

MILLIMAN REPORT

Global pension risk transfer market outlook

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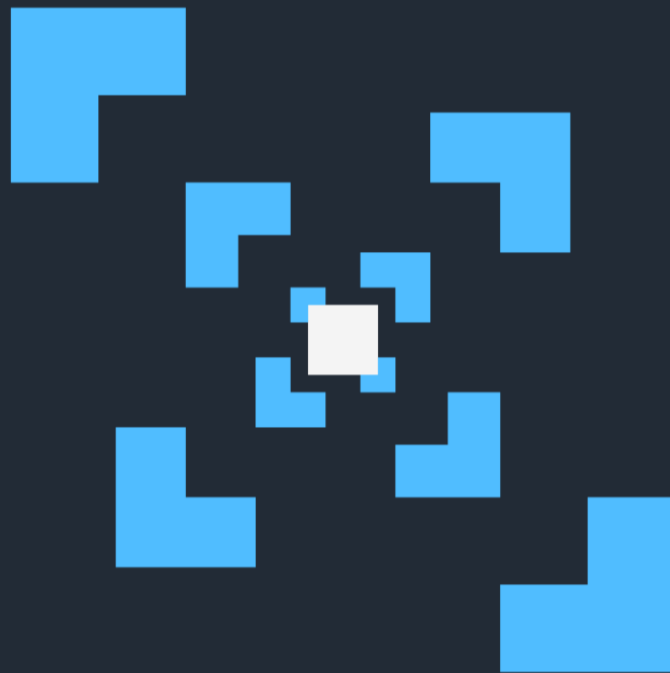


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1. Introduction

Members of a defined benefit (DB) pension scheme, the trustees and the sponsor all want to ensure that the benefits due to members are paid and the risks of the scheme not being in a position to do are minimised. Globally, the pension risk transfer (PRT) market offers an important mechanism for pension schemes seeking to de-risk, with significant demand for PRT deals from DB schemes in various markets. All stakeholders involved in transferring this risk to insurers should be aware of the current environment that insurers operate in, and insurers themselves must navigate various current developments and key challenges in order to be successful in the running of their businesses.

DB pension schemes exist in various territories across the globe, and in this paper we deep dive into several markets: the UK, US, Netherlands and Ireland. For each territory we consider the PRT market in more detail, including the following topics:

- The current landscape of the PRT market, including understanding where the demand for PRT deals comes from and why insurers write PRT business
- The main challenges faced by the industry
- The key regulatory considerations
- Lessons learned from that territory's experience

The UK market is considered the most mature of all the markets, and in this paper we first consider the UK in most detail. Some topics that are covered in the UK section also apply to other regions; therefore, we have avoided going into such depth in subsequent sections to avoid repetition.

1.1 SUMMARY OF SIMILARITIES AND DIFFERENCES ACROSS COUNTRIES

- A key driver for demand in all markets is the prevailing higher interest rate environment. The fall in the present value of liabilities is larger than the fall in the value of assets, and this consequently has improved funding ratios¹ of pension schemes across all markets covered. Improved funding ratios mean that a greater number of schemes are in a position to consider approaching an insurer to de-risk and secure the benefits of the scheme's members. Demand has increased to such an extent that some markets are expected to experience record years for volumes of PRT business transacted.
- The increasing demand is likely to encourage more insurers to enter the market.
- Some markets are more established than others. The UK and US typically experience very large volumes in their markets and have been writing PRT business for some time, whereas other markets are smaller in size or are at an earlier stage.
- Some challenges impact all markets, including:
 - The lack of availability of resources, particularly skilled personnel
 - Poor quality of data held by schemes to transact efficiently
- The regulatory environment differs across territories, reflecting different capital standards imposed by the local regulator, and different laws and reforms that impact the pension industry. Typically, the level of engagement with the PRT market specifically from the local regulator is proportionate to the size of the market.

¹ Ratio between assets and liabilities with the liabilities valued using a specified discount rate.

1.2 TYPICAL STRUCTURE OF PRT TRANSACTIONS

Under a typical PRT transaction the pension scheme pays a premium to the insurance company and in return the insurance company insures the pension liabilities of the scheme, with the two main types of transaction being referred to as a “buy-in” and “buyout.”

Under a “buy-in” transaction, the premium is used to buy a bulk annuity insurance policy from the insurer, which reimburses the scheme in bulk for its payments to its members. In this case, the pension scheme continues to administer benefits for its members.

Under a full scheme “buyout,” the insurance company becomes responsible for the administration of the scheme and annuity payments, the scheme members become customers of the insurance company, the sponsor is no longer responsible for the liabilities of the scheme and typically the scheme is wound up.

There are various other types of transaction that take place, as well as variants on the traditional buy-in and buyout. These include longevity swaps, partial buy-ins and partial buyouts.²

² Longevity swap - A type of transaction that transfers the longevity risk of members by making fixed payments to the insurer (such payments being determined at the start of a contract as the expected claims plus a fee). In return, the actual pension payments (the floating leg) are paid by the insurer.

Partial buy-ins/partial buyouts - Similar structure as the full version; however, only the risks of a subset of lives are involved in the transaction. Also known as “carve out” transactions in some markets.

2. United Kingdom

2.1 CURRENT LANDSCAPE OF THE PENSION RISK TRANSFER MARKET

2.1.1 Introduction to the UK PRT market

The UK PRT market is well established and thriving; pension schemes have been transferring pension liabilities to UK insurance companies for over two decades. At the time of writing, there are nine insurers writing buy-in and buyout business in the UK; one provider, M&G, re-entered the market in September 2023. Various other entities are considering entering the market, and as a result the number of insurers writing PRT business is likely to grow whilst demand from schemes is at a high.

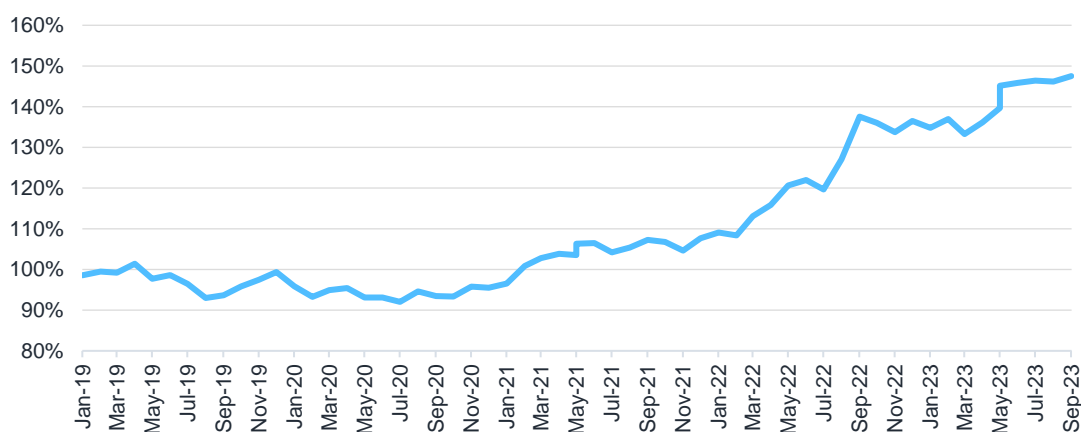
In 2022 there were £44.7 billion of buy-in, buyout and longevity swap deals, of which £28.1 billion were buy-ins and buyouts.³ In the first half of 2023, for the seven providers who have published their buy-in and buyout volumes and were also writing business in 2022, six have seen an increase compared to the first half of 2022. In H1 2023, based on volumes published by providers over £20 billion of premiums have been written to date, which would make it the strongest first six months of trading in the PRT market's history.

2.1.2 What is driving demand for PRT?

The next few years are expected to be a busy time for the UK PRT market. This is due to high de-risking demand from pension schemes. A survey from Mallowstreet in its Trustee Report 2022⁴ stated that 43% of schemes are targeting a buyout as their endgame solution, and of this proportion 50% are targeting a buyout within the next five years. Key reasons behind the demand from pension schemes are as follows:

- The recent rises in interest rates (and gilt yields) have improved the funding position of UK pension schemes, which has accelerated their plans to de-risk. This is because a rise in gilt yields has a greater impact on reducing liabilities (on a Section 179 basis⁵) than its impact on reducing assets,⁶ and over the previous 12 months to September 2023 there has been a small increase to equities which improves the value of assets. Figure 1 shows the aggregate funding ratios (on a Section 179 basis) of UK DB Schemes published by the Pension Protection Fund.

FIGURE 1: FUNDING RATIOS OF PENSION SCHEMES IN THE PPF 7800 ON A S179 BASIS



As a result of the marked increase in funding ratios during 2022, many schemes will take the opportunity to lock in this position by seeking a PRT deal.

3 Stapleton, J. (March 2023). L&G takes BPA top spot as insurers report 2022 results. Professional Pensions. Available at: <https://www.professionalpensions.com/news/4087003/takes-bpa-spot-insurers-report-2022-results>.

4 Mallowstreet. Trustee Report 2022. Available at: <https://mallowstreet.com/Research/Report/TrusteeReport2022>.

5 As set out in the Pensions Act 2004. <https://www.legislation.gov.uk/ukpga/2004/35/section/179>.

6 The PPF quotes the following rules of thumb: a 0.3 percentage point rise in gilt yields reduces scheme assets by 2.6%. Meanwhile, a 0.3 percentage point rise in gilt yields reduces aggregate scheme liabilities by 5.2%. A 7.5% rise in equity markets boosts aggregate scheme assets by 1.7%. Note that the rules of thumb only apply to small changes from the 31 March 2022 level. https://ppf.co.uk/-/media/PPF-Website/7800/2023/PPF_7800_September_Update.pdf.

- A survey from Mallowstreet in its Trustee Report 2022 stated that for 82% of trustees, a key challenge is the growing regulatory complexity of pensions, which takes up resources and increases running costs of the DB scheme.
- Insurers have increased their capabilities (financially and operationally) in order to transact so called “jumbo” transactions (i.e., transactions over £1 billion) in recent years, and as a result several very large pension schemes are known to be exploring PRT deals.

Subject to limitations surrounding market capacity and the necessity for careful risk management highlighted by the Prudential Regulation Authority (PRA), insurers will wish to make the most of this demand and new record high volumes could be achieved.

