SLAUGHTER AND MAY

# Pensions derisking

# Our team

We have a broad and deep team who work on our derisking matters. A selection of key members of the team is shown below. Our core team is supported by a strong range of specialists in all the usual fields.

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# Derisking defined benefit pension liabilities

Slaughter and May's Pensions Derisking Group is at the forefront of devising and implementing structures which enable insurers to remove or limit corporate sponsors' defined benefit pension liabilities and, if appropriate, pass on part of that risk to reinsurers or other counterparties.

Many different factors influence the decision as to the right structure, the right ingredients for that structure and the right counterparties. These can include:

- **the risks being mitigated** - all or some only of longevity risk, interest rate risk, inflation risk, investment risk
- **price** - whether the budget of the trustee can pay for the desired level of risk transfer
- **timing** - how quickly the scheme and the corporate are able to transact
- **scheme specific factors** - data quality, benefit structure, historic compliance
- **trustee risk appetite** - whether the trustees are willing to consider less "vanilla" options
- **insurer's requirements** - including the level of risk that the insurer wishes to retain and its desired treatment of the business (including for capital purposes).

The necessary attributes for legal advice in these transactions are:

- extensive experience of many types of structure and in particular the expectations of counterparties
- a desire to innovate
- a deep understanding of liability transfer - what this entails and its limitations
- an ability to manage and complete large complex legal transactions to often demanding timescales
- an ability to draft for the long term - the implemented structures need to rely on documentation which is clear and predictable enough to last for the duration of the structure (often 40 years+)
- experience of working co-operatively with other advisers.

Our Pensions Derisking Group has these attributes and a track record to back it up. We are leaders in the areas of scheme buy-outs and buy-ins, longevity hedging and reinsurance and portfolio transfer and optimisation.

> **Always very thorough, technically very strong and creative in finding solutions to problems.**
>
> Chambers UK, 2017

# Our expertise

**We believe it is a significant advantage to use a law firm with our level of expertise and experience, in particular where a bespoke approach is required. Even where aspects of BPA work are becoming more standardised, these are transactions with potential for significant reputational and financial risk and we would typically spend as much time considering, and discussing with you, different approaches and their risks and consequences, together with scenario planning, as drafting legal terms. Below are a few examples of our experience in this space.**

## Buy-ins

We advised Akzo Nobel/ICI in the biggest UK buy-in to date at the time – ICI Pension Fund's deal with Legal & General (£3 billion) and Prudential UK (£0.6 billion).

In October 2017, we advised Legal & General on the de-risking of The Pearson Pension Plan by way of a circa £600 million buy-in transaction with the Trustee of the Plan. The buy-in utilises an innovative umbrella contract structure that allows for further transactions to be completed quickly under existing contracts.

Also in 2017 we advised the trustees of the Monsanto scheme on a buy-in transaction with Scottish Widows and 3i on a buy-in by its scheme with PIC.

## Buy-outs

We advised Royal Philips NV on the transfer of £2.4 billion of the Philips UK Pension Fund's defined benefit obligations to PIC. This was expected to give rise to the largest full pension buy-out in the UK at the time.

In 2016, we advised a leading insurer on the initial due diligence stages of a substantial "all risks" bulk annuity transaction.

The market to date has seen fewer large buy-outs than buy-ins. As market capacity increases, we expect more large buy-outs – most of the underpinning technology is the same as for buy-ins.

## Longevity swaps and reinsurance

In March 2014, we advised Aviva on the largest longevity hedge transaction in the UK to date. This involved the derisking of the Aviva Staff Pension Scheme by way of a circa £5 billion longevity hedge transaction involving insurance and reinsurance arrangements, which allowed the defined benefit scheme to reinsure the longevity risk relating to approximately 19,000 of its members.

We advised Delta Lloyd Levensverzekering, the Dutch life insurance arm of the Delta Lloyd Group, on a transaction with Reinsurance Group of America (RGA) to mitigate longevity risk related to its Dutch life insurance portfolio by way of a six year longevity swap. The swap is based on Dutch population mortality data and relates to underlying longevity reserves of approximately EUR 12 billion.

We advised AEGON on (i) its €12 billion longevity swap with Deutsche Bank. The transaction is based on Dutch population data which is applied to a synthetic portfolio and will enable AEGON to hedge liabilities on a portion of its annuity book; and (ii) a second innovative longevity transaction to reduce its risk from future improvements in longevity in the Netherlands. Aegon's partners in the execution of this transaction were Société Générale in the role of intermediary and Risk Management Solutions as modelling agent. The risk was assumed by third-party investors and reinsurers including SCOR.

> They have bucket loads of previous experience and are quite innovative, solution-driven and practical.
>
> Chambers UK, 2016

We also advised AEGON Levensverzekering as one of the syndicate of reinsurers hedging the exposure of Deutsche Bank AG under its longevity swap with the Trustees of the Rolls-Royce Pension Fund. The longevity swap relates to £3 billion of the fund's liabilities to approximately 37,000 pensioners.

We advised Aviva on a transaction with PartnerRe and RBS under which Aviva transferred the longevity risk on a £475 million book of business until 2018. An innovative transaction structure was used under which the risk was ultimately placed with a range of capital markets investors.

## Benefit change exercises

We have advised on a very large number of these including INEOS Grangemouth, Unilever, United Utilities, Caterpillar, BOC, GSK, Royal Mail, Cadbury and Ladbrokes.

More and more case law (most recently, the IBM case) raises technical barriers to effecting benefit change in addition to the usual matters such as employee and trustee consent – it is important to be able to identify and deal with such aspects in a clear and timely way.

