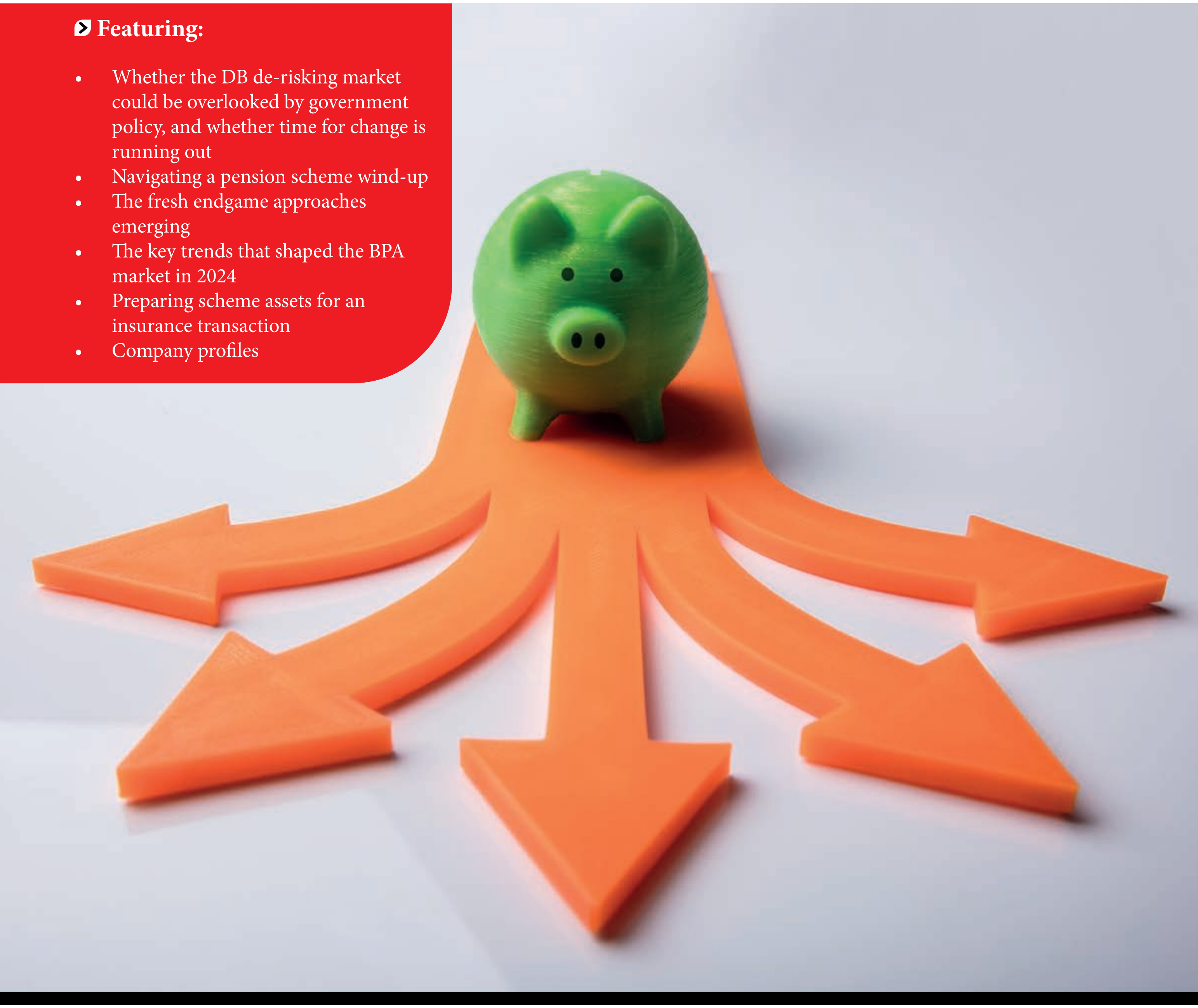
De-risking Guide 2024:

The many paths to choose

Featuring:

- Whether the DB de-risking market could be overlooked by government policy, and whether time for change is running out
- Navigating a pension scheme wind-up
- The fresh endgame approaches emerging
- The key trends that shaped the BPA market in 2024
- Preparing scheme assets for an insurance transaction
- Company profiles



Summary
- The DB de-risking market has been thriving in recent years, as scheme sponsors sought to lock in recent funding improvements, with more money transitioning from the pension industry to the insurance sector.
- Some schemes are still adopting a 'wait and see' approach while awaiting further clarity on DB surplus sharing rules, although many have already set their endgame strategies.
- Industry experts have raised concerns that this lack of clarity could therefore limit the DB sector's ability to help meet the government's intent to increase UK investment.