2.1.3 Why is PRT business attractive to insurers and other market players?

For many insurers PRT is the area of greatest strategic focus due to the demand for deals and long-term profitability of the business. Sales of life savings products such as with-profits have decreased dramatically in the UK in the past few decades; in terms of volumes, life insurance protection business is not a particularly large market; and sales of individual annuities, although having increased in recent months, have not recovered to pre-pension freedoms legislation⁷ levels. Therefore, outside of pensions auto-enrolment⁸ business, PRT is where the majority of new business volumes are expected to be sold for life insurers in the near future.

There are various reasons why the PRT market may also be attractive to asset managers and other categories of financial investors. Such firms currently provide asset management services to pension schemes, but this source of income is likely to reduce over time as pension scheme assets move into insurance companies. It is, therefore, potentially attractive for asset managers and similar organisations to invest in PRT capabilities that allow them to continue to access asset management revenue for assets used to meet DB pension liabilities.

The matching adjustment (MA) provides a regulatory mechanism which can increase the attractiveness of PRT business to potential investors by reducing the amount of capital required to be held against PRT liabilities. In particular, the MA allows insurers (with PRA approval) to increase the discount rate used to discount the liabilities by the portion of the credit spread broadly deemed to reflect the illiquidity of the assets held. As insurers are generally holding these assets to maturity, they are not exposed to the risk of changing credit spreads prior to maturity. Applying the MA has a twofold advantage for insurers’ capital requirements: it reduces the liabilities of the insurer as well as reducing the insurer’s solvency capital requirement (SCR), i.e., the capital required to be held in excess of the liabilities. Assets that can be eligible for the MA (subject to regulatory approval) include corporate bonds and certain types of illiquid assets.

Profits for PRT insurers can arise through the excess spread earned on assets over and above that required to meet the insurer’s outgo to policyholders and other expenses. Illiquid assets typically have a higher spread than corporate bonds of comparable quality traded on public markets; as a result, investment in illiquid assets (due to the returns available and the associated capital benefits as a result of the MA) is a key source of profitability for UK PRT insurers.

There are risks inherent in PRT business which insurers typically choose not to fully retain, and there are various mechanisms in place (including hedging or reinsurance) that help insurers to manage these risks and support their involvement in the PRT market. It is typical practice for insurers writing PRT business to transfer a large proportion of their longevity risk to reinsurers, often with pre-arranged terms through “flow” treaties. This is because, although there will be a fee paid to the reinsurer, the insurer’s capital requirements under the UK Solvency regime will be reduced. Risks related to fluctuations in interest rates, inflation and exchange rates are generally considered by insurers to be unrewarded risks and typically are closely hedged.

⁷ Pension freedoms legislation came into force in 2015. A key aspect of this legislation is that it removed the requirement for retirees to purchase an annuity.

⁸ It is a legal requirement for employers in the UK to set up a workplace pension scheme for employees, subject to certain criteria. Therefore, employees are automatically enrolled in the scheme unless they choose to opt out. This is referred to as “auto-enrolment.”

From the perspective of investors in PRT insurers, capital must be made available to cover the expenses and capital requirements of the business, which can be substantial. For a given PRT transaction, it will typically take at least two to five years before sufficient surplus emerges to break even, assuming the deal is priced competitively. However, beyond this point the business is steadily cash generative and, for an established insurer, much of the capital needs of new business can be funded from surplus emerging on its back book. For an established insurer, the business is therefore typically profitable with attractive long-term returns. For a new or fast-growing insurer, shareholders would typically not receive any dividends for an initial period, as the profits emerging are required to be retained in the insurer to cover the capital requirements of writing new business. Insurers are also able to issue tier 2 or 3 capital—for example, subordinated debt—to fund new business; however, for a new firm it will likely be some years before the available terms for such debt are attractive.

2.2 CHALLENGES FACED BY THE INDUSTRY

2.2.1 Illiquid assets

One of the findings from Milliman's industry-wide 2023 Illiquid Asset Survey⁹ (with participants who are active players in the UK PRT market) is that many participants are aiming to increase their exposure to illiquid assets to support new business. This is despite recent market conditions including rising interest rates and inflation and the weakening of the pound against the dollar, which have the potential to make GBP illiquid assets seem relatively less attractive (given the increased returns available on gilts and non-GBP assets). However, for insurers surveyed improving risk-adjusted return was noted as the top priority for investment in illiquid assets, when combined with a potentially increased MA benefit this is a key reason for their popularity with insurers.

Supply constraints

A key challenge for UK insurers in light of the volumes of PRT business expected in the coming years is sourcing a sufficient volume of illiquid assets meeting their desired criteria, with key criteria including yield and credit quality. In particular, there is expected to be some competition amongst insurers within the available pool of suitable assets.

The most common illiquid asset classes include commercial real estate loans, lifetime mortgages, infrastructure debt and social housing bonds. According to Milliman's 2023 Illiquid Asset Survey, it was most common for insurers to source illiquid assets using their in-house expertise; however, participants were most likely to use third-party asset managers or seek support for real estate loans, local authority loans, commercial and residential ground rents and private equity. Firms generally noted that they expect to make greater use of specialist external services or asset managers to support their origination of assets over the next 12 months.

Insurers funding lifetime mortgages have the advantage of a direct flow of this type of illiquid asset; however, lifetime mortgages sold require securitisation in order to comply with MA rules and volumes are subject to there being sufficient retail demand. Lifetime mortgages demand has reduced in 2023, potentially due to recent rises in interest rates, with the Equity Release Council stating that new plans agreed in Q2 2023 have reduced by 46% on an annual basis when compared to Q2 2022. Therefore, if this trend is likely to continue, firms will have to look to other types of illiquid assets to meet their increased demand for assets in the booming PRT market.

Regulatory burden

For each category of illiquid assets held, insurers must possess sufficient expertise and data to assign an internal credit rating, and to model the cash flows and capital requirements of the asset for asset and liability management and solvency purposes.

Should an insurer seek to invest in a new type of illiquid asset, the asset would need to be included within their approved MA application in order to obtain an MA benefit. Otherwise, the insurer would be required to carry out an MA reapplication process, which may be costly and require significant resource.

⁹ Ward, R. and Gingham, F. (July 2023). 2023 Illiquid Asset Survey. Milliman. Available at: <https://www.milliman.com/en/insight/2023-illiquid-asset-survey>.

Challenges of in-specie transfers

Illiquid assets also feature as part of the asset mix for many UK pension schemes. In some cases, UK pension schemes have a plan in place to gradually reduce their holding of these assets as they approach a buyout. As scheme funding ratios have improved at a greater pace than expected, some schemes may have been “caught out” in that they are in a position to buyout sooner than anticipated, without having sufficiently reduced their holdings in illiquid assets. This can present a challenge for pension schemes as the illiquid assets in their portfolios may not be structured in such a way as to meet the MA eligibility rules, or perhaps they have a sub-investment grade rating for which insurers have very little appetite. As a result, they may be challenging for insurers to accept in-specie (i.e., transferring the asset itself to the insurer), and schemes may therefore consider either selling these in the secondary market (perhaps with the assistance of the insurer) or to consider whether the insurer would accept a deferral of the premium to allow time to sell these illiquid assets.

2.2.2 Resource constraints and solutions to meet the demand

There are a number of constraints affecting the rate of growth of the PRT market in the UK. Given the increased demand from pension schemes for PRT transactions, insurers are faced with the challenge of ensuring they have sufficient resources, both financial and operational resources, to write the volumes of business that they wish to. The key areas that affect capacity for individual insurers and for the market in general are availability of skilled personnel and capital, as well as availability of MA-eligible illiquid assets with sufficient yield and credit quality (discussed earlier in this paper).

An operational constraint for PRT insurers is the capacity of their pricing teams, which require specialist expertise that takes time to develop. Moreover, it is typical for BPA transactions to involve multiple rounds of pricing, which places further constraints on pricing teams when it comes to the volume of quotations that they can realistically participate in. This can potentially be mitigated by developing more streamlined pricing processes for transactions below a certain size, resulting in fewer steps in the pricing process and greater standardization and, consequently, automation.

In order to solve the issue of availability of capital, insurers may look to their shareholders. Shareholders may wish to provide a capital injection to write increased volumes of new business. The shareholders would also need to be comfortable with the volumes being proposed and the risk versus reward trade-off of taking on the business. It typically takes a few years for profit to emerge from PRT business, as in the short term it is capital consuming. However, the profitability and return on capital metrics achievable are strong and the growth in PRT business is a key reason for an increase in operating profit for many UK BPA insurers.

Another option used by insurers to solve the issue of availability of capital is the use of funded reinsurance. Essentially, funded reinsurance (also known as asset-backed reinsurance) involves a reinsurer taking on a proportion of the insurer’s existing or new liabilities in return for a single premium. There are various reasons why an insurer would wish to pursue this type of reinsurance contract, not least for capital efficiency reasons, but also reinsurer pricing may well be appealing. However, this type of reinsurance brings with it various risks including a significant exposure to the risk of reinsurer default and has come under scrutiny from the PRA; this is discussed in more detail in a later section.

2.2.3 Uncertain impact of COVID-19 on longevity

Assumptions around future levels of longevity are important for UK PRT insurers, and adjustments to mortality assumptions can result in large impacts on profits for UK PRT insurers. Insurers will use data from their own internal experience studies, supplemented by external data and/or models, for example the mortality projections tool published by the Continuous Mortality Investigation (CMI) and postcode mortality tools,¹⁰ in order to develop their own assumptions

The COVID-19 pandemic brought with it an increase in mortality rates (and hence a reduction in life expectancy); according to the CMI, mortality rates in 2020 were 13.9% higher than in 2019. While these excess mortality rates have reduced in 2022, with mortality rates in 2022 being 6.2% higher than in 2019, it is unusual to see three consecutive years of mortality rates differing greatly from recent trends, and these years are seen by many as not being representative of future mortality rates. There is significant uncertainty amongst experts in the industry as

¹⁰ Postcode mortality models assume that an individual’s postcode area provides insight into their future longevity. These models assign a risk rating to individual postcode areas in the UK that can be used to adjust the life expectancies assumed for individual pensioners.

to what the reasons are for the continued high mortality rates, this could be due to the impacts of so called “long COVID,” or due to delays which occurred to medical treatments during the pandemic. There is also uncertainty as to whether this effect will be temporary or permanent.

