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MetLife

Comparing Pension Risk Attitudes and Aptitude

in the United Kingdom and United States

EXECUTIVE SUMMARY

The United States (US) and United Kingdom (UK) both have a long heritage of defined benefit (DB) plans or, as they are known in the UK, schemes. Although there are some unique structural and regulatory distinctions, their DB landscapes share more similarities than differences.

In both countries, the challenging global economic environment is making pension plan risk management exceedingly difficult. Sponsors on both sides of the Atlantic are very worried about managing the critical risks which have the potential to threaten the viability of plans. Today, many plan sponsors sponsors appear concerned about which strategies to employ to manage these risks going forward.

MetLife in the US and MetLife Assurance Limited in the UK commission annual research of DB pension plans, in their respective countries, to assess the current state of risk management. The 2011 MetLife US Pension Risk Behavior Index^{SM} (US PRBI)[1] and 2011 MetLife Assurance UK Pension Risk Behaviour Index^{SM} (UK PRBI)[2] studies surveyed respondents on 18 investment, liability and business risks to which their plans are exposed. Data from each survey were used to assess respondents' attitudes toward and aptitude for managing pension risk. Respondents in the US were comprised of sponsoring employers (plan sponsors); in the UK, both sponsoring employers (scheme sponsors) and trustees were surveyed.

This second annual comparison of the results considers how attitudes toward pension risk management have changed year-over-year, and highlights areas for action.

Notable findings from the comparison include:

- The index values for the US PRBI and UK PRBI, which effectively measure respondents' attitudes toward — and aptitude for — managing pension plan risk, continue to be virtually identical, improving slightly from 2010.
- Respondents in the US and UK are taking a more selective approach to pension risk management. In contrast to the 2010 results, respondents have carved out a core set of risks they deem most important.
- Market volatility continues to impact plans in the US and the UK. As a result, the most significant pension risk concern in both countries is a liability-related risk specifically dealing with plan funding. Underfunding of Liabilities in the US and its UK counterpart, Funding Deficits, are ranked first in importance in the respective countries among the 18 risk factors.

[1] Available at www.metlife.com

[2] Available at www.metlife.co.uk/metlifeassurance

- Respondents in both countries are intensely focused on some liability-related risks facing their plans. In addition to Underfunding of Liabilities (US)/Funding Deficits (UK) ranking as the most important risk this year, Asset and Liability Mismatch ranked second in the US and third in the UK. This is notable for the US, where until recently, assets rather than liabilities have been the main concentration of pension plan management, and any collective focus on assets and liabilities has typically centered on reporting rather than analysis. The UK has been a bit ahead of the US in this particular trend.
- While respondents in the US and the UK are both focused on liability management, there are some notable differences in their approaches. A deeper dive into the data shows that UK respondents may be more concerned about securing contributions to their scheme in order to meet their obligations, whereas US respondents are more concerned about seeking excess returns from their assets to meet their liabilities. Additionally, there are some interesting findings for each country with regard to the importance ascribed to asset-related and liability-related risks.
- Respondents in both countries continue to report that they are successfully managing many of the risks facing their plans . However, they report that they are not as successfully managing some of the most critical risks facing their plans.

PENSION RISK ATTITUDES AND APTITUDE: COMPARING AND CONTRASTING THE FINDINGS OF BOTH STUDIES

Index Values

For both the US PRBI and the UK PRBI, an index value was calculated to calibrate the importance that the survey respondents ascribed to managing each risk, their perceived success at implementing comprehensive practices to manage each risk and the consistency between the two. The index effectively measures both attitudes toward, and aptitude for, managing pension plan risk. While the calculation of the index value itself is fairly complex, the higher the index value, the greater the degree to which respondents report they believe they are successfully addressing important risks facing their DB pensions.[3]

In 2011, both the US and the UK saw a slight increase in index values. The PRBI value in the US was 81 out of 100 — up from 79 out of 100 in 2010. The PRBI value in the UK was 79 out of 100 — up from 78 out of 100 in 2010. These slight improvements are reflective of the underlying results of the study that show a shift toward a smaller, more concentrated group of risk factors. As success lags awareness, we would not expect to see a significant increase in the Index values until a consistent set of risks stabilizes, providing sufficient time for attention to be translated into success.