## Funding structures

We are leaders in structuring and establishing vehicles which allow company property to be used to fund pension schemes whilst remaining within the control of the sponsoring employer and have acted for many corporates and pension schemes doing so including Marks & Spencer, Diageo, Aviva and ITV.

## Other derisking

In an effort to identify and mitigate particular risks and concerns, many structures are unique in their mix, or may have aspects used for the first time. We acted for Uniq on one of the first pension deficit for equity swaps. We acted for Unilever in setting up a global centrally held insurance policy which itself counted as a plan asset for corporate accounting purposes.

We advised Tata Steel on the restructuring of the £13 billion British Steel Pension Scheme.

## Portfolio transfer and optimisation

We advised RSA on its disposal of £834 million of UK legacy liabilities to Enstar in 2017, which took the form of a Solvency II compliant collateralised reinsurance arrangement (initially on a funds withheld basis with a fully-funded Bermudian segregated account company, with novation to a Bermudian reinsurer with third party custody and collateral management arrangements) followed by a subsequent Part VII transfer of the business.

In December 2017, we advised Legal & General on the sale of its £33 billion Mature Savings business (including both unit linked business and its with-profits fund) to the ReAssure division of Swiss Re for £650 million, which involved an innovative reinsurance structure pending a subsequent Part VII transfer.

## Solvency II

We also routinely advise insurers on Solvency II optimisation work, including in relation to matching adjustment-compliant structures in respect of their existing portfolios. We have published a market-leading guide to Solvency II (recently updated).

In the run up to the implementation of Solvency II we advised Legal & General on the collapse of its longevity ISPV, LGPL, into LGAS and the establishment of a series of matching adjustment compliant SPVs to optimise real estate, FX credit and ERM portfolios.

## A. Examples of buy-ins and buy-outs where Slaughter and May has advised

| No | Sponsor/scheme/provider | Size (reported) |
|---|---|---|
| 1. | ICI Pension Fund (ICI) | £3.6 billion |
| 2. | Royal Philips NV | £2.4 billion |
| 3. | RSA | £1.9 billion |
| 4. | Cable & Wireless (Prudential) | £1.05 billion |
| 5. | GlaxoSmithKline | £900 million |
| 6. | Pearson (Legal & General) | £600 million |
| 7. | BBA Aviation | £300 million |
| 8. | General Motors UK | £230 million |

## B. Examples of longevity swaps or reinsurance where Slaughter and May has advised

| No | Sponsor/scheme/provider | Size (reported) |
|---|---|---|
| 1. | AEGON annuity books | €12 billion + €1.7 billion |
| 2. | Delta Lloyd Levensverzekering (DLL) | €12 billion |
| 3. | Standard Life annuity book | £6.7 billion |
| 4. | Aviva – Aviva Staff Pension Scheme and RAC (2003) Pension Scheme | £5 billion + £0.6 billion |
| 5. | AEGON – Deutsche Bank/Rolls-Royce Pension Fund | £3 billion |
| 6. | Deutsche Bank – AstraZeneca and Carillion schemes | £2.5 billion + £1 billion |
| 7. | Aviva – Aviva annuity book – RBS – Partner Re and other investors | £475 million |

## C. Examples of funding structures where Slaughter and May has advised

| No | Sponsor/scheme | Aggregate size (reported) |
|---|---|---|
| 1. | Marks & Spencer | £1 billion |
| 2. | Diageo | £430 million |
| 3. | ITV | £215 million |
| 4. | John Lewis | £95 million |
| 5. | Whitbread | £85 million |

Note: the Slaughter and May client in each case was the corporate, the pension scheme or the counterparty.

# Our broader insurance and pensions practices

## Insurance

We have a market-leading insurance practice that spans both the life and general sectors. In addition to our experience in a full range of derisking transactions we advise many of the major players in the sector and have been involved in the largest and most complex insurance work. This includes:

- private and public M&A, joint ventures and closed fund deals (including the recently announced Prudential demerger, Standard Life Aberdeen-Phoenix and Legal & General-Swiss Re transactions)
- establishment and structuring of insurance and reinsurance operations for a variety of other insurance ventures, both large and small (for example, establishing the Resolution and EICG vehicles and through our Fintech Fast Forward programme)
- financing matters, which includes the regulatory capital needs of our insurance clients, such as acting on recent RT1 note issuances (we advise a majority of the major insurers on treasury work)
- demutualisations, flotations, restructurings and Part VII transfers (including a substantial number of Brexit-related Part VII transfers)
- commercial contracts, including distribution, administration and outsourcing arrangements
- regulatory and governance advice, including the implications of Solvency II.

## Pensions

One of the hallmarks of our pensions practice is our involvement in the most complex and innovative pensions related matters.

We act both for sponsors and trustees on a range of matters, including:

- establishing and operating all kinds of registered and non-registered UK schemes
- pension benefit change exercises/pension fund deficits including funding valuation negotiations/derisking solutions
- investment issues including implementation of liability driven investment strategies and funding via asset backed partnerships
- restructuring, merging and winding-up of schemes
- pension aspects of M&A, flotations, privatisations, reconstructions and demergers including applications for clearance from the Pensions Regulator
- assisting employers in compliance with auto-enrolment duties under the Pensions Act 2008
- pension disputes
- routine advice including attendance at trustee meetings.

**An outstanding firm. Their technical ability continues to be a differentiator in our industry, and they are incredibly responsive and very pragmatic.**

Chambers UK, 2017

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