

# A Practical Guide For Evaluating Terminal Funding Annuity Placement Providers

*“The skill and expertise of the annuity placement provider are an essential component of ensuring that plan liabilities are settled in a manner that is timely, accurate, and which minimizes expense.”*

Terminating a defined benefit pension plan is a lengthy and complex process which requires the support of many different service providers. A smooth and painless plan termination process requires relying on a team of expert professionals. The objective of this paper is to focus on the role of the terminal funding annuity placement provider, who plays a key part in the distribution phase of the plan termination process. The skill and expertise of the annuity placement provider are an essential component of ensuring that plan liabilities are settled in a manner that is timely, accurate, and which minimizes expense. Fiduciaries who undertake the process of terminating a pension program will want to carefully consider which service providers they choose to partner with. **Included within this paper are specific provider evaluation questions which we recommend plan fiduciaries consider as they discuss and think about the terminal funding annuity placement process.**

In order to consider the specific capabilities of an annuity placement provider, one must first understand the overall plan termination process as well as the specific areas where annuity placement providers deliver value to their clients.

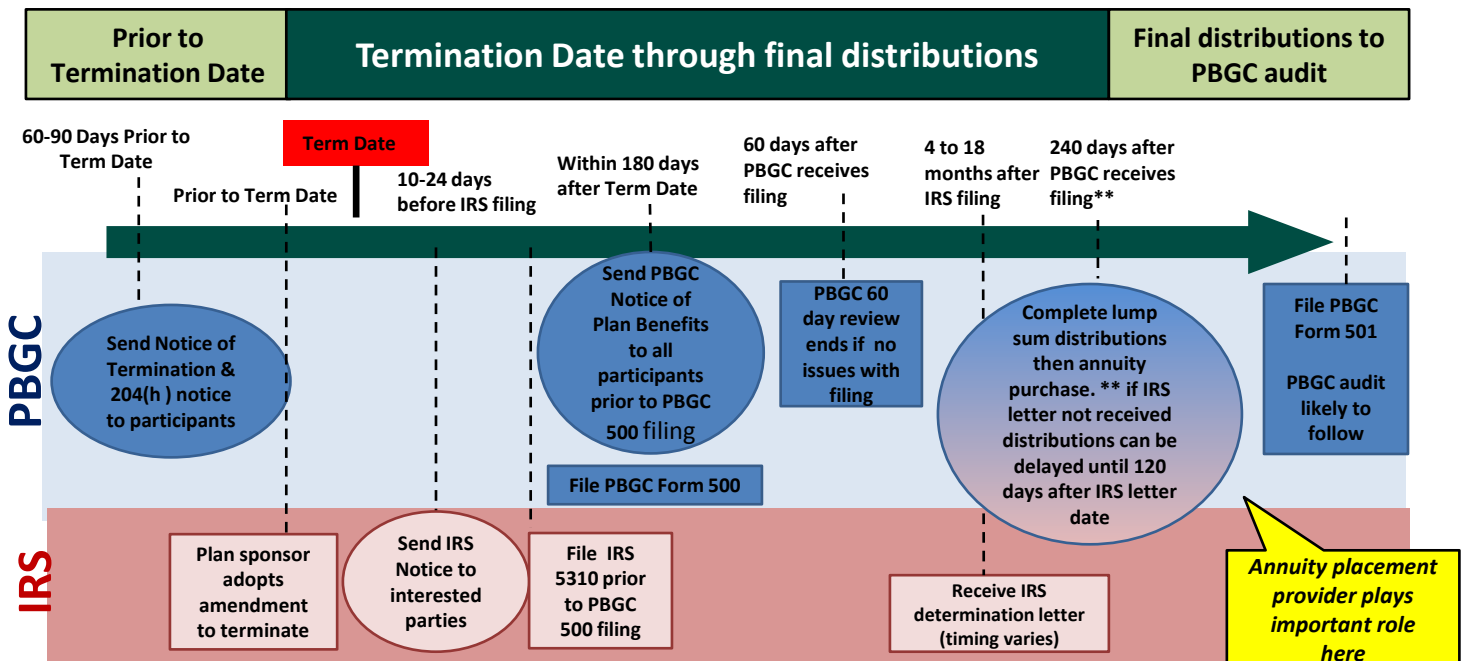
## The Plan Termination Regulatory Process