Importance of Managing Pension Risk

Both Countries Take a More Deliberate Approach to Pension Risk Management, Concentrating on a Core Set of Risk Factors

Contrary to the results of the 2010 US and UK PRBI studies, where respondents ascribed relatively equal importance to all of the 18 risk factors to which their DB pension plans were exposed, the 2011 results reveal that respondents on both sides of the Atlantic are zeroing in on a narrowed set of key risks.

This trend emerges when looking at the number of times a risk factor was selected as the most important when it was presented to respondents. Overall in the US, the selection range for all 18 risk factors is wide this year at 62 percentage points, versus a range of just eight percentage points in 2010. In the US, the most important risk factor was selected 66% of the time, and the least important risk factor was selected 4% of the time. In 2010, the most important risk was selected 29% of the time, and the least important risk factor was selected 21% of the time.

[3] For a full explanation of how the index is calculated, please refer to the 2011 MetLife US Pension Risk Behavior Index℠ (US PRBI) or the 2011 MetLife Assurance UK Pension Risk Behaviour Index℠ (UK PRBI).

In the UK, the range between the most important risk and least important risk in 2011 is 57 percentage points, with the most important risk being selected 58% of the time, and the least important risk selected just 1% of the time. This compares to just eight percentage points in 2010.

The narrower focus is further evidenced by the disparity between the Importance Selection Rates — a percentage reflecting the number of times a risk was selected as the most important when presented alongside other risks — of the top risks and the next most important risks in both the US and the UK. In the US, the Importance Selection Rates for the top two risks are 66% and 60%, respectively. The Importance Selection Rates for the third and fourth most important risks fall to 45% and 41%, respectively.

Respondents in the UK are also starting to discriminate when it comes to ranking the risk factors to which their schemes are susceptible. The selection rates of the top three risks — at 58%, 49% and 48%, respectively — are significantly greater than those of the next three risks, at 40%, 38% and 37%.

These findings indicate that respondents in the US and UK are now differentiating among the risks facing their plans, as opposed to 2010 where a "democratization" of risks seemed to exist in both countries. At that time, respondents were reluctant to identify any risk as unimportant.

Other similarities between the importance rankings in the US and the UK include:

- Three of the same risk factors fall into the top four in both countries for 2011:
  - A liability-related risk, Underfunding of Liabilities in the US, and its UK counterpart, Funding Deficits, ranked first in importance in the respective countries.
  - Asset and Liability Mismatch, also a liability-related risk, ranked second in the US and third in the UK. Its importance has risen, moving from the sixth most important risk in both countries in 2010. It was selected as the most important risk factor in the US 60% of the time, and in the UK 48% of the time in 2011.
  - Meeting Investment Return Goals (US)/Meeting Investment Return Targets (UK), an investment-related risk, ranked fourth in both countries.
- Liability Measurement (US)/Measurement of Technical Provisions/Liabilities (UK), which was ranked first in both countries in 2010, moved to the seventh most important risk factor in both countries in 2011. It was also reported to be the most successfully managed risk, an indication that respondents in both countries now feel they are in a better position to make funding and asset allocation decisions, presumably because they have spent a significant amount of time understanding and measuring their liabilities.

Table 1: Importance Selection Rates — US and UK

Risk Category	Risk Item	Importance Selection Rates			
		US – 2011	UK – 2011	US – 2010	UK – 2010
Liability	Underfunding of Liabilities (US)/Funding Deficits (UK)	66%	58%	28%	27%
Liability	Asset and Liability Mismatch	60%	48%	26%	26%
Investment	Asset Allocation (US)/Asset Diversification (UK)	45%	25%	27%	22%
Investment	Meeting Return Goals (US)/Meeting Investment Return Targets (UK)	41%	40%	23%	25%
Investment	Ability to Measure Risk (US)/Investment Risk Profiling (UK)	35%	20%	26%	25%
Business	Accounting Impact (US)	32%	N/A	22%	N/A
Business	Liability Measurement (US)/Measurement of Technical Provisions/Liabilities (UK)	30%	31%	29%	29%
Business	Plan Governance (US)/Scheme Governance (UK)	28%	21%	28%	24%
Business	Fiduciary Risk and Litigation Exposure (US)/ Litigation Risk Exposure (UK)	22%	1%	25%	21%
Business	Decision Process Quality	16%	11%	24%	23%
Business	Investment Valuation	16%	13%	24%	26%
Investment	Investment Management Style	15%	9%	22%	28%
Liability	Longevity Risk	12%	38%	24%	28%
Investment	Inappropriate Trading	8%	2%	26%	23%
Business	Advisor Risk (US)/Adviser Risk (UK)	8%	7%	26%	23%
Liability	Quality of Participant Data (US)/ Quality of Member Data (UK)	6%	14%	21%	22%
Liability	Mortality Risk	5%	26%	21%	25%
Liability	Early Retirement Risk (US)	4%	N/A	24%	N/A
Liability	Inflation Risk (UK)	N/A	37%	N/A	25%
Business	Employer Covenant (UK)	N/A	49%	N/A	28%