Too little, too late?

The DB de-risking market has seen record-breaking volumes in recent years, but is the DB space being overlooked by broader government policy, and is time for change running out? Sophie Smith reports

The DB pension market has faced growing scrutiny in recent years, after being thrown into the spotlight amid the 2022 gilt crisis, as headlines claimed that the sector was "on the brink of collapse".

But it seems reports of the death of DB were greatly exaggerated, and the significant funding improvements seen in the wake of the 2022 mini-Budget opened the door for record-breaking volumes in the bulk purchase annuity (BPA) market, as DB schemes and their sponsoring employers took the opportunity to de-risk.

Indeed, Standard Life BPA transaction manager, Alex Oakley, says that the BPA market has continued to thrive this year, with volumes expected to top £40 billion yet again.

"In addition, the pipeline of 2025 transactions is very strong and we are continuing to see strong demand from pension schemes of all size for insurance de-risking solutions," he says, highlighting this as demonstration that trustees and sponsors continue to see BPA as a secure home for members' benefits.

But the government's focus on DB has been dwindling, as the limelight recently shifted towards DC and the LGPS, in line with the focus of the government's Pensions Review.

And whilst the BPA market has continued to thrive, updates on alternative endgame options and broader DB changes have been sparse, despite industry calls for greater clarity around DB surplus rules.

A forgotten market?

In particular, whilst industry experts urged Chancellor, Rachel Reeves, not to overlook the role of DB pension schemes, the sector was omitted from her inaugural Mansion House speech to the disappointment of many in the industry.

"It is a shame that the recent Mansion House speech had no mention of possible changes in this area, as clearly the window for schemes to consider changing their long-term targets (or objectives) has a finite period and the longer the government remains silent on this issue the harder it will be for schemes to justify not securing their benefits with an insurer," XPS Group partner and head of investment risk settlement, Sian Pringle, says.

However, M&G associate director, corporate risk solutions, Max Koe, says that the group has seen some evidence of trustees and sponsors adopting a 'wait-and-see' approach in order to better understand the implications of any regulatory changes.

Pringle agrees, revealing that discussions about what the outcome of some of the various government consultations around the DB surplus sharing rules might mean for them has "undoubtedly" piqued the interest of a few schemes who are now considering run-on in the short term to see where these rules might land.

But with the BPA market showing no signs of slowing down, and limited progress on the clarity needed to encourage greater run-on, there has been some suggestion that the UK government could be 'missing its window' to make the most of DB investment in its push to encourage greater investment in the UK.

"Without unlocking the potential for run-on soon, it is hard to see that DB schemes will be able to provide sufficient investment in long-term growth assets to have an adequate impact on growth in the UK economy which could also lead to better outcomes for members," Pringle warns.

And whilst the government has been focused on how DC and LGPS investment could help address the £22 billion blackhole left in public finances, industry estimates suggest that 2024 volumes to date are around c.£40 billion, thanks to a number of 'megadeals'.

However, Isio partner, Steve Robinson, points out that the assets involved in these transactions are consolidating within the insurance sector, where the government can play a role in creating opportunities for productive investment.

"There are already billions of pounds in the insurance sector that could be allocated to suitable UK investments, even before the forecasted record-breaking wave of new business," he says.

Indeed, Koe also points out that, when a scheme transacts a buy-in, the insurer will typically invest those gilts or other de-risked assets into corporate bonds and private 'productive assets' such as infrastructure, social housing and the green economy, much of it in the UK.

Allowing the market to thrive

Whilst discussion around the potential public sector consolidator (PSC) has slowed since the general election, it has not been ruled out, with the Pensions Minister recently suggesting that further updates on this idea could be seen "in the coming months" *[read more about the PPF's latest thoughts on a potential PSC on page 56]*.

But recent record-breaking volumes in the BPA market have prompted industry experts to caution the government against these plans.

Indeed, M&G associate director, corporate risk solutions, Max Koe, says that the BPA market is a competitive and thriving market, with "significant innovations" over the past few years.

"Market consensus from advisers suggests that a vast majority of schemes that approach the BPA market are able to receive affordable buy-in quotes from a number of insurers, and competition at the smaller end of the market in particular has increased significantly, which can only benefit trustees," Koe continues.

"We would expect any public sector consolidator to be focused on schemes that are not well-served by the insurance market, i.e. they would not be looking to cover the same schemes that insurers already do."

Isio partner, Steve Robinson, echoes this, arguing that the BPA market is already responding to accommodate these needs, although new entrants face barriers to entry such as regulatory requirements.

