

APRIL 2026

PROPOSED CHANGES TO THE REGULATORY TREATMENT OF FUNDED REINSURANCE

On 29 April the PRA published a [consultation paper](#) on changes to the prudential treatment of funded reinsurance arrangements. The consultation was announced in a [speech by Gareth Truran](#), the PRA's Executive Director of Insurance Supervision.

After many months of informal consultations with industry and reams of data collected, the PRA has signalled a strong message that it wants to limit and restrict the use of Funded Re for life insurance (and particularly BPA) business. Although framed as a consultation, we can expect minimal changes to policy to arise between now and the policy statement, recognising that the PRA has heard many views and arguments on the position and clearly views this as a reasonable compromise of the available alternative options.

In this briefing we discuss the key proposed changes and the background to the proposals, and share our initial views.

Key points from the consultation

- A new definition of “funded reinsurance” is proposed. This will include entry into arrangements to back either annuity or capital redemption liabilities
- In order to align the regulatory capital treatment of funded reinsurance arrangements with other economically similar assets, the PRA proposes introducing changes to the Counterparty Default Adjustment calculation to be applied to recoverables under funded reinsurance arrangements. **It estimates that these changes would increase the amount of capital held in respect of funded reinsurance from 2-4% of the value of the underlying annuity liabilities to around 10%**
- The changes would not apply to arrangements where all the risks covered are fully transferred to the reinsurer by the end of September 2026. The PRA considers that applying the new requirements to existing in-force (and potentially long-term) arrangements could be excessively disruptive to the market
- Intra-group funded reinsurance arrangements, provided they meet certain criteria, will be excluded from the new requirements, as will interim reinsurance arrangements entered into as part of a Part VII transfer process
- The PRA has not at this stage proposed introducing volume limits on the use of funded reinsurance or above which a higher capital impact would be applied. It has not taken volume limits off the table, however, as a future option if ongoing monitoring suggests further action is required
- The consultation closes on 31 July 2026.

Background

The domestic context

The use of funded reinsurance by insurers to transfer risk assumed under pension derisking transactions has been a key area of scrutiny by the PRA for a number of years. Key concerns are the concentration and recapture risks associated with these transactions, including the risk that on a recapture the collateral held does not satisfy relevant matching adjustment requirements and cannot easily be transformed through planned management actions. A [supervisory statement](#) was published in July 2024 setting out how the PRA expected firms using funded reinsurance to ensure compliance with existing standards.

In September 2025, the PRA highlighted in a [speech by Vicky White](#) its ongoing concerns with the use of funded reinsurance. She indicated that the PRA was also questioning whether the prudential treatment of funded reinsurance under the Solvency II regime is appropriate, as an unbundling of the asset component from the longevity risk cover would result in a different treatment under the rules.

The PRA is also of the view, as discussed in the current consultation, that the use of funded reinsurance has led to large amounts of assets which insurers might otherwise invest in the UK being transferred to offshore reinsurers. It suggests in the paper that the proposals are “*expected to lead to an increase in UK productive investments*”. This may be an oversimplification, as it is difficult to say with any certainty the investments which insurers would have made absent the availability of funded reinsurance.

Industry roundtables were held in autumn 2025 and the PRA commented in its [January 2026 Dear CEO letter](#) that it was considering new policy proposals for the regulation of funded reinsurance, which might include explicit regulatory restrictions on the amount and structure of funded reinsurance or measures to address any potential underestimation of risk.

The international context

The UK is not alone in expressing concerns about the use of funded reinsurance. The IAIS published an [issues paper](#) in November 2025 on structural shifts in the life insurance sector, highlighting the increased use of funded reinsurance (described in the paper as “asset-intensive reinsurance”) and the supervisory concerns with these transactions - including complexity of the arrangements, recapture risk, concentration risk and the potential for regulatory arbitrage. As noted by the PRA, both the Dutch National Bank and the National Association of Insurance Supervisors in the US have recently taken steps to increase supervision in relation to funded reinsurance arrangements. In introducing specific changes to the prudential treatment of funded reinsurance, however, the PRA is currently an outlier - albeit that it is responding to developments which are to an extent particular to the UK market. This could have the potential to impact the attractiveness of funded reinsurance for UK insurers, and of UK reinsurance business for international reinsurance groups.

The detailed proposals

The PRA’s regulatory concerns

The PRA’s view is that the current regulatory treatment of funded reinsurance does not appropriately reflect the underlying risks and is not aligned to that of economically similar assets. It considers that this misalignment currently encourages insurers to rely excessively on funded reinsurance arrangements to support their BPA activity. The PRA’s figures suggest that in recent years about 15% of new BPA business written by UK insurers has been ceded via funded reinsurance.

The Counterparty Default Adjustment (CDA)

Under the Solvency UK rules, insurers’ insurance liabilities should be calculated net of reinsurance, with reinsurance recoverables calculated separately on the asset side of the balance sheet. In calculating the reinsurance asset, firms should apply a counterparty default adjustment to reflect expected losses due to the

default of the counterparty (the “CDA”). In order to more closely align the prudential treatment of funded reinsurance arrangements with economically similar assets the PRA is proposing changes to the rules relating to the calculation of the CDA. These changes will introduce a “fundamental spread” element to the calculation which the PRA considers would more closely align the CDA with the way in which the matching adjustment calculation reflects risks retained by the firm in respect of assets held to back its annuity liabilities.

The proposed changes to the CDA

The proposed changes would introduce a requirement that the CDA applied to a funded reinsurance arrangement must be equal to the fundamental spread for financial corporate bonds, corresponding to the credit quality step (“CQS”) and maturity of each of the funded reinsurance cashflows. The CQS should be based on the insurer financial strength rating issued for the reinsurer by an external credit assessment institution.

