

EXPLANATORY MEMORANDUM TO
THE INSURANCE AND REINSURANCE UNDERTAKINGS (PRUDENTIAL
REQUIREMENTS) (TRANSITIONAL PROVISIONS AND CONSEQUENTIAL
AMENDMENTS) REGULATIONS 2024

2024 No. 594

1. Introduction

- 1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of His Majesty.

2. Declaration

- 2.1 Bim Afolami MP, the Economic Secretary to the Treasury and City Minister at HM Treasury confirms that this Explanatory Memorandum meets the required standard.
- 2.2 Emma Kavanagh, Deputy Director for the Insurance and Pensions Markets Team at HM Treasury confirms that this Explanatory Memorandum meets the required standard.

3. Contact

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Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

- 4.1 Prudential regulation ensures that insurance firms act safely, reducing the chance of them getting into financial difficulty. The matching adjustment is a mechanism that may be applied when calculating the value of insurance liabilities. The matching adjustment allows insurance firms to recognise upfront as capital part of currently unearned cashflows, and in doing so reduce the value of their liabilities. This incentivises firms to match long-term annuities with long-term assets, contributing to their overall financial stability. The matching adjustment is subject to eligibility conditions set out in legislation and the Prudential Regulation Authority's (PRA) rulebook. Approval to include an asset in a matching adjustment portfolio is granted by the PRA.
- 4.2 The Insurance and Reinsurance Undertakings (Prudential Requirements) Regulations 2023 (S.I. 2023/1347) set out a series of reforms to the functioning of the matching adjustment, widening the number of assets eligible for inclusion in matching adjustment portfolios. This will allow insurance firms to invest in a wider range of assets from 30th June 2024.
- 4.3 The transitional provisions contained within this instrument ensure that on 30th June 2024, matching adjustment approvals in force immediately before 30th June 2024, which are granted by the PRA under assimilated EU law in regulation 42 of the Solvency 2 Regulations 2015 (S.I. 2015/575), remain valid.

- 4.4 The instrument also makes amendments consequential to the revocation of provisions relating to the matching adjustment in the Solvency 2 Regulations 2015 and the Commission Delegated Regulation (EU) 2015/35 of 10th October 2014 concerning the prudential regulation of the insurance sector. Those provisions will be repealed on 30th June 2024 by section 1 of, and Schedule 1 to, the Financial Services and Markets Act 2023.

Where does the legislation extend to, and apply?

- 4.5 The extent of this instrument (that is, the jurisdictions which the instrument forms part of the law of) is England and Wales, Scotland and Northern Ireland.
- 4.6 The territorial application of this instrument (that is, where the instrument produces a practical effect) is England and Wales, Scotland and Northern Ireland.

5. Policy Context

What is being done and why?

- 5.1 From 30th June 2024, insurance firms that want to include an asset in a matching adjustment portfolio must apply to the PRA for a matching adjustment permission under section 138BA of the Financial Services and Markets Act 2000 (FSMA 2000). Section 138BA and the Financial Services and Markets Act 2000 (Disapplication or Modification of Financial Regulator Rules in Individual Cases) Regulations 2024 (S.I. 2024/539) give the PRA the power to modify or disapply its rules. A matching adjustment permission enables an insurance firm to apply the matching adjustment by means of a rules' modification under those powers.
- 5.2 This instrument provides that firms who have approval from the PRA to include assets in their matching adjustment portfolio immediately before 30th June 2024 under regulation 42 of the Solvency 2 Regulations 2015, do not have to re-apply from the point at which the new rules for the matching adjustment take effect on 30th June 2024. These new rules are set out in the Insurance and Reinsurance Undertakings (Prudential Requirements) Regulations 2023 (S.I. 2023/1347).
- 5.3 Without this instrument, re-application would take up capacity in both insurance firms and the PRA, which would likely be costly and time consuming. From 30th June 2024, firms would also lose their existing matching adjustment benefit and would not be able to utilise this until a new permission was granted by the PRA. Such reapplications would therefore have no practical benefits given firms' likelihood to be approved under the new wider regime.
- 5.4 This instrument will also make amendments consequential to the revocation of regulation 42 of the Solvency 2 Regulations 2015 and other assimilated law on the matching adjustment, to ensure that the new matching adjustment regime functions as intended.