In the 2022 calibration of the CMI’s mortality projections model, the core version of the model applies a 0% weight to data from 2020 and 2021, and a 25% weight is applied to data in 2022. This reflects the fact that the CMI believe that it may be some time before mortality rates return to pre-pandemic levels.

2.2.4 Potential new entrants

With the levels of demand from pension schemes for PRT deals expected to continue for the foreseeable future, now more than ever there are various companies considering entering the UK PRT market, including some with significant capital backing. Some firms that may be considering UK PRT are existing UK insurers, others may be looking at setting up a new monoline entity entirely.

The downside for existing market players would of course be increased competition, In particular, new entrants may be prepared to price more aggressively at first in order to establish a market share.

New entrants will need to consider the following key areas, and will need cover them in detail within their business plan submitted to the PRA and the Financial Conduct Authority (FCA):

- **Business strategy**, for example their target deal size and type, competitive advantages and route to market
- **Financial strategy**, for example, sources of capital and reliability of capital availability over the business plan, including financial projections modelling
- **Target operating model**, i.e., which capabilities will be retained in-house versus provided by external vendors?
- **Risk management**, for example, which risks will be retained and which will be transferred externally?
- **Strategy for regulator interaction**, in particular a clear and detailed plan gives the regulator confidence that the insurer will have sufficient capital to execute its business plan, that it will have sufficiently skilled and knowledgeable resources available to it, and that it has sufficiently considered and planned for the mitigation of risks to its strategy, including a plan for an orderly exit should this be required.

Potential new firms may also consider at this stage the timing of any other applications they would wish to make once approved, the expected timescale for their application and approval, and the expected impact on their financial projections. This may include for example the matching adjustment, an SCR internal model or the volatility adjustment.

2.2.5 Operational challenges

There are various operational challenges associated with absorbing large schemes onto insurers’ administration systems under a buyout, whether the administration is done in house or is outsourced to a third-party provider. These challenges may include:

- There may be data missing, for example incomplete marital data, unknown postcodes, goneaways (i.e., members that are uncontactable) etc. However, the scheme may have completed some exercises on these prior to or during the quotation process, including data cleanses and goneaway tracing exercises.
- The scheme may not have completed a guaranteed minimum pension (GMP) equalisation exercise¹¹ or may have missing data causing difficulties in the GMP equalisation calculation.
- There may be issues with loading schemes with new or unusual features onto the insurers’ reporting system. For firms using different modelling systems for pricing and reporting, this can be time consuming and requiring detailed reconciliation exercises.
- After a buyout, the insurer becomes responsible for the calculation of transfer values when they are requested by deferred annuitants. This can prove to be computationally challenging, as in some cases these calculations could have to be done manually using the models used to price a particular scheme, unless a simplified approach is adopted across the board to avoid the requirement for excessive manual calculations.

¹¹ GMP is a proportion of a member’s total pension which applies to people who were contracted out of the additional state pension between 1978 and 1997. In October 2018, the high court made a judgement that schemes are required to equalise male and female pensioner members benefits in respect of GMPs (which historically assumed retirement at 65 for males and age 60 for females). There is no specific deadline for schemes to complete the GMP equalisation exercise by, and therefore many schemes have not yet completed it.

2.2.6 Alternatives to PRT

There are various alternative de-risking solutions, some of which are developed by insurers as these are often seen as part of the route to buyout.

As a long-term or "endgame" solution, pension schemes can opt for self-sufficiency, a buyout, or a transfer to a superfund consolidator (or superfund), with a survey from Mallowstreet in its Trustee Report 2022 stating that 28% of trustees are targeting some sort of self-sufficiency/low dependency solution which is the default under the new DB funding code,¹² with around 1% of trustees targeting the consolidator option.

The likelihood of choosing an alternative de-risking solution such as a superfund is dependent on the funding ratio of the scheme, in the Department for Work & Pensions (DWP) response to a consultation on superfunds published in July 2023¹³ it was stated that there will be a regulatory gateway for consolidation which will ensure that superfunds are only an option for schemes that are unable to afford a buyout now or in the near future. There is an interim regulatory regime in place and one superfund, Clara Pensions, has been authorised under this regime and recently received regulatory clearance for their first transaction with a £590m pension scheme.

The rationale for transferring to a superfund is that there would be economies of scale in combining various schemes into one; it is expected to result in reductions in running costs per member and improved investment returns due to having a greater scale and access to assets than an individual scheme. Assuming a scheme meets the requirements under the regulatory gateway, superfunds could also be an option for smaller schemes which are feeling crowded out in the current market, if insurer capacity does not increase. In addition, the pensions regulator has stated its optimism that a transfer to a well-run superfund could improve member outcomes through improved risk management, security and governance.

Certain superfunds operate a business model where they target the buyout of sections of the fund with an insurer five to 10 years after the scheme's assets and liabilities transfer to the superfund. Therefore, under the current regulatory regime, superfunds are not expected to pose a material competitive threat to UK PRT providers, and indeed some may in future approach insurance companies for buyout transactions.

There are some solutions offered by UK PRT insurers that offer some degree of risk reduction for pension schemes that are not financially in a position to buyout. These are typically expected to be a first step towards an ultimate buyout, rather than a long-term solution in and of itself. For example, Legal and General offers an insured self-sufficiency product which it states as being 10% to 15% cheaper than a buyout, that provides a limited amount of insurance to a pension scheme equivalent to covering a one-in-200 year impact to funding levels, in exchange for a contingent annual premium paid by the scheme that is not paid if the funding level deteriorates. Unlike a buyout, the assets remain with the pension scheme (managed by Legal and General Asset Management) and the scheme is not covered for a deterioration in excess of the one-in-200 year level. The assets are invested in such a way that the product can help to provide a route to buyout.

2.3 REGULATORY CONSIDERATIONS

2.3.1 Overview

The increasing number of deals in the UK market, and the expectation for this to increase further, has not gone unnoticed by the PRA (the UK prudential regulator). The PRA has stated that these PRT deals represent a "structural shift in the provision of retirement income and also give insurers an increasingly important role as long term investors in the UK real economy."¹⁴ This shift has led to an increased focus on PRT by the PRA, as it has a responsibility to ensure these risks are properly managed and that regulation is fit for purpose in an insurance industry that is becoming dominated by large volumes of PRT business.

12 ABI (June 2023). Solvency UK: Cross-sector co-operation to drive £bn investment into UK projects. Available at: <https://www.abi.org.uk/news/news-articles/2023/7/solvency-uk-cross-sector-co-operation-to-drive-100bn-investment-into-uk-projects/>.

13 UK Department for Work & Pensions. Government response: Consolidation of defined benefit pension schemes. Available at: <https://www.gov.uk/government/consultations/defined-benefit-pension-scheme-consolidation/outcome/government-response-consolidation-of-defined-benefit-pension-schemes>.

14 Bank of England (April 2023). Moderation in all things – Speech by Charlotte Gerken. Available at: <https://www.bankofengland.co.uk/speech/2023/april/charlotte-gerken-speech-bulk-annuities-conference>.

2.3.2 Solvency UK

The UK insurance industry in general is also experiencing a period of change with respect to regulation as the UK transitions towards Solvency UK, and firms operating in the PRT market will need to understand how the changes affect the specifics of their business. The PRA is consulting on the changes and has published a series of proposed reforms¹⁵ during 2023, including some material changes to the regulations and requirements around the MA.

While these reforms affect all UK insurers, there are specific changes that will have a more material impact on UK insurers operating in the PRT market. This is perhaps in line with the UK view of making Solvency UK more relevant to UK insurance risks.

2.3.3 Risk margin

One of the key proposals is a change to the method used to calculate the risk margin, which is part of an insurer's liabilities under Solvency II. The UK government has previously stated that these changes would be expected to reduce the risk margin by 65% for long term life insurers. This reduction is likely to be welcomed by insurers as it represents a reduction in the overall level of capital required to be held against PRT business, as well as a reduction in the sensitivity of insurer's solvency positions to changes in interest rates.

2.3.4 Matching adjustment

The MA is used widely by annuity writers in the UK. While the overall design relating to the derivation of the fundamental spread (FS)¹⁶ is unchanged some of the changes that have been proposed include:

- Increasing the risk sensitivity of the current fundamental spread approach to allow different notched allowances to be made within major credit ratings (for example, different allowances for assets rated AA+ or AA- compared with AA)
- Widening the range of eligible assets used in the MA portfolio to include some assets with "highly predictable" cash flows (currently all assets must have "fixed cash flows")
- Broaden the categories of insurance products eligible for the MA
- Remove the restrictions on sub-investment grade assets within the MA portfolios
- Increase flexibility in the treatment of MA applications and breaches

However, the reforms also propose potentially onerous quantitative and qualitative validation exercises that insurers will need to carry out in order to benefit from the increased flexibility.

The PRA specifically acknowledges¹⁷ that the MA reforms, particularly the increased investment flexibility, will allow insurers to invest in assets that may earn higher expected yields than the existing pool of eligible assets. The PRA expects in a competitive market some of these benefits to be passed on to pension schemes through more favourable pricing.

2.3.5 Productive investments

There is increased political focus into how illiquid assets are invested by insurers as it can be a source of infrastructure lending and regeneration projects across the UK.

In July this year, several UK insurers including BPA writers and the Association of British Insurers (ABI) founded the Investment Delivery Forum, who have signed a letter stating their commitment to invest in a range of large-scale infrastructure projects with capital unlocked by the introduction of Solvency UK (described later).

There is also a strong and growing ESG focus in the projects chosen by insurers, with green housing and renewable energy infrastructure being key investments. The majority of UK PRT firms have committed to a net-zero carbon emissions target for their asset portfolios, with some setting key milestones to identify progress. A

15 Bank of England (June 2023). CP12/23 – Review of Solvency II: Adapting to the UK insurance market. Available at: <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/june/review-of-solvency-ii-adapting-to-the-uk-insurance-market>.

Bank of England (September 2023). CP19/23 – Review of Solvency II: Reform of the Matching Adjustment. Available at: <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/september/review-of-solvency-ii-reform-of-the-matching-adjustment>.

16 The fundamental spread is used to determine the MA and represents the cost of default and downgrades of assets held by insurers to back insurance liabilities.

17 Bank of England (September 2023). CP19/23 – Review of Solvency II: Reform of the Matching Adjustment, paragraph 10.35. Available at: <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/september/review-of-solvency-ii-reform-of-the-matching-adjustment>.

firm's ESG rating is something that trustees are expected to take into consideration when choosing an insurer, as their members may well expect current investment commitments around ESG assets to be present in some form within the insurer.