"Capacity in the bulk annuity market is at an all-time high, and operational consolidators already serve small schemes," he states. "Furthermore, most new entrants to the BPA market have explicitly stated their focus on smaller schemes. The market is demonstrating its ability to provide solutions without the need for a public sector intervention."

XPS Group partner and head of investment risk settlement, Sian Pringle, also says that there has been little evidence of barriers to scheme's getting quotes, revealing that, every single scheme that XPS has taken to market over the past two years has managed to get competitive insurer pricing.

"However, if the PPF considers extending its role to provide stewardship and support to insolvent sponsors' schemes that are well-funded but cannot afford to transact with an insurer imminently. It could assist those schemes to buyout over the medium term providing better outcomes for members," Pringle acknowledges.

Shifting policy focus

But this could make policy changes in the insurance sector a more attractive option than DB policy changes, if the government is looking to encourage greater investment in the UK.

In particular, Robinson says that, given insurers must comply with PRA regulatory constraints, the government could help by enabling the development of appropriate investment opportunities, such as addressing the non-Matching Adjustment complaint equity component.

Creating more options

Industry innovation could also prompt a shift in strategy, as M&G recently agreed the market's first BPA deal to share value with a corporate sponsor with an unnamed UK pension scheme.

The deal was completed using M&G's newly launched Value Share BPA proposition, which was designed to allow trustees to insure the scheme in exactly the same way as a traditional buy-in transaction, whilst also allowing corporate sponsors to participate in the risk and reward generated from insuring their DB scheme.

Indeed, Koe says that the mindset of sponsors seems to be a shifting and many are considering how they could participate in the potential profit created by schemes approaching the insurance market.

And whilst larger schemes are thought to be the main target for run-on, Koe confirmed that group will also be targeting larger DB schemes for its Value Share BPA proposition, with future transactions expected to be at least £1 billion in size.

"We see our Value Share BPA proposition working within the definition of run-on, given the sponsor is retaining skin in the game over a long-time horizon but providing trustees and members with the ultimate security of a buy-in," he states.

Written by Sophie Smith

Navigating a pension scheme wind-up

How to balance member, sponsor, and trustee interests when implementing a scheme wind-up

Insurance buy-in transactions are a large and growing part of the pensions industry. Yet, while there is often a strong emphasis on executing the transactions efficiently, there can be less focus on the subsequent process of completing the buyout process and winding up the pension scheme. In some cases, a lack of resources and inexperienced teams can lead to direct impacts for your scheme members, the sponsor and pension scheme trustees alike. So, how can you ensure all parties have a positive experience?

Placing members at the heart of the process

Winding-up a pension scheme can be an unsettling time for members if the process isn't handled with care. With their benefits transitioning to be paid by a different party, the loss of the familiarity of regular newsletters and potential changes to terms for options such as transfer values, it's easy to see how members might feel uneasy.

The wind-up is also the last chance for the trustee to interact with its members so effective communication is essential to ensure a positive member experience. At worst, a complaint from a member about their benefits or the process followed could delay the whole wind-up so it's crucial to ensure members have confidence in the action taken.

Steps to help:

- Craft a clear member communication strategy
- Implement a well-managed project plan – to ensure you deliver on what you've told members you'll do; and
- Manage a smooth payroll transfer with the insurer – so members have confidence in the insurer from day one.

What sponsors need to know

From a sponsor perspective, winding up a closed defined benefit pension scheme removes balance sheet risk and helps control costs.

However, the complexities and costs associated with the buyout and wind-up phases can lead to frustration, especially if timelines aren't clearly communicated and progress is slower than expected.

There can also be difficult conversations over topics such as return of surplus, who carries the risk for any historical errors or future claims, and the tricky task of managing budgets.

Steps to help:

- Clearly outline the key tasks, timelines and budgets up front, ideally before the buy-in is signed so all parties understand the process
- Maintain regular communication between the sponsor, trustees and advisers to monitor progress
- Work collaboratively to address any challenges, with all parties understanding and acknowledging their respective interests.

Supporting trustees on the journey

Trustees can often feel a sense of relief when a buy-in transaction is completed. Securing all benefits in full with a regulated insurance company is a milestone for any pension scheme.

However, it's crucial to keep momentum as there are priority tasks at this point, including communicating with members, potentially implementing new member option terms and ensuring there is no risk that the trustee bank account will run dry.