What was the previous policy, how is this different?

- 5.5 There is no change in policy. From 30th June 2024, if a firm wishes to alter their existing matching adjustment permission or make a new application, they will still have to apply to the PRA to do this.

6. Legislative and Legal Context

How has the law changed?

- 6.1 Regulation 3 of this instrument makes a transitional provision for firms with approval to apply a matching adjustment on 30th June 2024 when the regulation under which that approval was given is revoked. It provides that firms can continue to apply the matching adjustment from this point.
- 6.2 Regulations 4-6 of this instrument amend existing legislation that refers to assimilated law on the matching adjustment that will be revoked on 30th June 2024. Existing legislation will instead refer to the new matching adjustment legislation set out in the Insurance and Reinsurance Undertakings (Prudential Requirements) Regulations 2023 and PRA rules, and to the new mechanism under which the PRA can approve a firm's application to use the matching adjustment which is section 138BA of FSMA 2000 and the Financial Services and Markets Act 2000 (Disapplication or Modification of Financial Regulator Rules in Individual Cases) Regulations 2024.

Why was this approach taken to change the law?

- 6.3 This approach makes clear that existing applications of the matching adjustment can continue, but in accordance with the legislation set out in paragraph 6.2. This is simpler than having different matching adjustment rules apply to different cases depending on when the application was made.

7. Consultation

Summary of consultation outcome and methodology

- 7.1 HM Treasury has not undertaken a formal consultation for this instrument, which maintains existing policy: ensuring existing matching adjustment approvals remain valid under the new regime as of 30th June 2024. HM Treasury has consulted with the PRA to enable the regulator to prepare for the changes to the Solvency II regime and ensure that the regulations in this instrument can work effectively with relevant regulatory rules.

8. Applicable Guidance

- 8.1 HM Treasury will not provide further guidance in relation to this instrument. It will be for the PRA to advise firms should they wish to make changes to their matching adjustment permissions from 30th June 2024.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

- 9.1 A de minimis Impact Assessment is submitted with this memorandum and published alongside the Explanatory Memorandum on legislation.gov.uk.

Impact on businesses, charities and voluntary bodies

- 9.2 There is no, or no significant, impact on business, charities or voluntary bodies as a result of this instrument. This is because transitional provisions for matching adjustment approvals mean that firms will not have to make a new application from 30th June.

- 9.3 The legislation does not impact small or micro businesses. Only firms above the threshold of writing €5 million of gross written premium are governed by these regulations. This will rise to £25 million on 31 December 2024.
- 9.4 There is no, or no significant, impact on the public sector. Only private sector insurance and reinsurance firms can apply a matching adjustment.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

- 10.1 The approach to monitoring this legislation is that HM Treasury will engage with industry and the PRA as necessary.
- 10.2 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015, Bim Afolami MP has made the following statement: A review clause would not be appropriate for this instrument. Transitional provisions provide for a one-off conversion of matching adjustment approvals, and it is neither practicable nor useful to revisit a provision of this nature. Firms seeking a variation of their matching adjustment permission from 30th June 2024 can apply to the PRA for this.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

- 11.1 None.

12. European Convention on Human Rights

- 12.1 The Economic Secretary to the Treasury and City Minister has made the following statement regarding Human Rights:
- “In my view the provisions of The Insurance and Reinsurance Undertakings (Prudential Requirements) (Transitional Provisions and Consequential Amendments) Regulations 2024 are compatible with the Convention rights.”

13. The Relevant European Union Acts

- 13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 (“relevant European Union Acts”). It does however relate to the withdrawal of the United Kingdom from the European Union because it relates to HM Treasury’s programme to deliver a Smarter Regulatory Framework for the UK through repealing assimilated law and tailoring regulation to the UK.