The chart below provides an illustration of the standard plan termination process. Underlying the process outlined below, are specific tasks owned by a myriad of stakeholders who participate in the plan termination process. This collective stakeholder group includes; regulators, actuaries, investment consultants, communication specialists, investment managers, trustee/custodians, accountants, plan fiduciaries, plan participants, annuity placement providers, and insurance carriers. The sections of this paper which follow will focus on discussing the role of the annuity placement provider whose expertise is critical to effectively distributing plan assets and legally discharging the plan benefit obligations. Minimizing execution risk is an important component of a successful plan termination, given the financial impact of the distribution process on the sponsoring organization’s business.

## The Role of a Terminal Funding Annuity Placement Provider

Having outlined the larger plan termination process which drives the need for an annuity purchase transaction, now let us consider why many pension plan sponsors hire a firm to assist with the annuity placement process. Generally, there are three core reasons why plan fiduciaries enlist the support of an advisor to assist with an annuity placement.

### PBGC Standard Plan Termination Process Overview



### 3 Basic Reasons Why Fiduciaries Hire a Terminal Funding Annuity Placement Provider

- Project Management Support
- Regulatory Compliance
- Competitive Bidding Process

When evaluating a specific firm or firms whom may be interested in taking on an annuity placement project, it is important to first understand that the items above serve as the foundation for defining the role and scope of work that should be expected. In the sections that follow we'll drill a bit deeper into each of the items above and detail some specific questions that fiduciaries may find useful to consider.

#### Reason 1: Project Management Support

The process of planning for and executing an annuity contract purchase involves several steps. It is not unusual for this process to span many months, involve a variety of insurance carriers, multiple rounds of annuity quoting, changing participant census data, and include an extensive Q&A process to ensure that all required plan benefits, rights, and features are effectively captured within the annuity providers pricing, proposal, and contract. While there is significant attention to managing the pre-sale process which culminates with the selection of an annuity provider, the post-sale conversion process is an equally important part of the overall support provided by an annuity placement provider. Ensuring that participant data is quickly and accurately converted to the selected insurance carrier's systems is an essential element to a seamless new contract installation process. Plan fiduciaries should also expect their annuity placement provider to assist in expediting and reviewing the formal group annuity contract to ensure its consistency with the initial terms of the sale outlined in the annuity providers proposal. The foundation for the entire annuity placement process is determined in large part by the clarity and accuracy of the "bid specifications" or "annuity quote request package". Fiduciaries should take great care in exploring the people and processes employed by an annuity placement provider.

#### Reason 2: Regulatory Compliance

ERISA fiduciaries are required to perform their duties solely in the interests of plan participants, and to demonstrate procedural prudence when making decisions involving plan investments. The Department of Labor, through its Interpretive Bulletin 95-1, outlines specific further guidance for fiduciaries to consider when selecting an annuity provider.

### Excerpt from Department of Labor Interpretive Bulletin 95-1

"...requires, at a minimum that plan fiduciaries conduct an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities. In conducting such a search, a fiduciary must evaluate a number of factors relating to a potential annuity provider's claims paying ability and creditworthiness. Reliance solely on ratings provided by insurance rating services would not be sufficient to meet this requirement. In this regard, the types of factors a fiduciary should consider would include, among other things:

- (1) The quality and diversification of the annuity provider's investment portfolio;
- (2) The size of the insurer relative to the proposed contract;
- (3) The level of the insurer's capital and surplus;
- (4) The lines of business of the annuity provider and other indications of an insurer's exposure to liability;
- (5) The structure of the annuity contract and guarantees supporting the annuities; such as the use of separate accounts;
- (6) The availability of additional protection through state guaranty associations and the extent of their guarantees.

**Unless they possess the necessary expertise to evaluate such factors, fiduciaries would need to obtain the advice of a qualified, independent expert..."**

Due to the items outlined above, many plan fiduciaries feel compelled to engage an expert to assist them in carrying out their fiduciary obligations under ERISA and DOL. It should be noted that simply engaging any "independent expert" may not be a sufficient course of action for ERISA fiduciaries who are required to prudently hire all plan service providers. Thus a fiduciary should have a solid understanding of the annuity placement provider's specific expertise, capabilities, and processes. **See "Sample Provider Evaluation Questions" on page three.**

#### Reason 3: Competitive Bidding Process

The final core element of an annuity placement provider's value proposition is their ability to effectively manage competitively bidding or "shopping" a pension plan's liabilities to help drive competing insurance carriers to provide their most aggressive (lowest) offer which ultimately reduces the cost of the annuity placement transaction.