2.3.6 Additional tools for the PRA

The PRA is expected to put in place new supervisory measures and tools it can use to maintain safety and soundness and policyholder protection. These measures¹⁸ include:

- The ability to require insurers to participate in regular stress testing exercises prescribed by the PRA
- The ability to require nominated senior managers with formal regulatory responsibilities and sanctions under the Senior Managers Regime to attest formally to the PRA whether or not the level of the fundamental spread on their firm's assets is sufficient to reflect all retained risks and that the MA can be earned with a high degree of certainty
- Allowing insurers to apply a higher fundamental spread to individual assets through an add-on

The overall impact of the reforms on insurers is still unknown. However, any increased requirement to provide financial information to the UK regulator could be seen as an operational burden. That said, in recent years insurers have already been asked to provide information to the PRA, (formally via impact studies or stress-testing exercises, or informally through bilateral conversations) to provide information to the PRA.

2.3.7 Use of reinsurance in PRT transactions

The PRA has also expressed concern related to the use of reinsurance, particularly the use of funded reinsurance, by UK insurers. When PRT deals are transacted with pension schemes, the use of reinsurance is not only used to enhance the overall capital strategy and provide more capacity to write further business, but insurers can also benefit from reinsurers' asset management capabilities and from exposure to jurisdictions with lower capital requirements and investment restrictions.

The PRA has noted some key areas of risk within these arrangements in a global life insurance market and are focussed on areas such as the risk of recapturing the reinsured business, wrong-way risk and a potential lack of available actions to mitigate the risks of reinsurer default.

2.4 LESSONS LEARNED

1. As the UK PRT market has been active for some time, there are of course some lessons that can be taken away from the UK experience which may be relevant to other global PRT markets and indeed potential new UK PRT insurers.
2. One thing that many UK PRT insurers do very well is to develop streamlined operating models which, in some cases, have been refined over several years and in others (for example, the monoline insurers) have been set up in this way from the outset. The operating model has a very intentional split between functions carried out in-house and those which are outsourced. The in-house functions are those representing the insurer's core areas of expertise and intellectual property—for example, deal origination and pricing, longevity expertise, hedging, asset origination and investment management is often carried out in-house. Investment management is, in some cases, carried out by another group company that is a specialist investment manager. Functions which are outsourced are those where the insurer does not feel the need to have the expertise itself, in particular where it is most cost-effective and efficient to outsource them. For example, pension scheme administration is often outsourced and firms often use third-party asset originators for specialist asset classes.

18 HM Treasury (November 2022). Review of Solvency II: Consultation – Response, page 4. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1118359/Consultation_Response_-_Review_of_Solvency_II_.pdf.

4. A key element to the success of a UK PRT insurer is in the efficiency of its modelling for pricing and reporting purposes. In particular, it is desirable to:
 - Have in place a pricing process which is as streamlined and automated as possible will result in less time being spent on producing and reviewing quotes
 - Have the ability to handle large datasets provided by pension schemes without excessive run times
 - Ensure the onboarding of new schemes onto reporting systems is smooth to avoid lengthy point-of-sale reconciliation processes
5. Milliman's Integrate system¹⁹ can meet these requirements, providing a streamlined end-to-end pricing and reporting process with robust built-in checks and fast run time.
6. UK insurers make efficient use of the solvency-related regulatory mechanisms available, with all established PRT insurers having approval to make use of the MA and a full or partial internal model for the calculation of their SCR. Combined with the use of reinsurance, insurers are therefore able to achieve a high degree of capital efficiency.
7. Another feature of the UK PRT market which is not the case in some other markets is that in various pricing processes, insurers enter exclusivity with a given scheme at an early stage, which undoubtedly alleviates resourcing pressures within insurers. Various UK insurers also offer a streamlined quote process for smaller pension schemes, which again means that these insurers can quote on a greater number of deals with their current resource capacity.

¹⁹ Milliman Integrate. <https://integrate.milliman.com/en>

3. United States

3.1 CURRENT LANDSCAPE OF THE PENSION RISK TRANSFER MARKET

The PRT market in the United States has been around for decades, but the market has seen significant growth in recent years. There were 568 transactions in 2022, totalling \$51.9 billion in premium, significantly outpacing the previous record-breaking total of \$38.1 billion in 2021. The market shows no signs of slowing, with \$22.5 billion in premium in the first half of 2023 representing a 28% increase over the first half of 2022, including a notable \$8 billion transaction between AT&T and Athene that was announced in May 2023.²⁰

In recent years, the number of insurers participating in the US PRT market has increased to 21. However, we have seen some insurers start to specialize their offerings, and in turn they may not all compete for all opportunities if it doesn't meet their desired target. While many participants are established traditional insurers, a number of newer entrants are backed by private equity investors and asset management firms who are able to achieve synergies between their investment capabilities and the long duration of pension liabilities. In addition to direct writers, there are reinsurers, including those backed by private equity investors and asset management firms, that are supporting the direct writers of this business.

Although activity is at an all-time high and the number of PRT providers has increased, the market retains significant additional potential. According to a Congressional Research Service report published in September 2023, defined benefit pension liabilities in the U.S. total nearly \$17 trillion as of December 31, 2022.²¹ While much of that liability is associated with public pensions (local, state and federal plans) for which PRT transactions are less common, corporate scheme liabilities alone amount to over \$3.7 trillion, representing a great deal of untapped potential. Given the market opportunities, growing demand from pension schemes, and the increasing interest rate environment, many potential buyers and sellers see this as the time to evaluate the potential benefits of participating in the PRT market.

Considerations for new entrants

Companies looking to make a successful market entry need to develop a thorough understanding of the market itself and the implications of various strategic decisions to be made. This preparation often begins with many, if not all, of the following activities:

- Understanding PRT market dynamics
- Evaluating start-up costs associated with market entry
- Analysing the impact key actuarial assumptions on profitability
- Analysing actuarial projections for PRT blocks of varying characteristics
- Reviewing the benefits and risks of varying asset strategies
- Scoping the potential for any offshore reinsurance benefits
- Developing administrative capabilities
- Considering rating agency designations
- Developing relationships with intermediaries

20 LIMRA (August 2023). LIMRA: U.S. Pension Risk Transfer Sales Jump 31% in Second Quarter 2023. Available at: <https://www.limra.com/en/newsroom/news-releases/2023/limra-u.s.-pension-risk-transfer-sales-jump-31-in-second-quarter-2023/#:~:text=WINDSOR%2C%20Conn.%2C%20Aug.,Annuity%20Risk%20Transfer%20Sales%20Survey.>

21 Congressional Research Service (September 2023). U.S. Retirement Assets: Data in Brief. Available at: [https://crsreports.congress.gov/product/pdf/R/R47699.](https://crsreports.congress.gov/product/pdf/R/R47699)

3.1.1 Demand from pension schemes

After a precipitous drop in pension funded statuses during the 2008 financial crisis, the funded statuses of many U.S. pensions had seen little improvement up to 2020. Although many plan sponsors made contributions and plan assets saw positive returns, a protracted decline in corporate bond rates used to discount liabilities meant funded statuses remained largely stagnant over the following decade. With the recent rise in interest rates, however, financial statements are showing funded status improvement. As a result, many plan sponsors are looking to capitalize by reducing the size of their pension plan footprint. Recently plan sponsors have been able to pay a premium at or near the liability of the plan to secure reduced expenses and mitigate volatility without a significant negative impact on the balance sheet. Transactions can also be structured to avoid one-time expense accounting under US GAAP or simply provide ongoing savings large enough to justify the expense. In other instances, PRT transactions can be a form of clean-up in anticipation of a corporate merger. In almost all instances, scheme sponsors prefer to focus on their core business and eliminate themselves of the role as the annuity provider.

In addition, administration of a frozen pension scheme can be taxing, especially as staff familiar with the plan retires. Plan sponsors can outsource that administration through PRT transactions, shifting the benefit side of the pension plan operation to an insurer.

Pension Benefit Guaranty Corporation (PBGC) premiums are another significant factor in plan sponsor interest in PRT transactions. The PBGC insures retirement private pension benefits in exchange for annual premiums that increase with inflation; many plan sponsors find these premiums to become increasingly burdensome in recent years.

Plan sponsors looking to optimize PBGC premium reductions include retirees with the smallest benefit amounts in a transaction, maximizing the headcount removed from the plan for the transaction amount paid (i.e., as headcount is a key driver of PBGC expenses). The PBGC premium savings extend into future years, which provide a significant financial incentive for plan sponsors to pursue PRT transactions.

3.1.2 Risk transfer models

In the United States, PRT transactions were historically associated primarily with plan terminations, but strategies removing only a portion of a sponsor's plan liability (de-risking) have become increasingly common. There are three types of de-risking strategies generally seen in the US:

- **Buyouts (Liftouts)** – Involve using plan assets to purchase a group annuity for a specific group of participants (typically in-pay retirees) removing them from the plan.
- **Lump-sum windows** – A limited-time offer to participants (typically terminated employees with deferred benefits) to receive their benefits as a single payment from plan assets, removing them from the plan.
- **Buy-ins** – Involve using plan assets to purchase a contract where the insurer reimburses the plan for payments to covered participants. The insurance contract is an asset of the plan, and the plan sponsor retains the liability obligation, continuing to pay PBGC premiums for covered participants, but is not subject to settlement accounting.

In the United States, the vast majority of transactions between plan sponsors and insurers are buyouts, which represented 93% of 2022 PRT transactions by premium (including plan terminations).²² Because buy-ins do not provide the same PBGC premium and administrative cost savings as buyouts or lump-sum windows, they are generally rarer in the US market, mostly appealing to plan sponsors in unique situations and in anticipation of a termination event. Other risk transfer structures, such as longevity swaps, have seen limited uptake in the United States.

In a buy-in or buyout transaction, the premium is paid by the plan's trust to the insurance provider; assets transferred are frequently paid in cash, but asset-in-kind transfers do occur episodically (often more common on larger transactions), and as a single lump-sum payment. The insurer is responsible for effectively managing the assets to cover future benefit payments, and profitability is determined by the pricing and management of three key risks.