Moving forwards, trustees will also need to keep a close eye on progress of the data cleanse process, as well as grappling with technical areas such as surplus refunds, GMP equalisation and legal uncertainties like the recent Virgin Media case. Not forgetting there are often other member benefits to secure outside the scheme such as AVCs or DC funds and historical annuity policies.

Trustees will also need to ensure they have adequate protection in place through trustee indemnity insurance and/or a sponsor indemnity in case a claim were to arise at the end of the wind-up process.

Steps to help:

- Set clear project plans, budgets and regular reporting so all parties hit the ground running post transaction
- Obtain practical advice from experienced specialists on technical areas and common issues; and
- Initiate discussions early to ensure robust trustee protections at the end of the wind-up process.

Ensuring a seamless transition

Transitioning from a buy-in to buyout and full wind-up is one of the most involved projects trustees and sponsors will face. Success hinges on a thorough understanding of the process, an actively managed plan and robust reporting – all overseen by experienced specialists. By doing so, you can achieve a smooth process with better outcomes for your members.

Written by LCP partner and post transaction lead, Rachel Banham, partner, Ken Hardman, and partner, Julian Jones

Opportunity in the endgame

What's next for DB pension schemes?

As UK defined benefit (DB) pension schemes mature, trustees face a pivotal moment: securing members' futures in a dynamic market. With new pathways like superfunds and an increasing focus on liability-driven investing (LDI), fresh endgame approaches are clearly emerging.

The past two years have transformed the UK's 5,000 DB schemes. Trustees face changing funding, rising interest rates, and macroeconomic uncertainties. However, amid these challenges there are some strong, new opportunities.

State Street Global Advisors, in partnership with Van Lanschot Kempen Investment Management and Clara-Pensions, surveyed 100 UK corporate DB scheme trustees in Q3 2024 to understand these dynamics and what schemes really want. All schemes were closed to new members; 52 per cent were also closed to accrual, and 52 per cent were 90 per cent funded or higher.

Finding the right strategy

The survey revealed no single dominant endgame path. Indeed, while traditional strategies like buyout (43 per cent) and run-on (38 per cent) remain popular, newer options, such as superfunds (10 per cent) and capital-backed journey plans (7 per cent), are fast gaining traction. Run-on strategies – which allow schemes to operate independently using robust funding and investment strategies – are challenging buyout's long-held gold standard perception.

Trustees identified three main challenges in setting an endgame strategy:

1. **Volatility and macroeconomic uncertainty (23 per cent)**
2. **Balancing stakeholder and member expectations (19 per cent)**
3. **Risk management and timing (18 per cent)**

While trustees generally feel well-informed about buyout (89 per cent) and run-on (91 per cent) options, they report knowledge gaps for less conventional strategies like superfunds (74 per cent) and capital-backed plans (55 per cent). A small but significant minority of trustees are targeting consolidation (10 per cent) and capital-backed journey plans (7 per cent) as their endgame strategy.

The role of scheme sponsors adds complexity. Nearly half (45 per cent) of trustees report shared influence between sponsors and themselves, while 17 per cent believe sponsors are more influential. External advisers are often brought in for endgame planning (68 per cent). This negotiation between sponsors and trustees requires careful balancing of multiple perspectives, often relying on third-party advice.

The growing role of superfunds

Superfunds have emerged as a compelling alternative endgame for schemes seeking to enhance member outcomes while lowering sponsor costs compared to buyouts. By consolidating multiple schemes under one trust, superfunds pool resources to create stronger financial foundations, improve governance, and potentially replace weaker sponsor covenants.

The appeal of superfunds lies in:

1. **Improved member outcomes (66 per cent)** – resource pooling and governance can secure or enhance benefits.
2. **Lower cost to sponsors (52 per cent)** – economies of scale free up resources compared to buyouts.
3. **Replacing weak covenants (31 per cent)** – particularly relevant for schemes with weaker financial backing.
4. **Access to additional funding (27 per cent)** – supporting the scheme in the short term.
5. **Governance improvements (24 per cent)** – consolidated governance offers robust oversight.

Trustees see superfunds as particularly advantageous for schemes with weak sponsor covenants, with 50 per cent citing this as a key factor. However, for schemes with strong covenants, only 27 per cent view superfunds as appealing.

Despite growing interest, participants cited: Financial stability and risk management (17 per cent), protecting member outcomes and choice (17 per cent), regulatory uncertainty (12 per cent) and lack of trust and familiarity (12 per cent) amongst the obstacles faced.

Addressing these concerns will be critical for broader adoption. Many trustees worry about the newness of superfunds and cite regulatory uncertainty as a challenge.