Top Risk in Both Countries is Liability-Related, But Drivers for Liability Management Differ

Today, in the aftermath of the economic downturn, and in an exceedingly uneven and challenging economic recovery that is rife with market volatility, most respondents in the US and UK are keenly aware of the challenges their DB pension plans still face. As a result, the most significant pension risk in both countries is a liability-related risk specifically dealing with plan funding. As mentioned earlier in this report, Underfunding of Liabilities (US)/ Funding Deficits (UK) ranked first in both countries.

While Underfunding of Liabilities has always ranked high in importance in the US — it was ranked second in the 2010 US PRBI study and third in the 2009 US PRBI study — in 2011 it was selected as important more often than any other risk factor in the history of the US PRBI study. It was selected as most important 66% of the time it was presented, compared with 28% of the time in 2010.

The identical risk factor in the UK, Funding Deficits, moved from the fifth most important risk in 2010, to the most important risk in 2011. It was chosen as most important 58% of the time it was presented compared to 27% in 2010 — far more often than any other risk factor.

While respondents in both countries may be focused on funding their plans' liabilities, there is an important distinction in how respondents in the two countries approach the management of their plan assets to meet their liabilities. Respondents in the US appear to be more concerned than those in the UK about securing excess returns from the plan's assets, while those in the UK appear to have concluded that the security of future contributions to their scheme is of key importance in order to meet their liabilities. Said another way, for respondents in the US asset performance is a key driver of meeting pension obligations; UK respondents are focused on demonstrating an appreciation of the importance of, and examining the viability of, the Employer Covenant to ensure that member benefits are secured.

The difference in focus becomes more evident when grouping the risk factors by the broader categories into which they fall. All five of the asset-related risks had higher Importance Selection Rates in the US than in the UK. However, in some cases, the differences in Importance Selection Rates were slight.

US Starting to Look at Assets in the Context of Liabilities

The UK has generally been recognized as being slightly ahead of the US in considering liabilities as centric to asset allocation decisions. However, the most recent US PRBI study has shown that respondents in the US may be poised to follow the UK's liability-centric approach to pension plan management. US respondents have begun to focus on making decisions about assets in the context of liabilities when managing their pension plan. Historically any discussion on liabilities in the US had typically centered on reporting rather than analysis. However, given market volatility, plans in both countries will likely continue to sharpen their focus on plan liabilities.

It is important to note that in many ways the results of the 2010 US PRBI study might be viewed as representing a bridge between old and new ways of looking at risks, from the traditional asset-centric model focused only on investment risk relative to external metrics to the more nuanced "assets in the context of liabilities" model that has been emerging more recently.

Today in the US, the highest importance is ascribed to two liability-related risks — Underfunding of Liabilities and Asset and Liability Mismatch. When these two risks are taken together with the results for the third and fourth ranked asset-related risks — Asset Allocation (45% selection rate) and Meeting Return Goals (41% selection rate) — it suggests that these four factors are viewed in a connected manner by a significant number of US plan sponsors. This indicates that liabilities are increasingly setting the context in which asset allocation decisions are made and return goals are set. It reflects a significant concern over liabilities, but may also point to sponsors' desires to ensure their assets perform well enough to help meet their plan's obligations.

To underscore the importance of managing assets in the context of liabilities, one US plan sponsor noted that the current period of economic instability "showed us the dislocation between asset returns and liability. We now are more focused on managing our assets towards our liabilities." Other US plan sponsors expressed related views. One commented "we take a more conservative approach to managing our liabilities while trying to generate returns on the asset side," while another stated that "we are…explicitly contemplat[ing] liabilities in our framework for deciding asset allocation."