- **Investment risk** – Given the speed at which transactions occur, accurately determining the appropriate asset allocation and an associated return expectation for use in pricing can be challenging, particularly in times of financial volatility. Since investment returns are a significant contributor to price, accurately determining the returns the company can invest the premiums is a critical aspect of PRT pricing. Depending on the duration of the liabilities, reinvestment risk also exists (i.e., more relevant for younger populations).
- **Longevity risk** – Mispricing could mean that participants live longer than expected; small differences may compound into significantly larger payments than expected in future years. This risk can be separated into two categories: mispricing risk and future mortality improvement risk.
 - Mispricing risk is the larger portion of this risk in the US – Did the insurer set the starting mortality assumption appropriately given the pension population? This risk is heightened when the plan doesn't have statistically credible data on their plan.
 - While future mortality improvement risk exists, unlike the UK, US pension benefits are not often inflation adjusted, so this portion of longevity risk is less impactful at pricing than mispricing risk.
- **Behaviour risk for participants with deferred benefits** – Complicated benefits, decisions to be made by active and terminated vested employees, early retirement subsidies, and other unpredictable plan features result in more uncertain cash flows, presenting challenges in pricing and asset/liability matching.

3.1.3 Private equities related insurers business models

Several active PRT players are partially owned by or have strong relationships with private equity (PE) firms. Such PE-related insurers account for a substantial proportion of pension risk transfer business transacted in recent years. Private equity firms provide investment expertise and direct origination capabilities across private credit, real estate, and other asset-based markets such as collateralized loan obligations (CLOs) and asset-backed securities (ABS). The participation of these PE firms has made the PRT market more competitive, lowering transaction prices, and their access to new capital helps increase the insurance market's capacity and appetite to absorb pension liabilities. The three largest publicly traded PE firms all have involvements in the PRT market in recent years:

1. **Blackstone Inc.**
 - a. Both Corebridge Financial (Corebridge, formerly AIG Life and Retirement) and Fidelity & Guaranty Life (F&G) have outsourcing arrangements with Blackstone to manage most assets. Blackstone previously had a minority stake in Corebridge, but Corebridge repurchased all shares from Blackstone in June 2023. Blackstone has no material direct ownership in F&G. These annuity providers have outsourcing agreement with Blackstone on managing their private, highly specialized assets.
 - b. In 2021, Resolution Life and Blackstone entered a strategic partnership in which Blackstone provides investment management for certain asset classes in Resolution Life's portfolio. Resolution Life acquired Voya in 2019, which includes a block of pension risk transfer liabilities.
2. **Apollo Asset Management, Inc.** – Apollo and Athene merged in early 2020. In Q2 2023, AT&T entered an agreement with Athene to transfer \$8.05 billion of pension plan liabilities. In Q2 2022, Lockheed Martin Corp transferred \$4.3 billion of pension obligations and related plan assets to Athene.
3. **KKR & Co, Inc.** – KKR acquired Global Atlantic in February 2021. Global Atlantic serves as a reinsurer in the U.S. PRT market since 2019, and entered as a direct PRT writer through Commonwealth Annuity and Life Insurance Company last year.

American National Insurance Company is another recent example of a PE-backed insurer that entered the U.S. PRT market in December 2022. American National was acquired in May 2022 by Brookfield Reinsurance, which is a Bermuda-based affiliate of Brookfield Corporation, a private Canadian alternative asset management company. Brookfield is one of the leading PRT companies in Canada.

3.2 CHALLENGES FACED BY THE INDUSTRY

3.2.1 Data availability and credibility

Data quality and availability have long been uneven in the PRT market. Plan sponsors aim to carry out administration efficiently and to accurately assess their liabilities, but maintaining high-quality data requires investment in technology and administration. Because pensions are generally not a core part of a sponsor's business operations, significant investment in data management may not be a priority, particularly for smaller companies. Accordingly, credible plan-specific data is often not available for assumption development in all but the largest transactions. While general trends can be used to develop assumptions from industry data, the effect of an individual plan's unique provisions (such as reduction factors for early retirement) can significantly alter participant behaviour relative to broader industry experience.

As a result, insurers may need to use conservative assumptions for participant behaviour to compensate for more simplistic models or less credible experience, which in turn would lead to higher premiums that are less attractive to plan sponsors. To be competitive, insurers must improve their modelling and assumption-setting capabilities. Using plan-specific experience where available and augmenting with external data sources allow insurers to gain a competitive edge without subjecting themselves to undue risk in the future.

3.2.2 Policyholder behaviour for deferred lives

Annuity buyouts commonly only include participants already receiving payments (retirees or in-pay). PRT transactions for deferred lives present a much smaller proportion of the current market for several reasons:

- **Fewer market participants** – Deferred pension obligations present several challenges for insurers during pricing. Lack of supporting data, complicated benefits, generous early retirement subsidies, and other unpredictable plan features result in more uncertain cash flows, exceeding many insurers' risk appetites and complicating the development of robust pricing models.
- **Increased costs for plan sponsors** – Reduced competition and conservative pricing assumptions for deferred lives can result in bids that make buyouts for deferred lives more expensive relative to those covering retired lives, reducing available supply of blocks for insurers to bid on
- **Available alternatives** – The more popular option for removing risk associated with deferred lives is a voluntary lump-sum window. Lump-sum windows can be much less expensive than a lift-out for the same deferred population and are also typically easier to execute.

Despite these market frictions, there remains a large proportion of plan participants with deferred benefits. According to the US Department of Labor's Private Pension Plan Bulletin for plan years ending in 2020, of the 31.9 million participants (excluding beneficiaries) in private defined benefit plans, 10.9 million participants are currently receiving benefits. The remaining 21.0 million remaining participants are either terminated employees with deferred benefits or active employees that will eventually terminate or retire. This represents a sizeable market opportunity for insurers that can address the obstacles facing PRT transactions for deferred lives.

3.3 REGULATORY CONSIDERATIONS

3.3.1 Regulations affecting plan sponsors

After the failure of Executive Life Insurance Company in the 1990s, the US Department of Labor (DOL) published Interpretive Bulletin (IB) 95-1, which provides guidance involving certain fiduciary standards applicable to the selection of an annuity provider for defined benefit plans. Plan fiduciaries must act in the best interest of plan participants in selecting an insurer that can supply the safest annuity available and are required to conduct an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities.

DOL 95-1 lists six criteria that must be considered:

- The quality and diversification of the annuity provider's investment portfolio
- The size of the insurer relative to the proposed contract
- The level of the insurer's capital and surplus
- The lines of business of the annuity provider and other indications of an insurer's exposure to liability
- The structure of the annuity contract and guarantees supporting the annuities, such as the use of separate accounts
- The availability of additional protection through state guaranty associations and the extent of their guaranties

In addition, items such as the provider's risk management and administrative capabilities should be reviewed. A fiduciary may consider the advice of a qualified, independent expert, and may conclude, after conducting an appropriate search, that more than one annuity provider is able to offer the safest annuity available.

The bar for satisfying DOL 95-1 is high—any insurer in the PRT space will undergo this analysis by pension plan fiduciaries before and during the annuity purchase selection process. Insurers will need to withstand the scrutiny and be able to address inquiries about variances in their statutory accounting statements. Plan sponsors and fiduciaries will likely want to know why capital and surplus ratios differ from insurer to insurer. They may also seek to understand what profitable and unprofitable lines of business an insurer has, and how well the insurer can withstand a down year. Although not specifically mentioned as criteria in DOL 95-1, many plan sponsors are also interested in the ratings from an insurance rating service. Insurers should understand and expect these types of questions if they are interested in entering the PRT market.

As part of the SECURE 2.0 Act of 2022, the Secretary of Labor is directed to review DOL 95-1 and consult with the Advisory Council on Employee Welfare and Pension Benefit Plans, to determine whether amendments to IB 95-1 are warranted, and report to Congress on the findings of such review and consultation, including an assessment of any risk to participants. This review is expected to be completed in 2023 and may mean additional criteria will need to be considered by plan fiduciaries when selecting an insurer in PRT transactions.

3.3.2 Regulations affecting insurers

The National Association of Insurance Commissioners (NAIC) has expressed an increased interest in asset assumptions, particularly relating to alternative assets and structured assets. Regulators have also turned their attention to the risks inherent to private equity-backed insurers. The search for higher yields has led insurers to place greater reliance on illiquid and often complex and less predictable assets on insurers' books, which could pose valuation challenges, liquidity concerns, credit risk and other potential market risks.

In 2021, the NAIC has adopted changes to the life risk-based capital (RBC) instruction with respect to C1 charges applied on assets, which includes expansion of the credit quality categories for bond and structured assets so that the alignment between credit risk and capital charges are more refined. In April 2022, NAIC also adopted a change that requires insurers to apply higher capital charges to residual tranches of structured securities: a 30% factor for year-end 2023 RBC filings and a 45% factor for year-end 2024 RBC filings.

3.3.3 Upcoming statutory requirement changes

In the US, the methodology to determine the statutory reserve requirements for PRT annuities is undergoing a dramatic change. The current methodology is prescriptive on key assumptions that the new proposed principles-based framework is moving away from. The insurance industry is working to update the statutory framework to better recognize and incorporate the material risks of the underlying business.

This proposed framework, often referred to as VM-22, has been disseminated for industry feedback, and field testing has been conducted under the current proposed framework to evaluate the impact for volunteer insurers. However, many conceptual topics remain unsettled as industry participants and regulators learn from the initial field testing results. As the proposal is expected to affect both statutory reserves and capital requirements, there is uncertainty about the impact of the proposed changes on PRT transaction profitability.

3.3.4 Utilization of offshore vehicles

Many insurers have established offshore subsidiaries, either fully owned or partly owned (sidecars), in which they reinsure the PRT business. Sidecars have been a significant recent development which has allowed insurers to manage insurance liabilities but raise capital from outside sources to take on the insurance and investment risk of the PRT liabilities. In turn, the insurer is paid for its management services (origination, administration and investment—often in conjunction with an asset manager), and external investors get access to investments they otherwise would not be able to originate. Apollo/Athene created the first sidecar, followed by Global Atlantic, but many have followed since, including MassMutual and most recently Prudential.

The Bermuda Monetary Authority (BMA) reserves and capital framework has lined up well with managing PRT liabilities, as it focuses on asset-liability management. However, at the time this paper is being drafted, the BMA has been reviewing its framework and exposing it to the industry in consultation papers. Many of the larger insurers servicing the PRT market currently expect that Bermuda will continue to be a reasonable destination for PRT liabilities after the new Bermuda framework is implemented but acknowledge that this will depend on the final details of the framework. Some insurers may examine the viability of other offshore jurisdictions for PRT liabilities.

