For pension-risk transfer (PRT), the issue of ‘if’ has been debated extensively. What’s been less covered is the ‘how.’ To discuss this essential component of PRT, Editor-in-Chief Kip McDaniel recently sat with MetLife’s Robin Lenna (EVP, Head of Corporate Benefit Funding), Wayne Daniel (SVP, Head of US Pensions) and Scott Gould (VP, Structured Solutions for US Pensions).

CIO: Despite the numbers involved, pension-risk transfer is still about people. So, the first step is identifying who, within the plan sponsor and the corporation, should be leading the charge?

Lenna: When considering a pension-risk transfer to an insurer, there is a mix of people—from the investment side to the treasury side to the human resources team—inolved in the process.

Daniel: Robin’s right. There are many important stakeholders. I think the CFO is key, particularly since accounting and regulatory pressures are at the forefront of their minds. That said, because of the size of many of these transactions—especially relative to the market capitalization of the plan sponsor—it is often even a CEO or board decision. Then there is a host of advisors—and often an independent fiduciary, for example—who participate and advise.

You end up with an internal team working on it in concert with all of the advisors. We recently had a discussion with a plan sponsor where the CFO was very keen to proceed with a PRT transaction—but the CEO, referencing the uncertain trading environment within his industry, said that at the moment he didn’t want to secure the retiree benefits with an insurer. So there are many different stakeholders, and they will discuss the right transaction and the right timing.

CIO: I find with the CIOs and the investment teams, the
largest ones generally prefer the hibernation or the liability-driven investing (LDI) route. Cynics—and I’m a cynic—would say ‘of course they prefer that because, in part, it retains their job.’ However, getting buy-in from the investment team will be essential in transitioning that portfolio. How difficult is it to get the investment team fully on board?

Daniel: I agree that tension can definitely exist, because you are moving from a situation where in-house resources were responsible for managing a large portfolio, to one where those responsibilities become outsourced to the insurance market. You’ve got that tension because it is going to impact some people within the plan sponsor.

But, if you look at the strategic evolution of pension plans, the old style where the CIO was looking for large outsized returns—especially back in the day when accounting rules included the pension returns in operating earnings—is no longer the way. There is too much volatility on the plan sponsor balance sheet, and the CFO doesn’t want to try to explain that to the investor community and other stakeholders. So, the investment strategy has evolved over time to become largely fixed income matching the liabilities. And, once you start moving down that de-risking LDI-type strategy, you are moving towards the next step: full de-risking to the insurers. It’s a spectrum of evolution.

Gould: I think it’s important to discuss volatility. A lot of these companies have a shrinking core business in relation to the size of the pension liability, meaning the pension can add volatility to the entire entity. Add in increased Pension Benefit Guaranty Corporation (PBGC) premiums, and it is often very material relative to the core business.

CIO: We’ve identified the decision makers internally. Let’s expand upon the swath of advisors involved once a PRT decision is made.

Daniel: The complexity and the size of the transaction drive the range of advisory services that become necessary.

At its simplest, some small transactions may be fine going directly through their pension plan actuary or advisor to the pension plan, directly to the insurance market. But, as you get a more complex plan with different benefit structures and significant investment considerations, then it becomes more of a risk for the plan sponsor not to engage an independent fiduciary and clearly separate the settlor function from the fiduciary function. Once you’ve engaged an independent fiduciary, they may say ‘Well, we’d like our own insurance, legal, and actuarial advisor.’

Gould: Typically, the structure of the process consists of a plan sponsor with their actuary and lawyers, the advisor—which may or may not be a bank or one of the big brokerages—and the independent fiduciary with their lawyers and actuaries. This is all necessary because they have very different perspectives that they must evaluate the transaction against.

CIO: Let’s discuss the financial analysis further. PBGC premiums are rising. You touched upon the size of the plan versus the market capitalization measurement. Tell me about the financial metrics that plan sponsors are looking at to make this decision. How are they deciding ‘It’s time to do this?’

Daniel: Affordability is the first one. The average plan is in deficit and so probably can’t afford to go to market and purchase a full buyout. So, a full termination may be a future aspiration—but may not be affordable today depending on funding level. The overall average funding level has been around 80% for the last few years.

But in terms of financial impact on the plan sponsor, the volatility and the plan sponsor’s financial reporting are unwelcome distractions from the underlying business. They’d rather focus on their business activities and the value that’s generating—and not whether their pension plan had a good or a poor investment year.

CIO: Let’s go on to cleansing participant data. How important is it? The devil’s in the detail, I’m sure.

Lenna: The process to de-risk can often take a number of years and a firm that has grown by acquisition may have accumulated many different plans. So having accurate information about your covered population, their status, and whether they are alive or dead—it’s clearly important and can have a meaningful impact on the cost of the PRT transaction.

