at Blue Prairie Group. Gnabasik led a panel discussion on DB de-risking at the 2014 PLANSPONSOR National Conference, in Chicago. The panelists, who represented a number of insurance and consulting firms active in the pension de-risking market, suggested that de-risking requires a significant amount of planning and a sensitive trigger finger. It's a double matter of first putting the plan in the position to de-risk, and then monitoring conditions for the best moment to transact.

According to panelist Mike Devlin, a principal at BCG Terminal Funding Company, many sponsors are currently considering the different forms of de-risking, especially pension annuity buyouts, which involve transferring a part or all of a company's pension liability to an insurance company through annuity purchases. Prices for annuity buyouts fluctuate daily, he says, and can swing by 10% or 15% in the span of just a few months.

Beyond full or partial annuitization through an insurance company, other sponsors are working with their advisers and third-party consulting resources to implement liability-driven portfolios that seek to optimize the investment program according to the projected benefit liability, Devlin says. Rather than simply maximizing plan growth, these sponsors want to minimize portfolio volatility and avoid the major swings in plan funded status that have occurred in recent years, he explains, adding that a less volatile plan should also be easier to annuitize at a later date.

Marty Menin, director of Pacific Life Insurance Company's retirement solutions division, says many sponsors like the idea of a risk transfer, but they can be scared off by the buyout premiums that are involved. Premiums currently stand somewhere around 8% to 10% of the accounting liability, he says. In other words, sponsors will have to pay about 110% of the projected pension liability to move that liability completely off the books.

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A premium is inevitable, Devlin explains, as insurers need an incentive to take on the very real longevity risk associated with pension liabilities. But at the current juncture premium figures can actually be misleading, he warns, because insurers are already using new Society of Actuary mortality tables that predict longer average lifespans than the outdated tables currently used by the typical plan sponsor. This has the effect of inflating the buyout premium relative to the accounting liability.

Sponsors should also consider scheduled increases in Pension Benefit Guaranty Corporation (PBGC) premiums, Devlin adds, and the administrative expenses that aren't typically factored into the accounting liability (see "PBGC Premium Hikes Shake Up Buyout Landscape"). The result is that the projected cost of keeping pension liabilities on the books is too low for most sponsors, and therefore the true risk transfer premium is less significant.

"If sponsors consider the impact that new mortality tables and higher PBGC premiums would have on the actual size of the pension liability, the difference between that and the risk transfer cost offered by the insurer is going to shrink substantially," Devlin says.
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----------*Today's Solutions for Tomorrow's Needs.*----------

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