3.4 LESSONS LEARNED

Given that the US PRT market has been active for some time, there are some lessons that can be taken away from the US experience which may be relevant to other global PRT markets and potential new US PRT entrants.

US plan sponsors have exhibited a desire to de-risk, and buyouts have been one of the main vehicles to do so. There is a significant amount of pension liabilities remaining, and new insurers continue to enter the market.

An insurer's competitiveness appears to be driven by its approach to investments (and in turn its investment assumptions) and how it evaluates the longevity assumption for the plan. The ability to analyse and model various asset strategies to match a company's strategic and risk-mitigation priorities provides the insurer a competitive advantage. Many insurers are also creating much more sophisticated longevity assumptions for PRT blocks based on participant location and demographics, potentially leading to more competitive bids. Some insurers are further along than others when it comes to sophisticated modelling techniques and structuring for its pricing and valuation of these liabilities. We expect that the trend of increasing sophistication will continue.

Most of the pension liabilities transferred to insurers to date have been in payment retirees. While many insurers have been less comfortable with deferred payment liabilities, some have managed to complete transactions with deferred payment liabilities. We expect to see increase demand from plan sponsors to offload these deferred payment liabilities, which may create opportunity from those insurers who can access data to support their models, and can in turn be comfortable with this type of exposure.

In the US, there is more general awareness of the increased role that private equity and asset managers are playing in the insurance industry, driven by the number of announcements of large private pension schemes transferring to insurance company balance sheets. As in other PRT markets, regulators have increased their focus on investment strategies, and this may end up having implications for PRT pricing in the future. We expect that regulators will continue assessing underlying risk and start with additional disclosures.

Insurers are exploring new vehicles to improve their competitiveness and gain access to new sources of capital to meet market demand. In the current environment, there has been an explosion of interest in setting up sidecars to facilitate the investment of capital by non-traditional participants. We expect that as industry capacity continues to grow, we will see more innovative structures come to fruition that reduce the friction of offering solutions to pension schemes.

It is noted that PRT transactions in the US can generally be executed within a shorter timeframe than the UK market for example; this could be something that could be explored within other markets. There would need to be solutions found to some of the issues faced by insurers in pricing processes within markets such as the UK—for example, the inconsistent data formats received for quotations and sometimes low quality of data received with incomplete information. This could be achieved through a greater use of standardised templates, which some UK EBCs do help their clients make use of for transactions, and increased levels of data cleansing prior to schemes approaching the market.

4. Netherlands

4.1 CURRENT LANDSCAPE OF THE PENSION RISK TRANSFER MARKET

4.1.1 Introduction to the Dutch PRT market

In the Dutch PRT market, the basic features of PRTs operate in a similar manner to those observed in the UK: in essence, transitioning liabilities from a pension scheme to an insurance company for a premium payment. However, in practice, the Dutch market has its own specificities and regulations which need to be understood. A key change to the market is due to a new pension law (the Pensions Act) which came into effect in July 2023, which is driving boards of pension schemes to consider a PRT transaction (such as a buyout) as an alternative for transitioning the entire pension scheme into a defined contribution scheme as prescribed in the recent pension reforms.

In this section we first consider insights into the Dutch market, based on our experience, and then discuss what distinguishes the Dutch market from other markets. We then move on to consider the impact of the new pension law, after which we discuss other potential drivers for demand.

In recent years the Dutch buyout market has been fairly quiet. This is because since 2014 there have been only around four key players active in the Dutch market. Compounding this, consolidation activity has regularly driven down the number of unique offerings. However, whilst the number of active players may be low, these parties typically have budgets of multiple billions in premiums they would like to write in the PRT market. But with the revised pension law due in 2023, the transaction volume for buyouts in 2022 was just €55 million, most likely as a result of funds waiting for clarification around the revisions before closing deals.

The Dutch market has traditionally been a defined benefit (or DB) market, where most pension schemes were either company-based pension schemes or industry-based schemes. There are currently 170 pension schemes registered in the Netherlands. These range from very large pension schemes (for officials and health professionals) to smaller company pension schemes. As at Q1 2023, the market value of the assets of the pension schemes was €1,542 billion (in 2022 the total value of the assets at its peak was €1,911 billion mainly caused by the low interest rate environment). However, it is worth noting that €1,056 billion worth of assets as at Q1 2023 were invested outside of the Netherlands.

In recent years, the Dutch retirement income system has been considered by some to be among the best in the world. That said, the more recent shift to defined contribution (or DC) schemes has introduced more uncertainty for employees during the accumulation phase. At the moment of retirement, the accumulated amount is used to purchase a fixed annuity or a combination of a fixed and unit-based annuity.

In the Netherlands, a high percentage of the population is insured via a pension scheme or via multiple pension schemes. The combination of a government pension scheme and an employer-based pension scheme results in relatively high pension benefits for the average pensioner compared with the rest of Europe. There is also a high proportion of participation in employer-based pension schemes in the Netherlands, with close to 90% of the working-age population participating in a mandatory occupational pension scheme, compared with roughly 50% in the UK. Another useful metric to consider is the amount of assets earmarked for retirement versus GDP as a percentage, as the metric highlights the impact of this difference in percentage participation. In the Netherlands the amount of assets earmarked for retirement amounts to over 200% of GDP in 2021, whereas in the UK this metric is closer to 125% of GDP. Although the UK's GDP is around three times that of the Netherlands, in terms of total assets for retirement the UK is less than two times the size of the Netherlands.

Looking at the typical PRT transactions in the Dutch market, pension schemes usually consider a buyout or a partial buyout. With a partial buyout a subset of the scheme—typically the pensioners and deferred lives—is “carved out” of the pension scheme and risks are transferred to an insurance company.

Whenever a substantial change is considered for a pension scheme, this latter option of a partial buyout of pensioners and deferred lives allows a pension scheme to “reset” to a more even balance between premiums paid versus benefits accumulated to assist in managing the scheme going forwards.

4.1.2 What is driving demand for PRT in the Netherlands

Traditionally there has always been an active PRT market in the Netherlands. However, recovery from the 2008 financial crisis and, until recently, the low interest rate environment have had a strong negative impact on the PRT market as a whole as funding ratios of pension schemes have been low in recent years.

More recently, funding ratios have been increasing due to rising interest rates, resulting in the request of a greater number of requests for quotations to insurance companies active in the market. Insurance firms regularly have a pipeline of proposals summing up to their yearly PRT premium budget, but expect most of these proposals not to complete based on their experience from the past 10 years. But change is on the horizon for the PRT market in the Netherlands due to the new Pensions Act, potentially resulting in a turning point for the market.

Under the new Pensions Act, built-up DB benefits will be transformed into DC capital. The traditional approach of an average premium percentage relative to salaries paid for all members regardless of their age will be abandoned in favour of an age-based premium ladder, with relative premium as percentage of salary increasing with age. For pension schemes with, for example, a sizable portion of pensioners and/or relatively older pension scheme participants, this could lead to discontentment. Pension rights long assumed to be a given are suddenly more flexible and explained to contain a (high) degree of uncertainty. Pension boards have several options before the transition to the new pension law must be implemented by 2028, with buyouts and carve-outs among the options. Going down the buyout route would mean that the accumulated benefits are guaranteed, and hence the uncertainty is reduced.

One area challenging pension schemes is the legal demand of "balance" in the move from DB- to DC-based pension schemes, which can be a daunting task if there is a diverse population of participants in the pension scheme. If a pension scheme finds it overly difficult, or unfeasible, to explain to their participants that changing their DB benefits to DC capital per person is performed in a fair and balanced manner, a buyout can offer an alternative that is far easier to explain. Where discontentment is largely among pensioners or deferreds, a carve-out can also be an option.

4.1.3 Why do Dutch life insurers write PRT business?

Broadly speaking, Dutch life insurers tend to write PRT business because:

1. There is margin²³ to be made
2. It increases the life book, which historically has been shrinking in the Netherlands for a long time, thereby aiding in cost efficiency of systems and services

Whilst the number of players active in the PRT market is low, these insurance companies have grown due to consolidation in the Dutch market and therefore are better positioned to close significant buyouts. More generally, the consolidation that has occurred allows them to offer buyouts under profitable margins due to an increased cost basis. These offers are also currently more appealing due to increased coverage ratios of pension schemes, which leaves room for future indexation—for example, tied to an inflation index.

Furthermore, servicing a buyout for an older book also allows the insurance company to potentially offer the servicing or administration of the (new) active defined contribution pension scheme under the new pension law. For a pension scheme, it can be appealing to have everything serviced by one insurance company. On the new defined contribution plans Dutch insurance companies can make a positive operational margin, the largest insurance firm NN reporting between 15 and 20 basis points of operational margin, while the capital requirements for these types of contracts are low.²⁴ As this portfolio grows, the operational margin could follow suit.

Some parties have stated that they expect tens of percentages of pension schemes to look for a buyout, with NN noting that if this happens they expect margins on buyouts to increase, as insurance companies do not have unlimited budget to take on risk.

²³ The margin mainly consists of investment margin and the diversification benefits. It is more common to reinsure (a part of) the longevity risk of the pension contracts.

²⁴ NN ziet pensioenmarkt verdubbelen in nieuw stelsel (beleggen.nl)

A potential factor which could see the current PRT market change could be new players being attracted to enter the Dutch market as a result of the new pension law and opportunities to service profitable buyouts and new defined contribution pension schemes. This could put pressure on existing Dutch insurance companies and also affect the likelihood for margin increases in the future.

In any case, if the Dutch life market moves to be more in favour of contracts serviced by insurance companies compared with the current approach of mandatory savings in corporate pension schemes and voluntary savings in bank savings contracts, it could be a breath of fresh air and change the outlook of life insurance companies in the Dutch market.

4.2 CHALLENGES FACED BY THE INDUSTRY

4.2.1 Challenges for insurers

In terms of challenges, the Dutch market is similar to the UK market with respect to resource constraints on both capital and personnel being able to meet demand. The life market in the Netherlands (including non-PRT business) has been shrinking for some time. The personnel base has also been shrinking, in a similar fashion, and it might prove difficult to grow the personnel base if the Dutch market becomes more like the UK market in terms of demand for buyouts.