Nonetheless, 55 per cent of trustees expect a rise in schemes transferring to superfunds within the next two years, with 61 per cent believing superfunds could deliver better outcomes than insurers for schemes exiting Pension Protection Fund assessments.

Liability-driven investing (LDI): A cornerstone of endgame planning

For DB schemes nearing their endgame, LDI plays a pivotal role in aligning assets with liabilities. LDI mitigates risks from interest rate changes and inflation, and an estimated 60 per cent of DB scheme portfolios being LDI-aligned.

However, recent events have also highlighted vulnerabilities in LDI strategies. The 2022 UK gilts crisis exposed liquidity risks, prompting many schemes to review their LDI managers. But, while 77 per cent of trustees have reviewed providers, only 23 per cent switched, citing concerns such as institutional knowledge loss (45 per cent) and governance disruption (39 per cent).

Trustees are starting to expect more from their LDI

LDI provider concentration is strongly on trustees' minds: With a few players dominating the market, 81 per cent of trustees are concerned that this lack of competition weakens service quality. Additionally, 80 per cent believe limited competition drives up fees, while 78 per cent worry the high concentration of providers may lead to inadequate servicing in a future market crisis.

Evidently, schemes are traditionally underserved by their LDI managers, and many are beginning to expect more. Risk management is the key area where trustees want their LDI managers to improve, such as through more bespoke hedging, robust stress testing and liquidity management, with 31 per cent saying this is the key change they wish to see in the LDI market. Nearly one-fifth (18 per cent) also want to see better communication and reporting.

A technology-led approach to LDI portfolio management may help providers alleviate these pain points. Integrating real-time analytics into portfolio management can give schemes greater portfolio visibility, allowing their status to be viewed as needed. This technological approach could also address the gaps in service delivery and communication, streamlining regular reporting and thus increasing the capacity of LDI portfolio managers to respond to specific client needs.

Conclusion: Opportunities amid transformation

The current environment presents an important opportunity for the trustees of DB pension schemes to reconsider and redefine their strategies. From buyouts and run-on strategies to newer pathways like superfunds and capital-backed journey plans, trustees must leverage this expanded market to make informed, member-focused decisions that balance sponsor and stakeholder interests.

At the same time, trustees should push for higher standards from LDI providers, particularly since market concentration is perceived to impact service quality. Real-time analytics, improved risk management, and streamlined reporting can strengthen LDI portfolios, enhancing trustees' ability to meet endgame goals.

By embracing a proactive, technology-driven approach, trustees can secure a more resilient future for members. The endgame market is evolving rapidly, and trustees have the opportunity to shape its direction, ensuring that member benefits remain squarely at the heart of their strategies.

Reflecting on 2024: Key trends that shaped the BPA market

Joe Haswell, BPA transaction manager at Standard Life, part of Phoenix Group, shares his views and discusses trends he observed in bulk purchase annuity origination over 2024

Relative to some lofty predictions at the start of the year, the consensus expectation that around £45 billion of bulk purchase annuities (BPAs) will be written in 2024 sounds pedestrian. For the first quarter of 2024 the pace did feel more like a stroll than a sprint, with the trickle of medium and large transactions (£100 million-plus) attracting near-full insurer participation, which has been uncommon over the past couple of years. The trickle became a flood with spring's arrival; thereafter, the market has been busy and closing in on near record volumes.

Are schemes trying to time the market for a better price?

The market for medium and large transactions feels back-end loaded each year, and looking at transaction volumes that is historically true. I reviewed our records since 2020 and filtering for schemes over £100 million in size that are targeting same-year execution, the number of request for quotes received in Q1 has remained broadly stable, while those received after has gradually increased by half over time. It confirms what I thought, requests ramp up around the start of summer, most often from schemes looking to sign in early winter.

It's hard to tell if this is by design, chance or a natural result of governance cycles; there's certainly a view among some that waiting can lead to better pricing as insurers compete to meet annual targets towards the end of the year. I'm sceptical of that, particularly for small and medium schemes, as insurers have limited human capital. Schemes may find that they receive fewer quotes than if they had approached the market earlier in the year. Nonetheless, both the large and small transactions we participated in from Q2 onwards have attracted multiple quotes, helped by consultancies and insurers remaining flexible and adapting to the most suitable timetables.