In the UK, a Renewed Concentration on the Employer Covenant, Longevity Risk and Inflation Risk

The emphasis on Funding Deficits in the UK has been accompanied by a concentration on the Employer Covenant, selected as the second most important risk in 2011. This is the same position the Employer Covenant risk factor held in 2010. However, its Importance Selection Rate increased from 28% in 2010 to 49% in 2011. Interestingly, the closest equivalent US risk factor — Accounting Impact — ranked sixth in importance.

As was found in 2010, Longevity Risk also continues to be much more important in the UK than it is in the US. Today, it is ranked as the fifth most important risk factor in the UK (with a selection rate of 38%), compared to the 13th most important in the US (with a selection rate of 12%). Inflation Risk, which has no companion risk factor in the US, is the sixth most important risk factor in the UK, where members' benefits are inflation-protected through legislation. This makes the issues of longevity and inflation even more critical to UK schemes. Similarly, the common definition of a "spouse" in the US — the spouse upon retirement — versus that of the UK — spouse at death — also has implications on costs and longevity.

The prominence of Funding Deficits and Employer Covenant — coupled with Longevity Risk and Inflation Risk — appears to demonstrate just how much respondents in the UK, especially trustees, appreciate the importance of, and examine closely the viability of, their sponsor as ultimate guarantor of the scheme. The higher importance ascribed to Employer Covenant in the UK — compared with the Accounting Impact risk factor in the US — might also be a reflection of the concerns about the tougher obligations on UK employers than on US sponsors for dealing with funding deficits, as well as the emphasis in the UK on securing contributions into the scheme.

Commenting on the Employer Covenant, one UK scheme sponsor noted that the "reduction in investment returns has led to increased company contributions and therefore a greater reliance on the Employer Covenant." Making the link between investment performance and the employer's ability to fund the scheme, a UK trustee commented that "we're a mature scheme so we have to take a little more risk in our investments than we'd like to due to the sponsor's inability to pay the balance of costs or make up any deficits on their contributions."

Perceived Success In Managing Pension Risk

US and UK Respondents Report Successful Management of Risk
As in 2010, respondents in the US and UK continue to report that they are successfully managing risks facing their plans. Consistent with 2010's results, respondents in both countries report that they are successfully managing Liability Measurement (US)/ Measurement of Technical Provisions/Liabilities (UK), ranking it as the most successfully managed risk. Interestingly, this was ranked as the most important risk in 2010, indicating that respondents in both countries may now feel they are better equipped to manage their liabilities and make investment decisions against them. It moved down in importance to the seventh most important risk among both US and UK respondents, perhaps as a result of the attention paid to this risk in the recent past.

Plan Governance (US)/Scheme Governance (UK) is reportedly successfully managed, ranking fourth in the US and third in the UK, respectively, as is Advisor (US)/Adviser (UK) Risk. It tied for the fourth most-successfully managed risk in the US and also ranked fourth in the UK.

In terms of the least successfully managed risks in both countries, Longevity Risk continues to be the least successfully managed risk for both US and UK respondents. In the US, the Average Success Rating for Longevity Risk fell from 3.48 in 2010 to 3.20 in 2011. It remained consistent in the UK at 3.49. Decision Process Quality also ranks low in success among US and UK respondents again this year. This risk ranks 16th in success in both the US (consistent with 2010 results) and the UK (up slightly from 17th in 2010).

Risks Reported as More Successfully Managed in the US
There are some notable differences in the success rankings between the US and UK. In the US respondents reported greater success at managing Asset Allocation (ranked third in success with a 4.55 success rating) than their UK counterparts reported regarding Asset Diversification (ranked 15th in success with a 3.94 success rating). US respondents also ranked their success in managing Inappropriate Trading second with a 4.62 average success rating, compared to an average success rating of 4.33 and eighth in the success rankings in the UK. Finally, respondents in the US report higher marks for successfully managing the Ability to Measure Risk (3.99) than UK respondents gave themselves for managing the comparable risk factor, Investment Risk Profiling (3.53), although in both cases the relative success rankings were low, at 12th in the US and 17th in the UK.

Risks Reported as More Successfully Managed in the UK

In the UK, there are also some important distinctions when comparing the success ranking to those in the US. UK respondents rated their success at managing Mortality Risk higher than those in the US, with an average success rating of 4.37 versus 3.95. Mortality Risk was ranked as the sixth most successfully managed risk in the UK and the 14th most successfully managed risk in the US. UK respondents also reported slightly greater success at managing the Quality of Member Data than their US counterparts reported with managing Quality of Participant Data. It is ranked as the seventh most successfully managed risk in the UK with a 4.36 average success rating, versus the 10th ranked risk in the US and a 4.28 average success rating.

