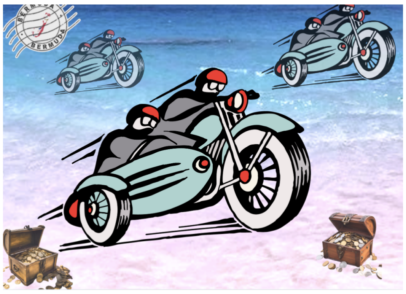
'Reinsurance Sidecars': A Capital Idea

By Kerry Pechter *Sun, Dec 1, 2024*

Athene Annuity & Life sold the most fixed deferred annuities in the first three-quarters of 2024. Its parent, Athene Holdings, has attracted billions in just-in-time third-party capital through Bermuda 'reinsurance sidecars.' Coincidence? Not likely.



The word *sidecar* evokes mental images of passenger-carrying attachments to motorcycles or of the sweet cocktail made from cognac, Grand Marnier, and lemon juice that was popular in London and Paris during the 1920s.

In the complex global reinsurance game, sidecar has a different meaning. It refers to off-balance-sheet special purpose vehicles (SPVs) that reinsurers set up, often in Bermuda or the Cayman Islands, to raise capital from, or share risk with, outside investors.

Property/casualty insurers have used sidecars for years to pay for the tsunamis of claims that hurricanes, wildfires and earthquakes can suddenly spawn. Starting in 2019, reinsurers affiliated with major life/annuity companies began creating them to share the cost and risk of selling fixed deferred annuities.

Athene Holding, parent of Athene Life & Annuity, set up the first big life/annuity sidecar in Bermuda in 2019. The vehicle was called ACRA (Athene Co-Invest Reinsurance Affiliate). It has raised billions of dollars from third-party investors for Athene to use as deal capital or capital relief and for Athene's affiliate, Apollo Global Investors, to manage. A small herd of others (see chart below) fast-followed.

Sidecars are a logical next step for the private equity/alternative asset managers that have steadily grown their footprint in the annuity business over the past decade. They are latest twist to the Bermuda Triangle strategy that *RIJ* has documented since 2020.

That strategy involves a private equity company with expertise in originating high-yield loans to risky borrowers; a life insurer that taps into the trillions in Boomer retirement savings by issuing fixed deferred annuities, and an (usually affiliated) reinsurer domiciled in Bermuda, with its flexible regulations and interface with international money. A sidecar makes the triangle a foursome.

Here's roughly how the story has unfolded:

- After the Great Financial Crisis, private equity companies, led by Apollo, infused ailing life/annuity companies with capital, buying their underfinanced blocks of annuities or showing them how to add high-yield private credit to their general asset mix.
- The private equity firms then began acquiring, starting, or reviving dormant life insurers to issue fixed indexed annuities and (since 2022's interest-rate rise made them so attractive) fixed rate deferred annuities.
- The private equity-led insurers set up their own affiliated reinsurers in Bermuda to move liabilities off their own balance sheets and reduce required capital. "Modified co-insurance" and "funds withheld reinsurance" allowed them to maintain control of the assets backing the liabilities.
- The reinsurers set up sidecar/SPVs to raise "just-in-time" capital to increase their annuity sales capacity, reduce their own capital burdens, or seize opportunities to buy pension funds or blocks of annuity business.
- Sidecars enabled hedge funds, sovereign wealth funds, and limited partnerships of private equity firms, and other asset managers to add stable, non-correlated, tailored diversifiers to their portfolios—for a few years or much longer.

Look for sidecars to proliferate. Traditional life insurers like MassMutual and Prudential have set up their own reinsurers or sidecars. In early 2023, upstart Kuvare Holdings set up Kindley Re, a sidecar that gave it access to $400 million in fresh capital. In December 2023, the traditional reinsurer RGA set up the Ruby Re sidecar, and expressed its "expectation that a number of life insurers will explore the use of sidecars in the coming years."

