2 April 2025

NOTICE

Prior Approval of New Long-Term Block Reinsurance Transactions

The Bermuda Monetary Authority (Authority or BMA) would like to provide an update on its Notice dated 8 April 2024 on the *Prior Approval of New Long-Term Block Reinsurance Transactions*. This Notice provides similar guidance to that outlined in the 8 April Notice while also clarifying the scope of transactions to be included under the prior approval process. In addition, it provides an update regarding the reconciliation of differences between the ceding company's Total Asset Requirement (TAR) and the Bermuda Economic Balance Sheet (EBS) TAR.

Context

As noted in the BMA Consultation Paper, *Proposed Enhancements to the Regulatory Regime for Commercial Insurers*[1], since January 2023, the Authority has required long-term (life) commercial (re)insurers (Classes C, D and E) (hereafter referred to as 'relevant insurers' or 'insurers') to seek prior approval for all block transactions. This requirement aims to:

1. Facilitate understanding of all block transactions occurring in the Bermuda market and the emerging risks they create for relevant insurers;

2. Ensure block transactions are subject to adequate review and oversight by the relevant insurers' control functions and governance forums in line with existing requirements;

3. Enable proactive, effective and efficient cross-border regulatory collaboration regarding specific block transactions and

4. Ensure block transactions are implemented in line with the regulatory and supervisory regime for commercial insurers.

[1] *Proposed Enhancements to the Regulatory Regime for Commercial Insurers* dated 28 July 2023: see page 3.

Scope

A long-term block reinsurance transaction is a reinsurance transaction involving the ceding of a defined group of in-force policies that results in the effective divesting of the liabilities and associated assets and transfers their risks (or most of their risks) to a reinsurance company. Transactions covering both future premiums (i.e., flow transactions) and in-force business are considered block transactions and are in scope. Examples of the types of transactions in scope include asset-intensive transactions, such as pension risk transfer and the ceding of fixed annuities, fixed index annuities, variable annuities and whole life or universal life policies. Examples of transactions that are not in scope include traditional mortality/morbidity solutions such as yearly renewable term reinsurance, longevity swaps and stop-loss coverage for biometric risks.

In addition to all new block transactions, modifications to existing block transactions will also be subject to the Authority's prior regulatory approval.

The requirement for prior approval of block transactions is in addition to the approval requirements that are applicable to 'material changes' under the Insurance Act 1978.

Transaction Specific Requirements

The BMA recognises that block transactions vary in size, complexity and impact on the risk profile of the relevant insurer. More complex transactions will require more comprehensive documentation, review, and regulatory engagement that align with the Authority's overarching risk-based and proportional supervisory framework. Accordingly, the scope and depth of the BMA's review of individual transactions varies on a case-by-case basis. Additionally, the BMA continues to support and implement strong cross-border regulatory collaboration with other global regulators, including through the transparent exchange of information. Consequently, the BMA will generally initiate transaction-specific regulator-to-regulator discussions.

The Authority's review process for block transactions is typically structured around a documentation review, followed by targeted discussions with the insurer's management team and, if required, other relevant regulatory contacts.

Existing requirements within the Insurance Code of Conduct require long-term (life) commercial insurers to maintain appropriate oversight and effective risk management and internal control frameworks, as well as adequate documentation regarding individual transactions. Therefore, the intention is that this process should not create any new process or documentation requirements for relevant insurers. Information provided to the Authority regarding proposed block transactions shall be the same as that used internally in the underwriting, risk assessment and governance review of the relevant transaction. In other words, the documents provided to the BMA shall be those that were used by the relevant insurer in its decision-making process and shall include information relating, but not be limited to[2], the following areas:

[2] Insurers may wish to contact their supervisors for further information required for specific transactions.

- Strategic rationale of the transaction
- Economics and key features of the transaction
- Information on strategy (underwriting and investment), expertise and risk and capital management
- Agreements for reinsurance, collateral and investment management
- Impact on solvency and stress testing
- Total asset requirements (technical provisions plus capital requirements) under both Bermuda and the cedant's regulatory basis
- Governance and risk management, including asset liability management

Information submitted to the BMA concerning the total asset requirements should include, but not be limited to:

1. Capital requirements and the associated breakdown of the key drivers (e.g., market risk, credit risk, insurance risk, operational risk, diversification benefit, etc.);

2. Target solvency ratios, which should be tied to the insurer's capital management policy;

3. Excess capital and surplus (i.e., capital buffer(s) above the capital requirements);

4. Best estimate liabilities and risk margin; and

5. Explanation and reconciliation of the material differences between the total asset requirements of the cedant and the Bermuda insurer's total asset requirement at a granular level.

The Appendix includes a detailed list of information that the insurer may consider submitting to the Authority regarding block transactions to facilitate an effective and efficient engagement and review process supporting its prior approval.

To facilitate an efficient review process, the BMA encourages relevant insurers to engage supervisory teams in preliminary pre-application discussions regarding transactions that are in advanced stages and may become the subject of a request for prior approval. This can be achieved either by including a 'deal pipeline' discussion as part of regular supervisory engagements and/or through ad-hoc engagement initiated by the insurer to notify the BMA of upcoming transactions.

The exact timeframe for the BMA's review of proposed block transactions is expected to vary. However, where requests are supported by effective and proactive engagement alongside complete documentation, the Authority expects to reach a decision within two to four weeks. Requests that do not meet these criteria may require additional time and/or information to be provided for the BMA to complete the review.