Daniel: For some plan sponsors, cleansing participant data in advance of a PRT transaction can be time-consuming because they could have decades of data in filing cabinets that’s not digitized, and it could be incomplete or inaccurate. We would advise any plan sponsor who may be contemplating PRT in the future to embark on and complete a ‘data audit’ to cleanse their participant data sooner rather than later.

CIO: Another thing on the plan sponsors’ to-do list of things I had never thought of before: The feasibility study. What does that entail?

Gould: The feasibility study is a quick assessment of what’s really involved in a pension de-risking transaction. Can we afford it? It looks at not only the dollar cost, but also the time and effort. Do we understand the process? A simple feasibility study will ask ‘What is our funding level, what can we afford to do, and what would the likely insurance cost be?’

But, before you can move from the feasibility study to a full process, you need a review of your data, your investments, and your decision-making governance process. You don’t want to go out to the insurance market too early. This is where pension advisors have been good in saying ‘We know the standard of data the insurers are going to request before you get competitive quotes. We know what the asset portfolio should look like before you can really contemplate an assets-in-kind de-risking transaction.’ I think the feasibility study is really to set the framework for
The process to de-risk can often take a number of years... so having accurate information... is clearly important and can have a meaningful impact on the cost of the PRT transaction. —Robin Lenna

An increasing number of transactions are seeking to settle assets-in-kind, or a mix of assets-in-kind and cash. —Scott Gould
Unable to actually post it to payroll, make the correct deductions, or get the correct documentation to the participant.

**CIO:** Editorially, we’ve always looked more at the cost and the big things. We haven’t discussed participant communication and service. Is this underplayed yet really important?

**Lenna:** In many cases, it’s very important. In fact, we commissioned a PRT poll of large plan sponsors last year. Nearly one-third of plan sponsors (31%) indicated that communication was the most important factor for ensuring PRT success, followed by the price/cost of the transaction (26%), among other factors. Communications can help participants feel confident that their benefit will be there when they need it. That’s why many plan sponsors put a lot of resources into participant communication.

The most important aspect of communications is for participants to know that a risk transfer to an insurance company, where the benefits earned are preserved in exactly the same form, does not represent a risk transfer to the participant in any way. The only thing that changes is the entity from which they are receiving their retirement income payments.

**CIO:** With more players entering the market, is the price coming down?

**Daniel:** Each and every deal is competitive. But regardless, there is always price competition for every transaction. Even if you only have one insurer bidding on it, the plan sponsor can choose not to transact. Unless the insurer is meeting the plan and plan sponsor’s expectations, you’re not going to have a transfer to the insurance market.

**CIO:** Next on the list: finalizing contracts. What are the pain points in finalizing the contract once plan sponsors put the RFP and that they’ve chosen the winning bid?

**Gould:** It’s become much more routine. The number of law firms that participate in this is pretty small and they deal with issues that may arise, such as material adverse change clauses and certain limitations of liability transfer in the normal course of business.

Assets-in-kind transfers add a certain degree of complexity—and an increasing number of transactions are seeking to settle with assets-in-kind, or a mix of assets-in-kind and cash. In fact, MetLife has carved out a specialty for accepting certain assets that other insurers may not be willing to analyze or accept.

**CIO:** I imagine that once this is all done, the transition—from the outside—looks like the heavy lifting has been done. I imagine that from the inside that’s not the case. There’s a whole lot of work that goes on as you implement this and put it into action. Same question there: What are the pain points?

**Daniel:** Once the insurer is selected, then the hard work begins. The main stages of the transaction are the transfer of data, the transfer of assets or the premium, and then the transfer of the contracts. So, the work stream on the data, the work stream on the premium payment and the assets, and the work stream on the contracts are run simultaneously.

**CIO:** We’ve already spoken about communication with retirees. Let’s take a step back, though: Is it truly done for the plan sponsor? Let’s say a retiree in Wyoming is now working with MetLife: Does the company ever have to interact with that person again or is it all you?

**Lenna:** PRT transactions, including implementation, are customized to fit the needs of the plan. There’s a welcome packet, and there’s a handoff. If retirees still call the company about pensions, the company will redirect them to us. We’ll set up our call center interaction to the specification of the plan sponsor, so it will be seamless to the retirees. It’s one of the benefits of doing a lot of these transactions and being in the business a long time. MetLife currently manages nearly $38 billion of transferred pension liabilities. We have developed a reputation for our experience in successfully administering complex plans and providing a superior participant experience.

Unless the insurer is meeting the plan and plan sponsor’s expectations, you’re not going to have a transfer to the insurance market. —Wayne Daniel

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