Sidecars defined

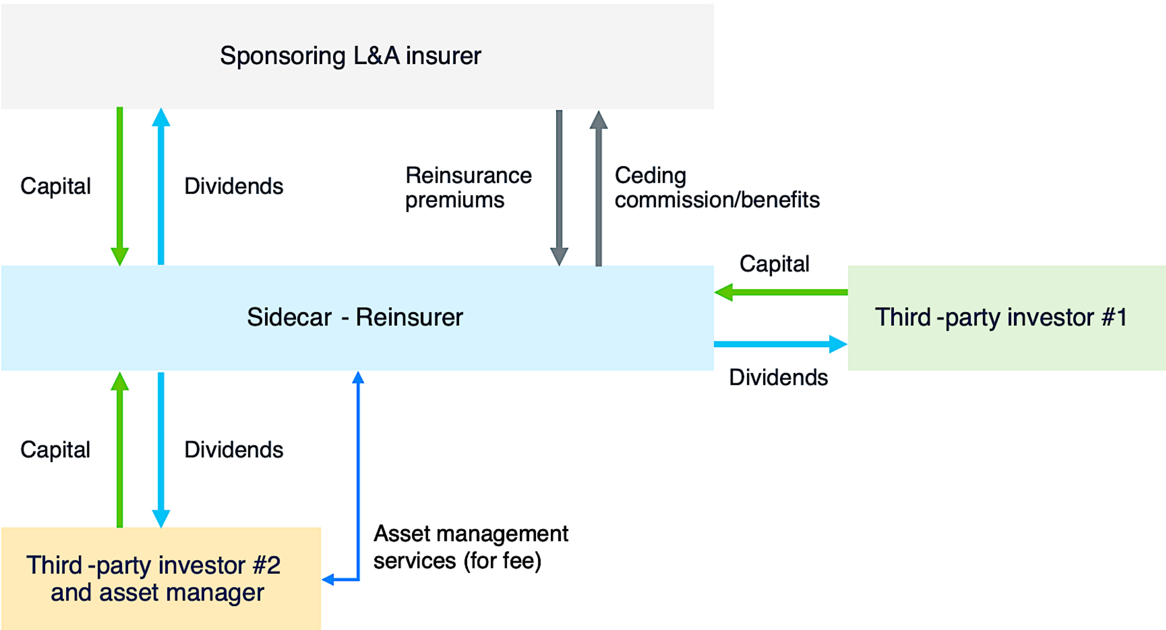
"'Sidecar' reinsurers are typically formed by a sponsoring insurance group with the support of third-party investors, the latter of which may provide capital in exchange for a portion of the sidecar's excess returns [i.e. profits]," according to **ALIRT Insurance Research**. "Third-party investors may also enter into agreements to manage a portion of the assets that support the sidecar's assumed policy reserves."

In the property/casualty realm, FINRA has described reinsurance sidecars as "special purpose vehicles that issue debt or equity and invest the proceeds in low-risk securities, which serve as collateral." Investors in the sidecar earn a variable yield from the securities, as well as a reinsurance premium. But the original insurance writer can tap that collateral—all of it, if necessary—to meet a catastrophic wave of claims or surrenders.

"Like traditional reinsurers, the sidecar reinsurer assumes a portion"—a "quota share"—of the ceding company's underwriting risk (including losses and expenses) in exchange for a like-percentage premium (hence the term 'sidecar')," according to a report published by **International Risk Management Institute**.

"Sidecars are usually set up by an affiliated insurer or reinsurer and capitalized by equity and debt financing. The capital is invested and used to pay claims. Funds are also returned to the affiliated company to pay debt interest and shareholder dividends."

Sidecars are related to but differ from traditional reinsurers and also from captive insurers, although there may be some overlap in how the three balance sheet management tools are used. Since a reinsurer can set up a sidecar, or a primary insurer can "sponsor" a "reinsurance sidecar," the terminology can be confusing. MassMutual's Martello Re reinsurer is not, it has been said, a sidecar.



Source: Milliman.

Drivers of sidecars

Athene's asset management arm, Apollo Global Management, was the first big private equity firm to start buying U.S. life/annuity companies insurers, and the first to set up a sidecar. After ACRA in 2019, which attracted a reported $6 billion in outside capital, Athene created the "Athene Dedicated Investment Program" (ADIP) in 2022. ACRA II and ADIP II soon followed.

Competing annuity issuers (and their asset manager-owners) quickly joined in. So far they include Global Atlantic (KKR), Security Benefit (Eldridge), MassMutual (Barings, Centerbridge) American Equity Investment Life/(Brookfield Asset Management), and Kuvare Holdings (Blue Owl).

Their goals are similar to Athene’s. “ACRA I provided Athene with access to on-demand capital to support its growth strategies and capital deployment opportunities,” according to Athene’s latest 10-K. “Similar to ACRA I, ACRA II was funded in December 2022… These strategic capital solutions allow Athene the flexibility to simultaneously deploy capital across multiple accretive avenues, while maintaining a strong financial position.”

The sponsoring insurer can use the capital that others invest in the sidecars for either offensive or defensive purposes. For instance, it can serve as a second line of defense if and when a life/annuity company suffers losses on its own investments that threaten its ability to pay annuity contract benefits or surrenders.

A sidecar can also serve as an offensive weapon; as “on demand” capital, as noted above by Athene, or “just-in-time” capital, as described by AM Best, to be tapped when an opportunity to underwrite new risks or to buy an attractive block of existing business. Accessing capital on a “just-in-time” basis allows the insurer to practice the “capital-light” business strategy that private equity-led life/annuity companies aspire to. [An insurance company is more profitable, but weaker and more leveraged, when its owners tie up less of their own capital in the business.]

ACRA and ADIP have paid off for Athene Holding. “Third-capital enables Athene to grow in a highly capital-efficient manner and supported 35% of Athene’s gross new business” in the second quarter of 2024, according to a report in the Bermuda-focused insurance magazine at Artemis.com.