The BMA encourages insurers to notify their BMA supervisory contacts of any envisaged block transactions that the insurer plans to engage in as early as possible.

Appendix: Detailed Information to Support a Block Transaction's Prior Regulatory Approval

Relevant insurers may wish to consider the following considerations as the basis for efficient and effective engagement with the Authority regarding future block transactions. Information provided to the Authority may, therefore, include, but not be limited to:

1) Strategic rationale for the transaction;

2) Structure of the transaction;

3) Details of the underlying product (i.e., features and key terms), as well as the profile of the target policyholder(s);

4) Business background of the counterparty, including the results of its recent ratings and an assessment of its latest audited financial statements;

5) Risk profile, including a summary of underwriting risks and position against approved risk appetites and or risk limits;

6) Details regarding the transaction's funding;

7) A holistic picture of all relevant fees related to the transaction, e.g.,:

    a. Ceded commissions;

    b. Asset management fees projected to be earned by intra-group and affiliated entities; and

    c. All fees that accrue to the cedant or an affiliated party in any other way;

8) Liability profile (e.g., information on duration, the duration metric used, the basis of the duration calculation, etc.);

9) Asset portfolio profile (i.e., actual allocation and target allocation, if there is a difference);

10) Collateral and custodian arrangements;

11) Reinsurance and or retrocession arrangements and agreements, if any;

12) Investment management arrangements and agreement(s);

13) Total Asset Requirement (TAR) for this transaction: The Bermuda long-term reinsurer should provide a detailed breakdown of the TAR based on the solvency regime of the cedant, such as the US Statutory and RBC framework if the ceding company is in the US,

as well as the EBS framework. The following information should be provided at a minimum:

a. Capital requirements and the associated breakdown of the key drivers (e.g., market risk, credit risk, insurance risk, operational risk, diversification benefit, etc.);

b. Target solvency ratios – this should be tied to the capital management policy;

c. Excess capital and surplus, i.e., capital buffer above the capital requirement;

d. Best estimate liabilities and risk margin; and

e. Explanation and reconciliation of the material differences between the TAR of the cedant and the Bermuda EBS TAR at a granular level. The cedant TAR should be reported both on the cedant reporting basis, e.g., book value and market value basis, if this does not already apply under the cedant regime. The Bermuda long-term reinsurer should perform an attribution analysis to demonstrate the impact of each of the following changes, as the reserves, capital requirements, and eligible capital transition from the cedant's solvency regime to Bermuda EBS. The minimum steps involved in the attribution analysis are as follows:

    1. Begin with the market value of the assets supporting the cedant's total asset requirement at the cedant's target solvency ratio (MV TAR). Please disclose the target solvency ratio used;

    2. If the cedant's solvency regime is on a book value basis, then convert the MV TAR from 1 to a book value basis (BV TAR). Generally, any unrealised loss is added to the MV TAR to get the BV TAR and any unrealised gain is subtracted from the MV TAR to get the BV TAR;

    3. Subtract the cedant's required capital from the BV TAR (MV TAR if the cedant's solvency regime is not on a book value basis) to get the cedant's Technical Provisions;

    4. Subtract the cedant's risk margin (if any) from the cedant's Technical Provisions to get the cedant's Best Estimate Liability (BEL) or reserves;

    5. 5a, 5b, 5c, etc. Include a separate step to quantify each material difference in liability assumptions, methodology difference and discount rate difference under the cedant's BEL/reserve approach and the Bermuda Standard Approach;

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    6. Calculate the Bermuda BEL using the Scenario Based Approach (SBA), if such an approach is to be used;

7. Add the Bermuda risk margin to get the Bermuda technical provisions;

8. Add the Bermuda required capital to get the Bermuda TAR. Please disclose the target solvency ratio used; and

9. If the company plans to make changes to the asset allocation, calculate the Bermuda TAR assuming the new asset allocation has taken place.

For reinsurance transactions that include multiple product types, the TAR should be disclosed for each product. GAAP or International Financial Reporting Standards IFRS reserve numbers should also be provided.

14) Impacts on solvency and stress testing, such as:

a. Impacts on excess (economic) capital;

b. Impacts on surplus liquidity;

c. Financial projections for the next five years;

d. Capital projections for the next five years; and

e. Proforma Bermuda solvency capital requirements.

15) Operational impacts, including comments on the continued suitability of the current capital charge for operational risk;

16) Impacts on the SBA (if utilised);

17) Actuarial analysis and commentary on assumptions;

18) Termination events;

19) Risk function's view of the transaction and an assessment of risks to the relevant insurer that are inherent within the transaction; this should also detail the risk function's involvement in the transaction;

20) Minutes and papers from the meetings of the appropriate governance forum within the Company confirming approval of the proposed business;

21) Internal memos, including pricing, experience studies for key assumptions, or any other management information considered for the transaction;

22) Confirm whether the cedant requires regulatory approval to complete the transaction; and

23) Contact details of the cedant supervisor.

Please note that the Authority does not expect separate documents to be created to cover the above information requests. However, it may be helpful to provide a cover sheet, if needed, to provide relevant context to the prior approval application, indicate where relevant information is located or indicate when any information not provided may be expected to be submitted to the Authority.

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