Smoothing the journey from buy-in to wind-up

As more DB schemes are securing benefits with insurers, many trustees and sponsors are turning their attention to starting the scheme buy-out and wind-up process.

In recent years, many schemes completed full-scheme buy-ins much sooner than they expected. Trustees and sponsors could capitalise on rapidly improved funding positions after the market developments of 2022, or could take advantage of favourable insurer pricing at specific times.

But a quick journey to buy-in often means that trustees and sponsors haven't begun essential work needed to buy out and wind up the scheme. If they wait until all benefits are insured before starting this work, they might find a longer time to wind-up than they expected. The scheme could also incur more costs, possibly eroding a surplus that might have been available to members or sponsors.

While focusing on the buy-in, many trustees might not think about the whole process from a full-scheme buy-in to buy-out and wind-up. They might be unsure how long it might take, or what they can do to reduce this time and manage the risks.

How long will it take?

With a planned and well run process, it could take 18 months to convert a full-scheme buy-in to a buy-out, and a further year to wind up the scheme. So in an ideal world, trustees and sponsors could expect the whole process to take two or three years.

However, the process often takes longer. Three to five years might be more likely for many schemes. That's an extra year or two of running costs that the scheme might have avoided.

What could cause delays?

Most delays come from three sources: data, benefits and assets.

To settle all benefits and wind up, a scheme needs complete, accurate and fully electronic member records. Most schemes need a lot of work to achieve this. Many data items aren't needed for effective day-to-day administration – for example, contingent spouse pensions for all members. Schemes often use workarounds, so even well run schemes face challenges here.

Trustees might only start investigating how much there is to do after the buy-in, so they might not know the exact scope of data work. Another challenge comes from resourcing constraints in pensions administration teams. This live issue in the pensions industry can add to delays.

A scheme that's winding up needs a legally reviewed benefit specification that aligns with scheme practice and covers all benefits. The trustees need to resolve known historical issues through rectification, or implement measures to mitigate the residual risks once the scheme has wound up. These residual risks include members coming forward to claim they have different benefits.

Finally, the scheme needs a suitable investment portfolio for the residual assets after the benefits are insured. It needs enough assets that it can realise when needed, without applying a haircut.

How can schemes reduce the risk of delays?

Delays to the wind-up process are costly. The longer a project takes, the more expensive it becomes, as trustees and sponsors pay for more of their advisers' time. But incremental project costs from delays are often dwarfed by an extra year or two of scheme running costs.

The extra costs erode potential surplus that might have been redistributed to members or a sponsoring employer on wind-up. So it's important that trustees and sponsors mitigate the risk of delays.

We have four tips for managing the risks and delivering on time:

Start early

Develop your wind-up strategy at least a year ahead of the planned full-scheme buy-in. An effective strategy includes getting assets ready, understanding powers around winding up and how to distribute surplus, and managing residual risk.

A strategy like this puts you in a stronger position when you negotiate terms with the insurer. If you know your requirements, you can ask the insurer to tailor its offer to meet them when you have the most leverage.

Don't forget the small stuff

Some small benefits can take a disproportionate amount of time to settle, particularly if they involve third parties. Examples include additional voluntary contributions or historical individual annuities. Previous buy-ins covering benefits that don't match scheme benefits can take time to review and update.

Find out what you have in this category, and decide when to start discharging these benefits. Doing this work up front might mitigate the risk of needing to run the scheme while you wait for these benefits to be settled.

Assess your data and benefits

Review the member data and benefits needs for wind-up, so you have a better idea of how much work you'll need to get them ready. Then put in place a data improvement plan.

This plan should take into account the scheme's history, and the trustee's and sponsor's risk appetites. A well run wind-up process typically has this plan in place a year before buy-in, to minimise the risk of surprises (and therefore delays) after the transaction.

Get your governance right

An appropriate governance structure focuses on the goal and keeps momentum going. It also enables a plan with accountability and the right management information to the trustee board so the trustees can monitor risks and be resilient to problems. The need for detailed project management varies between schemes, but someone accountable for programme management is a must.

If you have a full picture of your scheme's steps to wind-up, you have a good idea of the work that you need to do. You can then take steps to reduce the risk of delays, identify efficiencies and maximise the value you get from all your advisers, service providers and even the insurer.

Want to find out more?

If you would like to discuss your scheme's journey from buy-in to wind-up, please get in touch.

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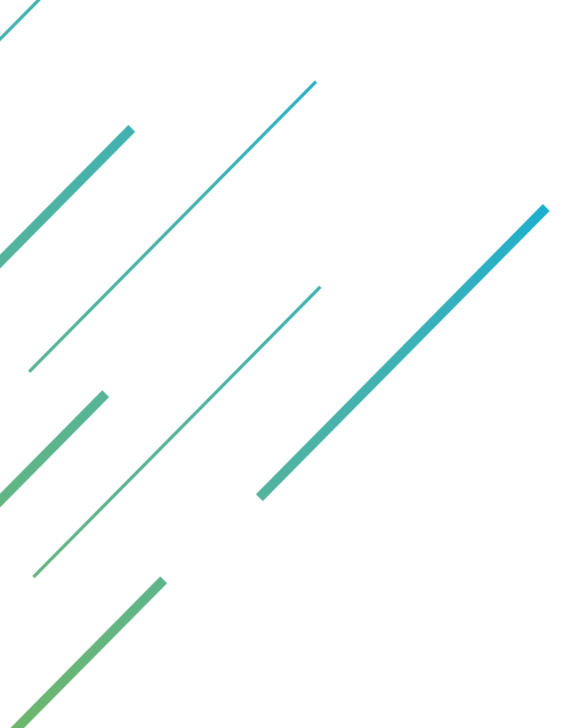

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