“At the mid-point of 2024, ADIP program invested assets reported by Apollo stood at more than $69.25 billion, with some $9.26bn of inflows via the ADIP sidecar program just in the first-half of this year. Apollo also reported a gross IRR of 24% for ADIP I investments, as of the middle of this year.”

Life/Annuity Reinsurance Sidecars			
Sidecar name	**Sponsor/Asset Manager**	**Funding**	**Launch date**
ADIP II/ ACRA II	Athene/Apollo	$6 bn	July 2024
Malibu Life Re SPC	Third Point LLC		May 2024
Ruby Re*	Reinsurance Group of America		Dec 2023
Prismic Life Re	Prudential/Warburg Pincus		Sept 2023
ACRA II	Athene/Apollo		Sept2023
Ivy Re II	Global Atlantic/KKR		July 2023
Kuvare Holdings	Kindley Re/Blue Owl	$400 m	Jan 2023
AEL Bermuda Re	American Equity/Brookfield	$300 m	Jan 2022
Martello Re	MassMutual/Barings, Centerbridge	$1.615 bn	Jan 2022
Skyridge Re	Security Benefit/Eldridge		2021
Ivy Re	Global Atlantic/KKR	$1 bn	April 2020
ACRA I	Athene/Apollo	$3 bn	2019
Sources: Artemis.com, Milliman. *Domiciled in Missouri; all others offshore.			

Sidecar passengers

On the other side of the deal are the third-party investors in the sidecars. These institutional investors want exposure to the life/annuity industry (and, through it, to the profits associated with managing the vast pool of retirement savings in the U.S.) but don’t want to buy shares in a life/annuity insurer.

Investors in these sidecars are said to be hedge funds, sovereign wealth funds, the limited partnerships of other private equity funds, and asset managers who might invest in the sidecar and take part in managing the sidecars’ overall investments or a portion of them.

For those entities, “Life/annuity sidecars should be considered as another investment opportunity, like investing in a public life insurer’s stock or buying an ILS [insurance-linked security; a type of high-yield debt],” Milliman’s Prannoy Chaudhury told *RIJ* recently.

A sidecar’s ability to offer customized investment opportunities is part of their appeal to third-party investors. “The sidecar is ring-fenced from a broader set of activities that, for example, a large insurer may enter into. A sidecar usually has a tailored set of activities with oversight from a board that consists of representatives from investors," Chaudhury said. Well-defined time periods, as well as well-defined risks, can be targeted for entry and exit from a deal. Or participation may be open-ended.

Third-party investors also use sidecars to diversify the risks of their own portfolios. Exposure to the U.S. life/annuity industry can give them a source of uncorrelated risk that reduces portfolio volatility when the stock and bond markets are shaky. "Diversification is a key aspect" of sidecars for those investors, Chaudhury said.

"But not only diversification from other investments, such as corporate bonds," he added. "A sidecar can be tailored to focus on a type of liability and/or married with an asset strategy, which in total an investor might want exposure to."

Reinsurance sidecars give birth, in a sense, to new platforms for private equity/private credit dealmaking—replications of the strategy that motivated the Apollos and KKRs to get into insurance in the first place. Even if the big asset managers are committed to the life/annuity business for the long-term, "the sidecars to which they retrocede a small share of the business typically follow a traditional private equity model, in which the limited partners commit to a three- to seven-year investment horizon," according to a March 2024 report by Michael Porcelli of AM Best.

These life/annuity sidecars are best for investors with an appetite for the risks associated with investment-like annuities (deferred fixed indexed and fixed rate annuities) that private equity-led life insurers prefer to sell—as opposed to the "biometric risks" associated with annuities that guarantee "income for life."

To use a fancy term, the investors are engaging in "asset-intensive" reinsurance. They're taking the *financial* risk that the sponsoring life insurers' assets will fail to generate enough income to pay all the benefits promised on deferred fixed annuities as they come due. They're not buying the risk that the insurers' *liabilities* will spike—as they could if the insurers' actuaries underestimate the lifespans of owners of annuities that guarantee "income for life."

The road ahead

Life/annuity industry analysts think the sidecar phenomenon is just getting started.

"There is little expectation of a near-term slowdown" in this trend, AM Best analysts wrote last March, "as owners maintain a large amount of committed capital to provide to these operating entities once further deals are identified and executed."

Milliman's Chaudhury wrote, "As the spate of transactions underpinned by strategic shifts continue in the L&A [life and annuity] space, combined with the growing interest from various third-party investors and asset managers looking to enter or enhance their exposure to the L&A space, the topic of sidecars is expected to be a key consideration as part of the U.S. L&A landscape and will likely widen its influence as a topic across the global L&A insurance industry."

"Although U.S. life sidecars are in an early stage of development, they are growing fast and they are transforming," analysts at S&P Global predicted in 2023. "With the evolving competitive landscape of the U.S. life insurance sector, we expect more and more companies to assess if a sidecar fits with their core strategy. As such, we expect this growing side of the industry to garner a lot of attention in the next few years."