Table 2: Perceived Success in Managing Pension Risk — US and UK

	Success Rank		Average Success Rating	
Risk Item	US – 2011	UK – 2011	US – 2011	UK – 2011
Liability Measurement (US)/Measurement of Technical Provisions/ Liabilities (UK)	1	1	4.77	4.82
Inappropriate Trading	2	8	4.62	4.33
Asset Allocation (US)/Asset Diversification (UK)	3	15	4.55	3.94
Plan Governance (US)/Scheme Governance (UK)	4	3	4.54	4.61
Advisor Risk (US)/Adviser Risk (UK)	4	4	4.54	4.48
Investment Valuation	6	5	4.48	4.40
Meeting Return Goals (US)/Meeting Investment Return Targets (UK)	7	9	4.39	4.20
Investment Management Style	8	10	4.36	4.13
Accounting Impact (US)	9	N/A	4.34	N/A
Quality of Participant Data (US)/Quality of Member Data (UK)	10	7	4.28	4.36
Underfunding of Liabilities (US)/Funding Deficits (UK)	11	12	3.99	4.00
Ability to Measure Risk (US)/Investment Risk Profiling (UK)	12	17	3.99	3.53
Asset and Liability Mismatch	13	11	3.99	4.01
Mortality Risk	14	6	3.95	4.37
Fiduciary Risk and Litigation Exposure (US)/Litigation Risk Exposure (UK)	15	14	3.87	3.94
Decision Process Quality	16	16	3.66	3.54
Early Retirement Risk (US)	17	N/A	3.51	N/A
Longevity Risk	18	18	3.20	3.49
Inflation Risk (UK)	N/A	13	N/A	3.97
Employer Covenant (UK)	N/A	2	N/A	4.65

Figures for the Average Success Ratings were rounded to two decimal points.

Pension Risk Importance and Success

Alignment Between Importance and Success Reveals Some Inconsistencies

In comparing the US and UK PRBI study results, key areas for concern and action emerge in both countries when looking at the consistency between the importance rankings and respondents' reported success at managing them. Risks identified as highly important, but low in success, deserve more attention than those risks that are identified as low in importance but reported to be successfully managed.

In 2011, while both US and UK respondents ranked Underfunding of Liabilities (US)/Funding Deficits (UK) as most important, the risk was reported to be the 11th most successfully managed risk by those in the US and 12th in the UK. Similarly, Asset and Liability Mismatch, which is the second most important risk factor in the US and third most important risk factor in the UK, was reported to be the 13th most successfully managed risk in the US and the 11th in the UK. Since these risks fall in the high importance/low success quadrants in both countries, this may be an area of concern.