The market has coped well with high demand from small schemes

A key trend for 2024 has been the sheer number of bulk annuity policies written. The six months to June saw the greatest number of deals completed in any half-year, which is despite the general trend for greater second-half volumes. While volumes might fall short of record levels, I expect the number of transactions to comfortably set a record this year. This has been driven by schemes under £100 million approaching the market and finding it better serviced than ever before, with four established providers quoting regularly on small schemes and new entrants looking to find their feet in this segment of the market. I expect this trend for a greater number of smaller trades to continue into 2025 and beyond: out of the c.5,000 total universe of UK DB schemes, roughly two-thirds of pension schemes are under £100 million in size. However, transacting and subsequently transitioning buy-in policies to individual policies is time consuming regardless of size, so increasing numbers of smaller transactions will need to be accompanied by continuous investment from insurers into their pricing and onboarding processes.

Insurers are increasing operational capacity, but there's no golden bullet (yet)

Human capital remains one of the key constraining factors for the risk transfer market. Specifically for transactions, it means insurers cannot quote on every opportunity and need to be selective. The straightforward approach to increasing capacity is growing the team, and we have done this in 2024 by hiring across the full spectrum, from experienced hires to school-leavers. We have also focused heavily on using technology to improve team efficiency, by building a team whose main focus is on improving our platforms and processes within bulk annuity pricing.

Generative AI has been touted as a technology with the potential to revolutionise how we prepare quotes and cleanse data. In the medium and long term, I think this is true. However, I've yet to see an off-the-shelf product for BPA quotations. There would need to be – amongst other things - strong controls to protect confidential and restricted data before any is implemented, so it might be some time until it's possible to feed raw data and benefits in and get a premium out. For me at least that's a good thing; my house keeps finding new ways to leak, so I need the work. In the short term, there could be some quick wins for efficiency from generative AI, such as finding information from simple databases, summarising information and for drafting written communication (not for this article, but I did try it).

Schemes are better prepared

Schemes and their advisers can also do their part in increasing capacity for writing new business, by coming to market well-prepared and with clear objectives. Over 2024 the trend of schemes being better prepared has continued from previous years, particularly at the smaller end with respect to data and benefits.

Schemes are also increasingly coming to us with a solution for illiquid asset holdings already decided and in progress, or alternatives available to assess the value of insurer solutions against. Time has passed since the rapid increases in funding levels seen over 2022 and into 2023, which saw some schemes reach buyout affordability sooner than expected and subsequently transacting quickly to take advantage of this. Funding levels have been relatively stable since, and schemes that have taken more time to come to market have had time to explore solutions outside of the BPA process. Moreover, the industry's collective experience on dealing with illiquid assets has improved, meaning advisers and insurers can offer a wider range of solutions.

Full-scheme transactions dominate

Partial scheme buy-ins, where schemes insure only a portion of their membership, dominated our pipeline five years ago. Like 2023, partial buy-ins remained in the minority this year and are often reserved for the very largest of schemes which are insuring liabilities in (still very large) chunks. When the occasional pensioner-only buy-in is discussed at the triage meeting, the room becomes very nostalgic! No doubt improved scheme funding positions have meant a series of partial buy-ins is no longer required, but the narrowing pricing differential between pensioner and deferred members will have played a part too.

With full scheme buy-ins, the timeframe for the scheme to transition to individual policies is typically shorter and the moment that scheme members will become individual policy holders is more tangible. Coupled with more schemes expecting to retain a surplus after buying out, trustees and their advisers are putting ever greater importance on member experience when choosing an insurer.

If full scheme buy-ins are good, why not do a double?

Another notable theme in 2024 was for separate schemes which share a sponsor, or whose sponsors have some corporate relationship, approaching the market as a single process. This has been a favoured approach for some time, in order to bring a larger total transaction size to the market as a single process with the aim of driving greater insurer interest. This year, it has been more common and with more distantly related schemes. I expect setting up efficient governance processes under this approach takes some patience, but they are effective and take only marginally more time than a single policy to execute.

Looking forward

Typically, January would see a lull of activity, but we are already working on a number of proposals due promptly in the new year, so I'm expecting the pace to start quickly next year. In my view the market can comfortably support record volumes of £50 billion-plus, but for these to be hit we would need to see a return of more £2 billion-plus transactions, which were relatively uncommon in 2024. Even at record volumes, I am expecting pricing to remain highly competitive, and I will be interested to see whether the recent (re)entrants affect that as they look to build a market share.

But for now, as we get to the end of the year, I hope everyone in the market gets some time to wind down and pursue other interests. Personally, I will be experimenting with some market-timing of my own, waiting until the right moment to buy large numbers of tulip bulbs for a pittance.

Written by Standard Life BPA transaction manager, Joe Haswell

In association with

Standard Life
Part of Phoenix Group

Pre-transaction planning: Getting asset-ready

Preparing scheme assets for an insurance transaction is one of the key steps trustees need to take to get their schemes ready to go to market, but what does this mean in practice?