There are a host of variables (census data, plan provisions, bond yields, risk appetite, competitive forces) which affect insurer pricing decisions, and these variables can often create a low price which is 5-10% less expensive than an insurer who may be using more conservative assumptions. An annuity placement provider's ability to understand the pricing drivers is an important component which drives their effectiveness at managing the bid process. Another important item to consider is the detail and quality of the "bid specifications" or "annuity bid request package" developed by the annuity placement provider. Utilizing "bid specs" that clearly and completely articulate the pension plan data and provisions is necessary to ensure that quotes received are consistent with each other. Some additional key elements to managing the annuity bid process include effectively navigating a host of underwriting questions from insurance carriers and communicating annuity quote census changes as data is refined throughout the lump sum election process which is part of most pension plan terminations.

### Best Practices for Evaluating & Selecting an Annuity Placement Provider

Having discussed the key background elements surrounding the annuity placement process, we can now turn our attention to specific items that may be useful for plan fiduciaries to consider when determining how to select an annuity placement provider to work with. An easy starting point for many plan sponsors will be to solicit input from existing service providers. Our experience has shown that actuaries, investment consultants, and ERISA attorneys are often called upon for their input regarding the annuity placement process. We recommend that plan fiduciaries talk to their existing service providers, and suggest they consider the following questions as they approach those discussions:

#### Questions to Ask Your Incumbent Service Providers

- What specific experiences do you have with plan terminations and annuity placements?
- Are you aware of other service providers who specialize in the annuity placement process?
- Do you have the capability to provide an expert level of support around the annuity placement process?

In addition to the items detailed above, it may be useful and prudent to consider having a formal evaluation process to select an annuity placement provider. Whenever possible, that process should entail a formal meeting and presentation process which allows each service provider to be vetted in person.

The section that follows contains several questions which fiduciaries and other pension plan stakeholders may wish to consider when evaluating the specific capabilities of a terminal funding annuity placement provider.

#### Sample Provider Evaluation Questions

- Please describe the organizational structure of your firm and its history.
- How many years has your company been active in group annuity contract negotiation for plan terminations?
- How many group annuity purchases has your firm placed in the last 24 months?
- Are annuity placement projects a core business activity for your firm? Approximately what % of your organization's total annual revenue is derived from annuity placement projects?
- What % of your annuity placement projects are conducted on behalf of clients who are not existing customers of your organization and/or its affiliates?
- How many employees does your organization have whose job function is primarily related to annuity placement projects?
- Does your organization (or any of its affiliates) provide services to or receive services from the life insurance companies who provide single premium group annuities for terminating pension plans?
- Provide the names of the consultant(s) to perform the work and a brief statement as to why each consultant is qualified to provide services to the client.
- Describe in detail your firm's process in performing a "safest available" annuity search.
- Describe your process of maintaining current data (ratings, etc.) on the pool of annuity providers.
- Please provide three references of clients for whom you have performed annuity searches.
- What capabilities would be important to know about your firm relative to your competition? What limitations does your firm have relative to your competition?
- Describe all anticipated fees involved with your annuity search process.

## Conclusion

Managing a pension plan termination and the tangential annuity placement process require the support of experienced and professional service providers. Plan fiduciaries will often find it valuable and necessary to engage an expert to assist with the annuity placement process. In order to evaluate annuity placement provider firms, plan fiduciaries must first have an understanding of the specific areas where these firms provide value to their clients. Moreover, there are several specific questions which can be helpful in evaluating a firm's annuity placement capabilities. Engaging the input of other service providers and considering the utility of a formal selection process may help support making an effective decision to hire any service provider. While evaluating the differences amongst experts within the same field can often devolve into a commodity-like price driven exercise, it is the author's hope that the material provided in this paper will raise the awareness of pension plan stakeholders regarding specific areas of differentiation that exist amongst annuity placement service providers.

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### About the author:

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