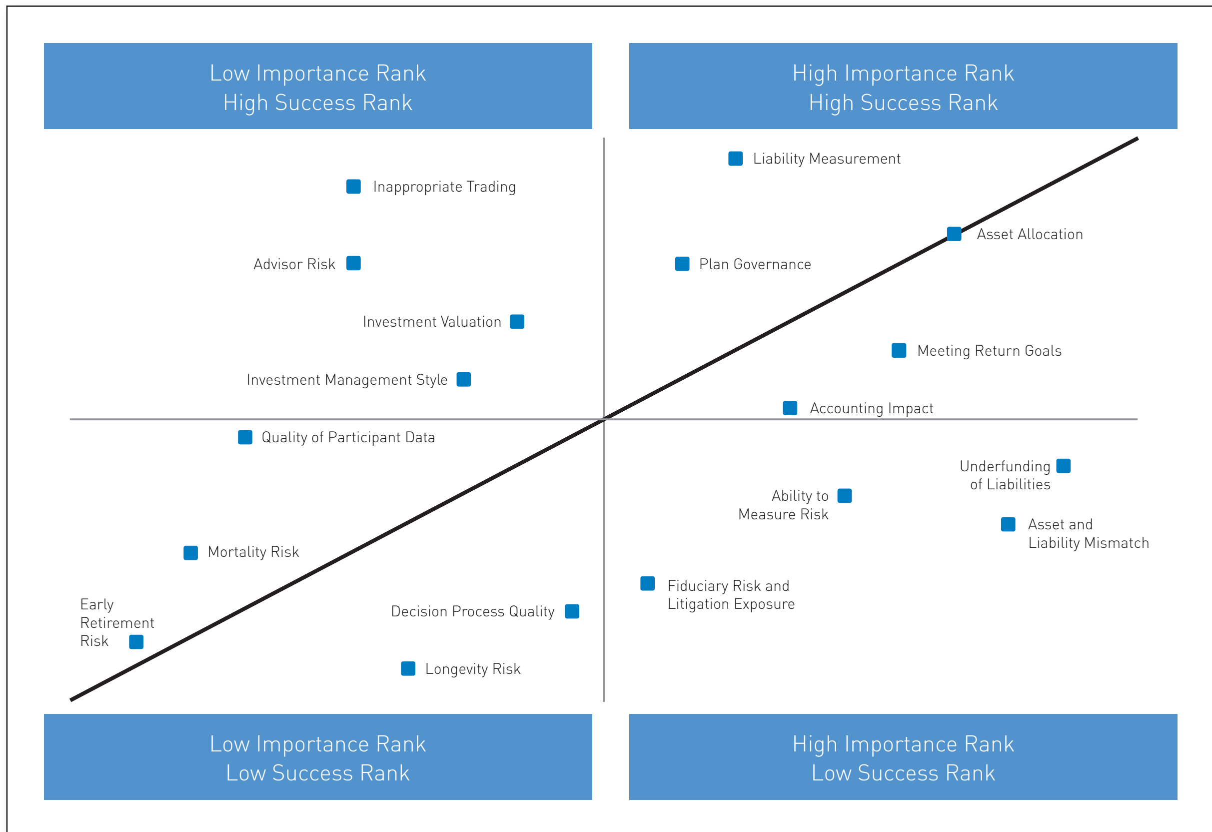
In contrast, Inappropriate Trading, Investment Valuation and Advisor (US)/Adviser (UK) Risk fall into the low importance/high success categories in both countries. There may be an opportunity to shift some of the attention away from these well-managed risks to focus on the ones that immediately pose the greatest challenges.

Longevity Risk continues to be a challenge for respondents in the US and UK to manage, given the inherent difficulty in predicting future trends. In the UK, it is ranked as the fifth most important risk factor but ranks 18th in success. As a result, pension schemes are increasingly looking to mitigate, reduce or transfer Longevity Risk. It is also ranked as the least successfully managed risk in the US. Longevity Risk also ranked 18th in success in the US, but it is considered far less important there, ranking only 13th.

US Consistency Chart

The chart below shows a scatter plot of the Importance Rank and the Success Rank in the US for each risk item. The vertical distance from each point to the line represents the mismatch between the rankings. Five of the risk factors fall within the high importance/high success quadrant. Risk items with the same importance and success rankings would lie along the diagonal line, as Asset Allocation does.

Chart 1: Consistency of "Importance" and "Success" Rankings (US)