There are several key considerations that go beyond the value of the assets required to pay an insurance premium.

Should/can the assets of the scheme be reshaped to make them more suitable for an insurance transaction?

Many smaller transactions have a premium that is paid in cash and gilts only. Often, schemes will have such assets as part of their asset portfolio. Larger transactions may have a premium that can also be paid using corporate bonds, synthetics (such as derivatives) and other more complex assets.

If the assets of the scheme need to be transitioned, who will do this? It could be an existing manager, or the trustee may need to appoint a dedicated transition manager. In either case, trustees should liaise with their investment and legal advisers to prepare a transition plan. Where possible, early engagement with the insurer can help to ensure that when the scheme enters price-lock, its assets are in good shape.

A note of caution here is what happens if the transaction does not go ahead for any reason? Are the transitioned assets the sort that trustees would want to hold long term? Would they be suitable for transacting with a different insurer?

Can the assets be transferred to the insurer, and will the insurer want those assets?

Scheme assets will be subject to pensions-specific regulations, which insurers are not subject to. Similarly, the assets of an insurer will be subject to insurer-specific regulations, which pension schemes are not subject to. This impacts the desirability of certain types of assets from an insurer perspective and whether an insurer will want to hold assets itself for the longer term. This, in turn, can have pricing implications. Whilst trustees don't need to have a detailed understanding of the regulatory and capital requirements of the insurer, having a working understanding will help to assist in a smooth transaction, and might also inform the decisions that are taken to re-shape assets pre-transaction.

How will the assets be transferred to the insurer, or realised for cash?

Assets held directly, albeit in custody, can normally be transferred to an insurer on instruction. However, there will be different requirements and settlement periods for different types of assets. Trustees should ensure they have a detailed plan for the asset transfer process, as well as a contingency plan to deal with any assets that fail to transfer.

For assets that need to be sold in advance of an insurance transaction, how will this value be realised? For investments held indirectly, for example in a pooled fund, trustees are unlikely to have any rights in respect of the underlying asset and so will need to redeem their fund interest instead. This will require consideration of the permitted redemption dates as well as any restrictions on the number of interests that can be redeemed on any date. For synthetic assets (for example derivatives used as part of a scheme's LDI strategy), often these will need to be 'closed out' for a cash value, which will require advance engagement with counterparties.

Illiquid fund assets – case study

A key focus in recent years has been in relation to illiquid fund interests held by pension schemes (e.g. in private equity or private credit). Many insurers are reluctant to accept such assets, meaning that trustees will need to arrange a sale in what is known as the secondaries market.

Trustees are unlikely to have a unilateral right to sell an illiquid asset and so will need to engage with the relevant manager to obtain its consent. In advance, the transfer provisions (and any conditions that apply) and any applicable restrictions will need to be considered. These may include other investors having a right of first refusal or a right of first offer. There may also be restrictions on who the asset can be sold to, limiting the number of potential buyers for the asset.

Trustees may wish to appoint a specialist third-party broker to help with marketing the illiquid asset, providing advice on valuation (because it is unlikely that there will be a public price) and to support the transfer of the illiquid asset.

Once a buyer has been sourced, and consent has been obtained from the manager, a secondaries transaction operates like a mini M&A transaction. There will be various transfer documents and, importantly, a sale and purchase agreement, which will deal with considerations such as any liabilities retained by the trustees and the taxes that are payable.

A final practical point to note is that it is likely to be challenging to sell an illiquid asset during any price-lock period. This should be factored in

through early engagement or, in certain cases, by reaching agreement with the insurer to defer a portion of the consideration payable until the asset is sold.

Surplus assets on wind-up – a nice problem to have?

Having done the hard work to ensure that assets are transaction-ready, what happens if trustees end up having more than they need? Dealing with a surplus on wind-up is something that an increasing number of trustees are having to get to grips with.

There is no one-size-fits-all solution, and the options available in relation to use of surplus will depend on a number of factors. Some key issues to consider are:

• **Is there really a surplus?** Trustees and sponsors will want to have a clear picture of the likely amount of any surplus, after taking into account expected expenses, premium adjustment or other contingency that may be needed to deal with data cleanse or other benefit issues.

• **Who owns the surplus?** What scheme rules say on this point will be key, but reputational risk can also play a part in shaping any agreement about how surplus is used. It is a legal requirement that members must be notified about any proposal to return surplus to an employer on wind-up and given an opportunity to make representations. Experience to date indicates that some trustees and sponsors are open to revising proposals about how surplus is used in response to feedback from members.