The CQS can be adjusted upwards where the funded reinsurance arrangement meets one or more of the following criteria (with a potential one-notch upgrade in each case):

- the collateral fully covers the premium at inception and is adjusted thereafter only for changes in market conditions and claims experience (**adequate collateral**)
- the collateral is 100% MA eligible in line with the firm’s permissions and any mismatch between the cashflows of the collateral and the contractual cashflows of the funded reinsurance do not give rise to material risks (**absence of a need for collateral transformation**)
- the weighted average rating factor of the worst-case collateral portfolio indicates the collateral has a higher credit quality than the counterparty (**credit enhancing nature of collateral**).

The PRA has estimated that these changes would increase the amount of capital held in respect of funded reinsurance from 2-4% of the value of the underlying annuity liabilities to around 10%. This is likely to make the use of funded reinsurance less attractive than it is currently from the perspective of achieving a capital benefit, although the PRA considers that it is still less than the 11-15% of capital held in respect of economically similar assets. Gareth Truran noted in discussion following his speech that firms may also still be attracted to the use of funded reinsurance for other reasons, including to originate assets they cannot originate themselves or to manage capital strain.

Governance and oversight

The PRA proposes introducing an expectation that a firm’s approach to determining the CQS for a funded reinsurance arrangement is documented and approved by a Senior Management Function, and that the methodology is presented to the firms governing body.

Definition of funded reinsurance

The proposed new definition of “funded reinsurance” is:

“a reinsurance contract under which a firm transfers to a reinsurer credit risk or market risk relating to annuity obligations that arise under contracts of insurance falling within long-term insurance business class I or obligations that arise under contracts of insurance falling within long-term insurance business class VI”.

As noted above, this includes reinsurance in respect of capital redemption business. Intra-group quota share funded reinsurance arrangements meeting certain conditions and interim reinsurance in connection with a Part VII transfer will be excluded from the new requirements.

Implementation date

The changes would not apply to arrangements where all the risks covered are fully transferred to the reinsurer by the end of September 2026. The PRA considers that applying the new requirements to existing in-force (and potentially long-term) arrangements could be excessively disruptive to the market.

The 30 September date recognises that firms may have proposed arrangements already in train, but the PRA comments that it “*expects the volume of new funded reinsurance arrangements to be transacted before 30 September 2026 to be consistent with firms’ existing plans*”. It will no doubt scrutinise any attempts by firms to accelerated entering into funded reinsurance transactions ahead of that date in order to take advantage of the current more advantageous prudential treatment. As a practical matter, capacity constraints and the lead time on these arrangements make it less likely that a significant rush to transact currently unplanned new deals would materialise, though it could impact on how quickly cedants and reinsurers move to transact deals that are already in prospect (particularly where this could utilise existing framework terms).

What possible changes were rejected?

The PRA had considered addressing the perceived issues with funded reinsurance by “unbundling” the arrangement into distinct reinsurance and investment components and applying different regulatory treatment to each. Following industry feedback it decided against this approach due to the potential operational complexity and the modelling work which would be required. It considers that changes to the CDA should be a more straightforward method to achieve a similar regulatory outcome.

The PRA also considered adding volume limits on the amount of annuity liabilities that firms could cede via funded reinsurance arrangements. It has decided against this but comments that it could revisit this if ongoing monitoring suggests further action is required. Gareth Truran confirmed in discussion following his speech that the funded reinsurance component would remain in place in the next LIST exercise in 2028, which the PRA will use as an opportunity to reflect on the changes to the funded reinsurance regime and how it might develop this further in the future.

It is also notable that the PRA’s proposals would only apply to business for which the risks are transferred to the reinsurer after September 2026, without retrospective effect, which may attract responses in the consultation from insurers that have made less use of funded reinsurance to date than their competitors.

Comment

UK insurers using funded reinsurance for capital benefits will want to take time to model the economic consequences of the proposed changes and are likely to have a balanced decision to make on whether the cost and impacts are worth it, thus potentially reducing the number of funded reinsurance deals in the life insurance market.

UK insurers that use funded reinsurance in effect to access and obtain exposure to asset classes that are not otherwise readily available to them will also need to model the position carefully, but are more likely to be willing to accept the higher charge. They may, however, want to look more carefully at the credit quality of their counterparty.

Looking at the wider picture, and trying hard to find something positive in the proposals, the change may be of net benefit to the largest global reinsurance groups with high credit quality, as the changes may lead cedants to shy away from arrangements with smaller or lower credit quality groups that would result in a higher charge.

There is also a potential impact on the underlying bulk purchase annuity market as the use of funded reinsurance has the potential to reduce the costs for firms of writing BPA transactions. The strong capital position of insurers in this market and the competitive nature of the market, as well as the fact that a majority of business is not backed by funded reinsurance, may minimise this impact.

CONTACTS



NICK PACHECO
PARTNER
T: 020 7090 3143
E: nicholas.pacheco@slaughterandmay.com



NICK BONSTALL
PARTNER
T: 020 7090 4276
E: nick.bonsall@slaughterandmay.com



TOM PEACOCK
PARTNER
T: 020 7090 4256
E: thomas.peacock@slaughterandmay.com



BETH DOBSON
KNOWLEDGE COUNSEL
T: 020 7090 3070
E: beth.dobson@slaughterandmay.com

London
T +44 (0)20 7600 1200
F +44 (0)20 7090 5000

Brussels
T +32 (0)2 737 94 00
F +32 (0)2 737 94 01

Hong Kong
T +852 2521 0551
F +852 2845 2125

Beijing
T +86 10 5965 0600
F +86 10 5965 0650

Published to provide general information and not as legal advice. © Slaughter and May, 2025.
For further information, please speak to your usual Slaughter and May contact.

www.slaughterandmay.com