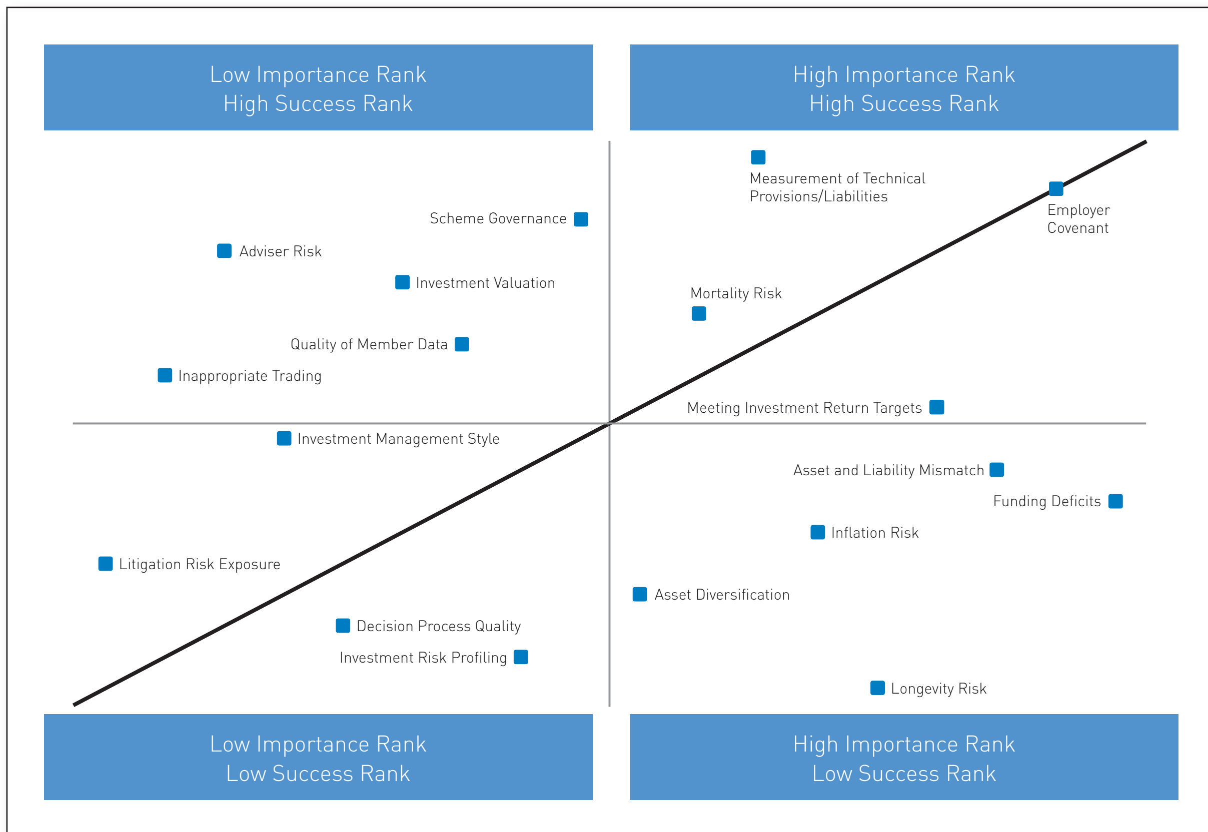


UK Consistency Chart

Only four risk factors lie in the high importance/high success quadrant, with Employer Covenant falling on the consistency line. Two of the most important risk factors, Funding Deficits and Asset and Liability Mismatch, fall into the high importance/low success quadrant.

At the same time, UK respondents believe they are managing some less important risks well. Scheme Governance, Adviser Risk, Investment Valuation, Quality of Member Data and Inappropriate Trading all fall within the low importance/high success quadrant.

Chart 2: Consistency of "Importance" and "Success" Rankings (UK)



THE US AND UK PENSION LANDSCAPES: A COMPARISON

In order to get a complete picture of the results of the US and UK PRBI comparison report, it is important to understand and acknowledge the similarities of and differences between the DB pension landscapes in both countries. While the US and UK pension markets appear nearly identical on the surface, their regulatory and economic environments, coupled with key underlying characteristics of both markets, differentiate the two.

While both markets have a long DB history, the frameworks and structures of their regulatory regimes have some significant differences. In the UK, DB schemes are set up such that trustees are responsible for managing scheme administration and investing the scheme's assets on behalf of a sponsoring organization. There is a clear separation of powers between fiduciary duty of the trustee and financial role of the scheme sponsor. In the US, the employer (or plan sponsor) has responsibility for both.

As such, regulations designed to ensure the viability of a pension plan and protect its participants tend to vary from one country to another. At the same time, economic forces have led employers in both countries to increasingly turn away from DB plans in favor of defined contribution (DC) plans.

In the US, the Employee Retirement Income Security Act of 1974 (ERISA) protects the assets of millions of Americans so that contributions to qualified retirement plans during their working lives will be there when they retire. Since fiduciary and financial responsibilities typically rest with the same body, the sponsoring employer, it was critical for ERISA to set forth certain fiduciary standards to address and protect against the potential conflict of interest. ERISA requires that employers who sponsor DB plans satisfy certain minimum funding requirements, and it also regulates the manner in which a pension plan may pay benefits, among other protections.

In 2006, the Pension Protection Act (PPA) was passed in the United States, with its requirements generally phasing in until 2012. It was the most sweeping pension legislation to be enacted in 30 years. With this act came a new era of discipline and transparency. For example, the legislation requires companies to analyze and more accurately report their pension plans' obligations. It also imposed new DB funding requirements, including increasing the funding requirements for severely underfunded "at risk" plans. In 2010, the Pension Relief Act was signed into law, making it easier for plans to improve their funded status as measured under the PPA.

