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WEALTH MANAGEMENT

OCIO Pension Easing

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The term OCIO stands for Outsourced Chief Investment Officer, and typically the services include asset allocation, manager selection, rebalancing, oversight might include trust custody. The reason why you're seeing a lot of growth in the space is because manufacturers like to spend time making things, colleges and universities like to spend time on education, health care systems like to spend time improving the quality of care, rather than managing a defined benefit pension plan.

The best fit for an Outsourced CIO approach?

A few things come to mind. Some may be drawn to the additional analytics and reporting that you might get. Think of one page dashboards or annual asset liability studies or monthly funding status reports. Some are drawn to the simplicity of the model working with one provider rather than coordinating services of ten providers. Some may feel they don't have the in-house expertise, and if that's the case, they'll have a duty under ERISA to delegate those services. If it's a carve out or spinoff situation, you might have to have a structure in place in a few months - an Outsourced CIO model can work really well there, and some providers can save money on fees with an Outsource CIO structure. The most common reaction or misconception from a CFO and Treasurer is the fear of giving up control. When they learn about how an Outsourced CIO model can be structured, they're still in the driver's seat very much with things like asset allocation, the investment policy statement, hiring and firing the discretionary manager, views on active vs. passive, even manager preferences they might have. So once they understand that structure, I think it's less about giving up control and more about the extra peace of mind that they gain.

The two key regulatory items?

The first is rising PBGC premiums. There's a fixed component that's based on the participants in the pension plan, and then there's a variable component that goes up as the plan is more underfunded. So sponsors want to take a look at whether or not it makes sense to contribute more than they're required to contribute to the pension plan to lower the PBGC variable rate component in future years.
The second is we're on the third round of funding relief, which for many corporations is set to expire over the next few years, and with that will come lower discount rates, higher liability values and higher deficits, and that may push out contributions a few years at a less favorable point the economic cycle. So those are the two regulatory changes to be mindful of.

The three things institutional investors should be focused on?

1. Whether or not they have the right operating structure, looking at the pros and cons of a discretionary model, which we talked about today, the Outsourced CIO model, or a non-discretionary model.
2. If it's a defined benefit plan it's important that they have a liability aware investing strategy, A liability aware investing strategy is one where objectives and risk tolerance is set in the context of liabilities, because a deficit is what drives volatility on the organization's balance sheet, income statement and cash flows.
3. They should be aware of all the fees that they' repaying in the management of the pension plan. Some of the vehicles, like mutual funds and ETFs, have embedded fees that some CFOs and Treasures aren't aware of, so it's important to take those into consideration when determining if the overall fee level is at a prudent level.