As seen in the UK, the use of reinsurance and capital injections from shareholders allow firms to increase their capacity to write new transactions.

Furthermore, investments in information technology to make processes more efficient and flexible are essential for all insurance companies, and these are unlikely to be as developed compared to other regions.

4.2.2 Challenges for pension schemes

From the perspective of the pension schemes, there are two main circumstances to consider. If a pension scheme is closed to new members, a buyout is a relatively commonly accepted alternative to other execution options, like joining a pension foundation (a Dutch pension law specific alternative legal structure that is allowed to service pension schemes) or merging with a (larger) industry pension scheme. For a closed scheme, this ensures that their participants are serviced and will benefit from improved efficiency, regardless of the specific option chosen.

For pension schemes that are still open to new members, there is a lot more pressure, as the decision to either transform the existing defined benefit rights into defined contribution scheme or consider a buyout is a once in a lifetime choice; it is irreversible and could be considered the most important decision a pension scheme board can ever make. This pressure is likely to lead to a lengthy process where due attention is spent on the intricate differences between all the options that present itself with the new Pension Act.

The transition period for schemes to amend their current pension scheme in order to be permitted under the new Pension Act is five years, effectively giving pension scheme boards until 2028 to come to a conclusion on all aspects.

4.3 REGULATORY CONSIDERATIONS

As well as the new Pension Act described above impacting the Dutch market, there are existing regulatory considerations which should be borne in mind. These are discussed in more detail below.

Under Dutch pension law, buyouts including partial buyouts are possible but require pension schemes to follow a formal procedure. These transactions are seen as embodiments of a "collective value transfer"²⁵ and must be judged as such. To complicate matters, from a pension scheme perspective, a collective value transfer must be requested by the employer(s) whom a pension scheme is servicing.

²⁵ The act of transferring and/or transforming pension funds belonging to a group of active and/or deferred lives and/or pensioners from one executing party to either a new scheme at the same party or a scheme at a different party. A specific article (#83) from the Dutch pension law covers this act.

A pension scheme is required to investigate options based on executability, feasibility, explicability and balance in terms of how pension rights are divided. When the pension scheme has come to a formal offer, the "Accountability Council" will give formal advice, and the collective value transfer must be reported to the Dutch National Bank. The Dutch National Bank can prohibit the collective value transfer from taking place (typically within a window of three months after the intended buyout has been reported). The board of trustees of the pension scheme must also approve the buyout or partial buyout.

Note that for partial buyouts there is an additional complication which arises as individual participants in the pension scheme can object if, for example, members deem there to be an unfair balance between the assets allocated to the partial buyout and the assets remaining in the pension scheme.

4.4 LESSONS LEARNED

In the Dutch market, a limited number of insurance companies are active in the PRT market. These active players have grown largely due to consolidation activity within the Dutch market, thereby allowing them to write significant buyout premiums.

With increased coverage ratios of pension schemes due to rising interest rates and a new pension law being enacted in the Netherlands, interest in buyouts and carve-outs is expected to reach an all-time high over the next couple of years, as pension schemes must investigate options to best service their participants and buyouts are on the table more than ever.

In the Dutch PRT market, the process of producing a quote is relatively efficient. Parties active in the market have existing models they can use to determine an offer and have an understanding of what the relative internal rate of return of the deal will be. From a computational perspective, the models have been relatively complex—for example, taking into account the expected claim on capital and allowing for possible indexation options over time based on economic scenarios.

Deals typically take a long time to close in the Netherlands, as pension fund boards seek explicit buy-in from the pension fund participants. In many cases the pension fund is tied to an active company, who would seek to avoid creating unrest amongst its employees. It is not uncommon for a quote to be discussed, and consequences to be presented at a meeting for employees with questions being relayed to the insurance company. Also, exclusivity with one insurer is uncommon. Multiple insurance companies will be competing within the quote process, which can lead to multiple consecutive offers if the buyout is of interest from the insurance company's perspective.

Prior to the new Pensions Act, the Dutch PRT market has been slow. Now that the act is in force, it can be a challenge for insurance companies to ramp up their activities if clarity on the new Pensions Act leads to significant demand from pension schemes. The use of reinsurance and/or expanding existing reinsurance contracts to support buyouts is not a common practice for all parties involved in the market. There could be an opportunity for a reinsurance company to enter the Dutch market to support the PRT insurers when (and if) the PRT market starts to grow.

If a large number of pension boards seek a buyout due to the new pension law and the market starts to grow rapidly, various challenges may arise for Dutch PRT insurers. Issues such as the maintenance of a successful investment strategy for a growing life insurance base and personnel challenges for the execution of deals present challenges the Dutch market has not experienced for quite some time.

5. Ireland

5.1 CURRENT LANDSCAPE OF THE PENSIONS RISK TRANSFER MARKET

5.1.1 Introduction to the Irish PRT market

This section of the report focuses on the PRT market in Ireland. Broadly speaking, the PRT market in Ireland has a similar structure to the equivalent market in the UK described in section 2, and much of the same terminology applies. However, there are some differences between the markets which we draw out in this section.

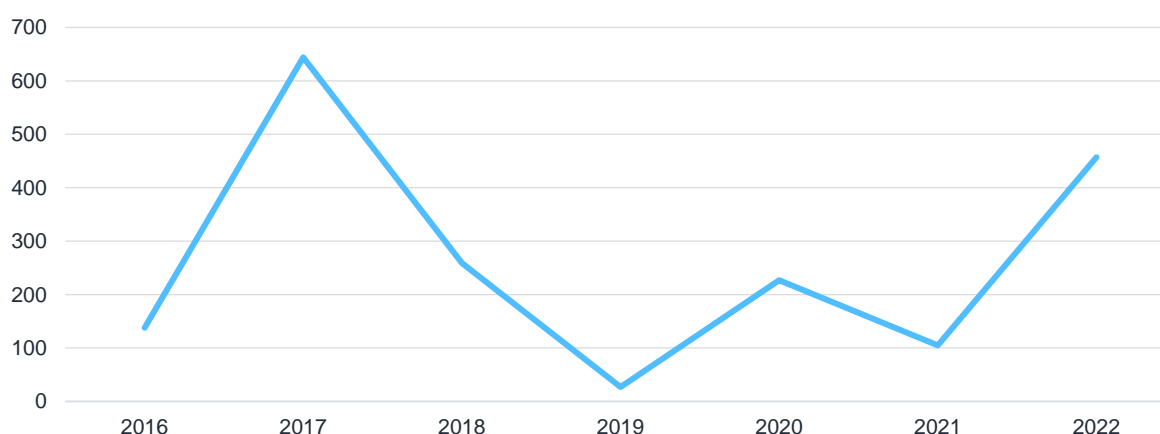
Perhaps the biggest differences between the Irish PRT market and the UK equivalent are the maturity of the market and (perhaps not surprisingly) its scale. Historically, risk transfer in the context of an Irish scheme focused primarily on activities such as managing investment risk through asset de-risking, and managing risks arising from the portfolio of deferred pensioners through enhanced transfer value exercises. Following the financial crisis in 2008, the minimum funding standard imposed by the pension regulator for DB pension schemes was suspended in 2009, and its reintroduction in 2012 saw funding challenges for many schemes. This contributed to growth in a bulk annuity market, primarily focused initially on pension buyouts relating to schemes in wind-up situations. Over time this has developed further, with buy-in transactions coming more to the fore as the focus shifts from wind-up situations to risk management of continuing schemes.

The overall scale of the Irish DB market is considerably smaller than the UK market, with figures reported by the Pensions Authority (the Irish pensions regulator) showing 525 DB schemes as at 31 March 2022 with total assets of c. €73.7 billion compared with liabilities of €65.0 billion.²⁶

Given the considerably smaller overall DB market in Ireland, it is no surprise that the PRT market is also considerably smaller. The chart below provides an overview of the estimated bulk annuity premium volumes in Ireland over recent years. Figures are estimates based on submissions provided by insurers active in the market. The chart highlights both the overall relatively small size of the market and the volatility of the market—a function of the “lumpy” nature of bulk annuity transactions and the relatively low volumes of transactions each year. 2017 was a notable high point, driven by the single largest transaction—a €335-million buy-in transaction between Irish Life and the Danske Bank Pension Scheme.²⁷

While transaction volumes have not yet matched the high-point of 2017, there was a considerable uptick in activity in 2022, driven in part by higher interest rates and cheaper annuity prices. We understand from sources in the market that there were transactions over the first half of 2023 totalling just over €100 million, but that a number of potential deals in the pipeline suggest the total figure for the year could exceed 2022 though the timing of completion remains uncertain.

FIGURE 2: BULK ANNUITIES ESTIMATED MARKET 2016-2022 FOR IRELAND



²⁶ The Pensions Authority (Ireland) (July 2022). Defined benefit schemes: Review of 2021 statistics. Available at: <https://pensionsauthority.ie/wp-content/uploads/2023/08/defined-benefit-schemes-review-of-2021-statistics.pdf>.

²⁷ Freimann, G. (December 2017). Irish Life seals €335m Danske Bank pension deal. Available at: <https://www.independent.ie/business/irish/irish-life-seals-335m-danske-bank-pension-deal/36422691.html>

5.1.2 What is driving demand for PRT in Ireland?

Initially, the bulk annuity market in Ireland was primarily led by buyout transactions focusing on schemes in wind-up situations. In more recent years, however, buy-in transactions have come more to the fore. This is in part a reflection of the improving funding position of schemes as the impact of the financial crisis has now largely washed through, with further notable improvements over 2022 and 2023 with rising interest rates. In addition, buy-in transactions are favoured by larger schemes where trustees can maintain the member relationship, and these can therefore tend to dwarf the scale of smaller buyouts.

Like the UK, the rises in interest rates have improved the funding position of Irish pension schemes as well as materially improving annuity prices. It is likely, therefore, that many Irish pension schemes that have not already de-risked will consider a buy-in. In particular, as well as providing de-risking from a longevity perspective, a buy-in may also effectively provide a DB scheme with access to higher-yielding assets. Going back five years or more, annuity pricing in Ireland was heavily driven by low-risk asset returns such as longer-term German sovereigns. In more recent years, however, the approach has changed with material proportions of higher-yielding assets being held.