In terms of member protection, while the UK's Pension Protection Fund (PPF) may seem like it is in its infancy compared to the Pension Benefit Guaranty Corporation's (PBGC) history in the US, it has existed for some time and is a critical part of the government's plan to ensure scheme members' retirement security. Efforts the PBGC has made around asset allocation, investment policy, risk premiums, opt-out provisions, and how rules and policy decisions have affected plan sponsor behavior in the US may offer the UK insight as the PPF develops and begins to address problematic UK pension schemes. By the same token, the PBGC can learn from the PPF as well. The PPF, for example, uses a risk-based levy set through a public consultation, rather than semi-flat levies set by Congress in the US.

Recently, the UK has seen a series of new pension laws which are set to fundamentally overhaul the retirement landscape for both DC and DB schemes. While the 1995 and 2004 Pensions Acts in the UK sought to increase confidence in the DB schemes, there are further initiatives on the horizon that, while aiming to ensure employees' retirement security, will have a significant impact on schemes and their sponsors. These include the establishment of auto-enrolment and the abolition of the default retirement age.

Over the period of its introduction, auto-enrolment is expected to lead to a rapid growth in pension membership. At the same time, the abolition of the retirement age means that people will likely work longer and retire for less time. These two initiatives may raise a number of questions around the funding for and future viability of DB schemes in relation to their DC counterparts in the UK.

Given this, it is not surprising that the UK Pensions Regulator has made reducing risk and better regulation a key focus. Its latest Corporate Plan focuses on improving governance and administration and reducing risk to both DB and DC members. It has also issued guidelines on areas including multi-employer schemes and employer departure, monitoring employer support, record keeping and incentivized transfer exercises demonstrating its ongoing interest in areas such as employer covenant and liability management.

Finally, the International Accounting Standards Board (IASB) intends to roll out new accounting requirements for DB plans that will likely have an impact on both US and UK plans. The US Financial Accounting Standards Board (FASB) and IASB have consistently indicated their long-term goal of alignment. The effect is already being reflected in large multinational firms moving voluntarily to mark-to-market accounting.

The combined effect of all the above, in particular the new accounting rules, new pension laws and continued economic volatility, has brought about a new focus on liabilities — one that many in the industry believe will open up new solutions for DB pension risk management on both sides of the Atlantic.

CONCLUSION

The results of the 2011 US and UK PRBI studies reveal that no DB pension plan is immune from the impact of financial market volatility. However, amid a slow and uneven economic recovery, plan sponsors in the US and scheme sponsors and trustees in the UK appear to be focusing more intensely on several critical risks facing their pension plans by moving beyond broadly ascribing importance to all risks, as they did in 2010. The first step in successfully managing these risks is to tackle the measurement of their liabilities. Both parties in the US and UK appear to have taken that step by reporting they are successfully managing Liability Measurement (US)/Measurement of Technical Provisions/ Liabilities (UK). As would be expected, once a risk is the object of consistent focus over time, success in managing it rises.

In the US, we expect that plan sponsors will deepen their focus on a core set of risks facing their plans, and develop and (over time) implement strategies to successfully manage them. In 2011, plan sponsors are in good position to tackle the top tier of liability- and investment-related risks — Underfunding of Liabilities, Asset and Liability Mismatch and Asset Allocation — that could positively impact their plans' funding positions, and in turn, their companies' balance sheets. The next set of risks will likely be made up of a "floating group" that changes year-to-year and is heavily dependent on the economic and regulatory environment. As a result, these risks may demand immediate attention at a particular point in time. Finally, plan sponsors will need to tackle longer-term (and less immediately critical) risks — i.e., Longevity Risk, Mortality Risk, Early Retirement Risk and Participant Data — head on.

In the UK, the 2011 PRBI study demonstrated just how many factors — many beyond respondents' control — can hit point-in-time scheme valuations hard. While sponsors and trustees appear to be moving toward a more coordinated approach to pension risk prioritization, the open question for the future is whether or not risk mitigation activity will be similarly coordinated. Frequent and ongoing communication between sponsors and trustees is critical for developing an agreed-upon plan to manage and mitigate risk. This is particularly important because there may be times when both groups will need to shift their focus in response to market forces, regulatory actions and changing scheme demographics. For both sponsors and trustees, managing long-term volatility and ensuring that member benefits remain protected into the future are inextricably linked.

MetLife

Metropolitan Life Insurance Company
200 Park Avenue, New York, NY 10166
www.metlife.com

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