• **Benefit augmentations** Trustees and sponsors might want to consider whether part or all of any surplus could be used to augment member benefits. Scheme rules should be reviewed carefully when weighing up this option.

Careful planning is needed to decide what form a benefit augmentation will take and when. A key consideration for trustees will be ensuring value and fairness between different cohorts of members. Other factors (including potential tax implications) may also be relevant to the shape of benefits provided.

Trustees don't necessarily have to pin down details of any augmentations at the point of transacting, but if benefit augmentations are likely in future, it is advisable to build flexibility into the contract terms agreed with any insurer upfront so that these can be reflected in the benefits secured at buyout.

• **Payment of surplus to an employer** Where surplus is being returned to a sponsor, the timing of any payment will be important to ensure that the scheme retains sufficient assets to cover the costs of buyout and wind-up. Return of surplus does not always need to take the form of a cash payment. Different considerations (including in relation to tax) will apply if surplus is being returned in other forms, for example, through transfer of an illiquid asset.

For trustees preparing for an insurance transaction, the message is clear: plan ahead. Ensuring that scheme assets are of the right type and in the right place at the right time will be key to ensuring that a scheme is in the best possible position to transact.

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Company Profiles

LCP

LCP helps clients to create and uncover new possibility by distilling clarity from complexity; fusing human expertise with powerful analytics to shape a more positive future. LCP is powered by bright and passionate people with a relentless sense of curiosity.

We are a tech-enabled consultancy known for our market-leading advice in pensions, investment and insurance, and we strive to help create a financially better future for our society. Our love of data, technology and posing solutions to the difficult questions of today, has taken us into newer areas. We now have a reputation for excellence in energy transition, health analytics and sport analytics.

As well as our award-winning pension risk transfer team, we have a dedicated post transaction team, which provides strategic advice and project management support to successfully move schemes to buyout and wind-up after a buy-in.

We provide structure and accountability to these multi-strand projects – coordinating stakeholders efficiently and offering practical solutions to any issues – allowing clients to focus on the important decisions relating to members' benefits, treatment of any surplus and managing residual risks.

Our specialist post-transaction team brings detailed technical knowledge, a wealth of experience and strong relationships with all the insurers in the market to provide clients with the confidence that their wind-up is in safe hands.

We draw on the expertise of wider LCP services (including our pension risk transfer team, data services, DC and our specialist trustee liability insurance broking team) to provide additional support to help ensure a successful outcome within desired timeframes.

Our well-established team is unique in its range of skills, depth of experience and robust project management capabilities. We have worked on over 100 wind-up projects for schemes ranging in size from £1 million to more than £1 billion.

State Street Global Advisors (SSGA)

For over four decades, State Street Global Advisors has served the world's governments, institutions, and financial advisors. With a rigorous, risk-aware approach built on research, analysis, and market-tested experience, and as pioneers in index and ETF investing, we are always inventing new ways to invest. As a result, we have become the world's fourth-largest asset manager* with US $4.73 trillion† under our care.

**Pensions & Investments Research Center, as of 12/31/23.*

†This figure is presented as of September 30, 2024 and includes ETF AUM of $1,515.67 billion USD of which approximately $82.59 billion USD in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

Standard Life

Standard Life is a brand that has been trusted to look after people's savings and retirement needs for nearly 200 years.

We're part of Phoenix Group, the UK's largest long-term savings and retirement business. We share an aligned ambition to help every customer enjoy a life full of possibilities.

People are living longer and we can support them at every step in their financial future. We know we can't achieve this without doing our part to build a strong and sustainable future. It's why we are integrating sustainability into everything we do; from incorporating responsible investing into our solutions, to fostering an inclusive savings culture and improving financial wellbeing for all.

Standard Life's Defined Benefit Solutions support us on this mission, providing tailored bulk annuity solutions to DB pension schemes. We pride ourselves on thinking outside the box, finding innovative solutions to meet the needs of our clients.

Standard Life
Part of Phoenix Group

Travers Smith

Travers Smith has a market-leading pensions practice advising some of the UK's largest pension funds, corporate sponsors, and established and emerging de-risking providers on all types of pensions risk transfer transactions.

We offer our clients a genuine multi-disciplinary approach provided by a fully integrated team where lawyers work closely together across all of the legal specialisms our pensions clients need including investment funds, derivatives and structured products, financial services and markets, corporate finance, private equity, finance, tax, employment, outsourcing and commercial contracts, data protection and dispute resolution. Whatever their needs, our clients get clear answers and options from lawyers who really understand pensions as well as being leading experts in their field.

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