One difference between the legislative environment for pension schemes in Ireland compared to the UK is that in Ireland there is no formal legal obligation on employers to support pension schemes in difficulty. In theory, this could drive different behaviours in terms of de-risking. From a trustee perspective, arguably the absence of a formal legal employer obligation could be an incentive to de-risk. Conversely, from an employer perspective, there may be more of an incentive to de-risk in the UK context given the ultimate legal obligation that sits with employers there. In practice, however, this factor does not appear to materially influence behaviours of employers or trustees in Ireland, though it is possible that over time, the lack of formal employer obligation may see a greater focus on de-risking among trustees.

5.1.3 Why do Irish life insurers write PRT business?

Perhaps a more accurate heading for this section would be “why don’t more Irish life insurers write PRT business?” Another material difference between the Irish and UK PRT markets is the number of insurers active in the market. While there have been five or six companies active in the market at various points over the last decade, the current number is much lower. We understand that since 2020 only two companies have written any material volumes of bulk annuity business. Unlike the UK, there are no monoline insurers specializing in bulk annuities, and no insurers for whom bulk annuities represent the most material line of business.

Part of the reason for this may come back to the “lumpy” nature of the transactions. Bulk annuities are expensive to sell, involving a considerable amount of time and expertise. In a market where there can be low numbers of transactions in a given year, this can require a material investment with potentially limited returns (given the small number of deals and binary nature of outcomes). In addition, the individual annuity market in Ireland has reduced in materiality over the last decade. Ireland has had a long-established drawdown product called the Approved Retirement Fund (ARF) that is now available to all DC pension retirees, and considerably higher volumes of ARF business are written each year compared to individual annuities. This may point to a lower prominence for annuity business in the arsenal of Irish life insurers.

No Irish annuity writers avail of the matching adjustment under the EU-wide Solvency II regulatory regime, and this may be a further indication of the appetite of Irish insurers for annuity business, as well as impacting the attractiveness of annuity pricing relative to alternative approaches. In part this is influenced by a technical point relating to the structure of the euro risk-free curve under Solvency II, which has a much earlier last liquid-point than the sterling equivalent. One effect of this is to materially reduce the impact of the matching adjustment on euro liabilities compared with sterling liabilities, and perhaps accounts for the lack of take-up of the matching adjustment in Ireland.

Despite these challenges, it does appear that there is increasing demand for PRT transactions in Ireland for the reasons outlined in the previous section, and this may well result in some growth in the bulk annuity market overall which may attract more insurers to enter the market.

5.2 CHALLENGES FACED BY THE INDUSTRY

5.2.1 Scale and maturity

Many of the challenges faced by the industry in Ireland are similar to those for the UK market, described in section 2.2. However, differences in the scale and maturity of the markets create some further challenges specific to Ireland. Lack of scale reduces the attractiveness of the market and leads to lower levels of competition among providers. It also creates challenges for alternative solutions. For example, longevity swap transactions are not a feature of the Irish market, as there are very few schemes that would have the scale to engage in a transaction of that nature. There have been some collateralized transactions, but again, transactions of this nature tend to require some level of scale to make sense, and the overall size of transactions limits the scope for collateralized arrangements.

Schemes themselves tend to be somewhat less mature than the UK market, and as a result, PRT transactions in Ireland tend to focus on pensioners in retirement. Unlike the UK market, we don't believe there have been many (perhaps any) transactions in Ireland that have covered deferred members as well as pensioners. This creates a challenge for schemes who would undoubtedly have some appetite for risk transfer solutions that could cover a more comprehensive set of members. Extending the scope of transactions to include deferred members would create a range of challenges for insurers active in the market. Perhaps increased competition could see a new entrant look to expand the level of coverage they were willing to provide, which could see a further expansion of the market as a result.

5.2.2 Inflation-linked benefits

One further challenge, more specific to the Irish market, relates to any pension benefits linked to Irish CPI. With far more limited options in terms of investments linked to Irish CPI or RPI, it is much more challenging for Irish insurers to find investments that match inflation-linked benefits accurately. The National Treasury Management Agency (NTMA) issued its first inflation linked bond in 2017, a private placement of a €609.5 million medium-term note maturing in April 2040. This was followed two years later by a second private placement of a €300 million medium-term note maturing in April 2045. Both notes are linked to the Eurostat Harmonised Index of Consumer Prices for Ireland (excluding tobacco). The limited availability of Irish-specific CPI-linked investments generates material basis risk and asset-liability matching challenges for any insurer taking on liabilities from Irish DB schemes. For the same reason, schemes themselves have challenges investing appropriately to match inflation-linked liabilities, which perhaps increases the incentive to de-risk through a PRT transaction in the first place.

5.2.3 Other challenges

As described in the section on the UK market, annuity pricing relies heavily on projections of future mortality rates. While this is inevitably a source of material uncertainty for annuity providers, the recent COVID pandemic has increased that uncertainty. Understanding the longer-term impacts of COVID on mortality rates, and the extent to which any increases in mortality rates arising from the pandemic are seen as temporary changes which will reverse over time, creates a heightened level of uncertainty, increasing risk for insurers and schemes exposed to longevity risk, and perhaps impacting insurer risk appetites and pricing approaches.

Irish insurers active in the annuity market tend to use material levels of reinsurance to further mitigate exposures to longevity risk, and the appetite of reinsurers for further longevity risk in the context of the wider uncertainty resulting from COVID may be a further challenge to the market in Ireland.

5.4 REGULATORY CONSIDERATIONS

5.4.1 Central Bank of Ireland

The Central Bank of Ireland (CBI) is the prudential regulator for insurance companies established in Ireland. Based on our discussions with participants active in the Irish PRT market, it does not appear that bulk annuities are a major area of focus for the CBI at present. In part, this may be reflective of the fact that the insurance companies active in the PRT market in Ireland are well-capitalised, long-established insurers, and perhaps in particular reflects the fact that bulk annuity transactions are not the most material line of business for any Irish insurer, with no monoline insurers concentrating solely on bulk annuity business.

As a result, the CBI's consideration of insurers' exposure to longevity risk and any concentrations arising from bulk annuity transactions is perhaps limited to the business as usual supervisory engagement with insurers, including oversight on insurers' risk management frameworks and the consideration of longevity risk in any relevant ORSA²⁸ scenarios.

5.4.2 Pensions Authority

The Pensions Authority is a statutory body charged with a range of responsibilities including the supervision of occupational pension schemes in Ireland, as well as advising the Minister of Social Protection on policy issues relating to pensions. We are not aware of the Pensions Authority having a formal stated view on PRT, but it does have an oversight responsibility relating to the funding of DB pension schemes, and we understand that Pensions Authority staff have encouraged scheme trustees to consider de-risking options such as buyout and buy-in transactions.

However, the position is perhaps a tricky one for the Pensions Authority to navigate. While de-risking strategies are likely to fit with the Pensions Authority's overall goals in terms of funding levels and related risks for DB schemes, it should also be acknowledged that pension risk transfer may not be a one-size-fits-all measure that works equally for all members. Under Irish pension legislation, the rights of pensioners in payment take precedence over deferred members or active employees. As a result, a pension buyout may provide a material benefit for current employees or deferred pensioners, as it may protect funding levels from sharp declines in interest rates. By contrast, this protection is unlikely to materially benefit retirees, while a buyout may potentially disadvantage retirees by impacting the likelihood of future inflationary increases to benefits.

5.4.3 Wider context of regulatory reform

Expected reforms in the Solvency II regulatory regime will clearly have an impact on Irish insurers (and on all EU insurers). In particular, proposed changes to the methodology for determining the euro risk-free rate, changes to the volatility adjustment mechanism and changes to the risk margin will impact the capital requirements for annuity writers. However, the political uncertainty around the final shape of the measures creates challenges for insurers active in this space or looking to enter the annuity market.

Occupational pensions schemes in Ireland have become increasingly focused on defined contribution (DC) solutions, with a decline in the number of DB schemes, and no material new DB arrangements being put in place. In parallel, the life and pensions industry in Ireland has become increasingly focused on unit-linked business and has seen reductions over time in the proportion of guaranteed business written by insurers.

The planned introduction of a DC auto-enrolment scheme in Ireland (targeted for launch in 2024, though this may be a challenging deadline to meet) will further cement the move towards DC arrangements in Ireland.

5.5 LESSONS LEARNED

Like the Netherlands, the Irish market has a small number of insurers active in the bulk annuity market at a time when there appears to be increasing demand for pension risk transfer solutions. Over the short term, we expect the high demand for buyout, and in particular buy-in solutions to continue, and this may attract more players into the market and lead to some innovation in terms of product design (for example solutions that also cover deferred members). However, over the longer term, we expect that the decline in relative importance of DB solutions will ultimately lead to a decline overall in the market for PRT solutions.

²⁸ Own Risk and Solvency Assessment as required under the EU-wide Solvency II regime.

6. Conclusions

- The Global PRT market in 2023 is bustling, and a common theme driving this activity is the higher interest rate environment which has improved funding ratios. The US and UK in particular are seeing increased demand, with expectations that volumes in these markets in 2023 will be record breaking.
- The Netherlands is anticipating more demand because of a recent pension reform which may encourage pension schemes to seek a PRT solution.
- Various challenges to insurers remain, and we observe similar issues reflected across the different markets. For example, having sufficient skilled personnel and capacity to write large volumes is seen as a constraint across all markets. Furthermore, ensuring the correct quality of data is accessible is a concern for insurers across markets.
- The regulatory environment highlights differences across markets as insurers in different markets will be regulated under different regimes. For example, some territories, such as those based in Europe, are undergoing reform of Solvency II, which is expected to change the way required capital is calculated.
- Some regulators, such as the PRA in the UK, explicitly expressed their concern on the PRT market, and so insurers should be mindful of the regulator's view in the management of their business. PRT activity is less likely however to be a worry for regulators of a smaller markets such as Ireland, where volumes are typically smaller.
- Those involved in the PRT market will of course wish to be aware of the activity and the changes that are taking place in the region that they are in. However, awareness of the global market should also be given thought; lessons can be learned from experience in the various global PRT markets that can be applied elsewhere. For example, there could be a lesson for other markets in the speed at which the US completes its transactions, and in the efficiency of the operating models of various UK PRT insurers.
- Stakeholders involved in PRT will likely benefit from looking at the global market and how it evolves year on year. The comparisons will provide useful insight and the sharing of expertise and experience can be helpful to the PRT market going forward.



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