



CP12/15 Responses
Jack Middleton
Prudential Regulation Authority
20 Moorgate
London EC2R 6DA

15 May 2015

Dear Jack,

AFM Response to Consultation Paper CP12/15, *SIMR: a streamlined approach for non-Solvency 2 firms*

1. I am writing in response to this consultation paper, on behalf of the Association of Financial Mutuals. The objectives we seek from our response are to:
 - Respond to the consultation proposals; and
 - Highlight specific implications for our members, where we consider the consultation has not taken proper account of differences in business model.
2. The Association of Financial Mutuals (AFM) represents 50 member companies, and in most of our member companies, customers present and future are the owners of the business. Between them, mutual insurers manage the savings, pensions, protection and healthcare needs of over 30 million people in the UK and Ireland, collect annual premium income of £15.9 billion, and employ nearly 38,000 staff¹.
3. The nature of their ownership and the consequently lower prices, higher returns or better service that typically results, make mutuals accessible and attractive to consumers, and have been recognised by Parliament as worthy of continued support and promotion. In particular, FCA and PRA are required to analyse whether new rules impose any significantly different consequences for mutual businesses.

¹ ICMIF, <http://www.icmif.org/global-mutual-market-share-2013>

4. We have highlighted over a number of years, to first FSA and subsequently the PRA and FCA, the need to consider separately the regulatory requirements for firms outside the scope of Solvency 2. A number of AFM members fall into this category, and as the consultation states there are around 100 NDFs in total.
5. We are pleased to see that PRA has shown willingness to adopt an alternative approach for non-directive firms. The time remaining for implementing any significant changes to the regime for non-directives are such that it is not practical to deliver the kind of 'Solvency 2 lite' regime that was at one time proposed. In any event it has not been established that the costs, for firms or regulators, would be proportionate, or that the benefits to consumers would outweigh implementation costs- which for a mutual would be borne by policyholders. We will look to the next PRA consultation for evidence that the broader restructuring of the rulebook for non-directives takes this into account.
6. AFM recently engaged with PRA about the definition of a non-directive. Paragraph 1.3 indicates that almost all firms outside the scope of Solvency 2 have assets below £25 million and premium income below £5 million. The exception stated in paragraph 2.17 therefore seems superfluous, as it states, as does paragraph 1.3, that firms with assets over £25 million will apply the SIMR for Solvency 2 firms. In any event, the Solvency 2 rules use equivalent numbers in euros rather than sterling, as does the PRA website² (which also suggests 125 firms outside the scope of Solvency 2, not 100 as stated in the consultation).
7. EIOPA's threshold also refers to a limit based on technical provisions, which are a measure of liability not asset, and therefore has a difference intention to the definition PRA has used in the consultation paper. And given the weakness of the euro at present, the €25 million threshold corresponds to technical provisions of around £18 million, and the premium income threshold of €5 million to approximately £3.6 million. This imprecision and ambiguity in approach suggests PRA is exercising some discretion in whether to include firms in the Solvency 2 regime. Our experience of late though is that the regulator has given relatively short notice to firms that they will be expected to apply Solvency 2.
8. With regards to the specific proposals in this consultation, we agree that the policyholders of non-directive firms should also expect that their insurer is run by people with clearly defined responsibilities, and who behave with integrity, honesty and skill. We agree that for non-

² <http://www.bankofengland.co.uk/pras/Pages/supervision/smallinsurers/nondirective.aspx>

directives, streamlining the SIMR requirements helps retain this, whilst also providing a proportionate approach.

9. PRA proposes that the small insurers senior manager function (SISMF) replaces a number of existing controlled functions, and that this function could be fulfilled by a single individual. We suggest that in very small non-directives this may be appropriate, though in many we anticipate that the 'two sets of eyes' principle will mean that this is neither practical nor appropriate. In any event, with FCA's SIF regime retaining most of the roles that the PRA does not seek to approve, the overall net effect is not very different from the current regime.
10. The four prescribed responsibilities for the SISMF offer a degree of proportionality, though in reality this is a summary of the 11 prescribed responsibilities in the SIMR, excepting those areas that are not relevant to a non-directive. In any event, FCA proposes to add to these responsibilities.
11. FSA and subsequently PRA and FCA have been consulted on the likely format and impact of Solvency 2 on the UK insurance industry for more than five years. They have in particular undertaken detailed assessment of the costs of implementation for firms that are subject to the Directive. This is the first consultation in that period to be directed at insurers that will sit outside the regime, and we consider that the regulators should adopt similar principles in assessing the cost and benefits of the new regime for non-directives, even if the level of analysis is much simplified.
12. Hence, whilst we accept the generalised view in the cost benefit analysis, that the overall cost on non-directives is little greater than at present, and that the effect on mutuals is not significantly different, we would expect to see comparisons- particular in future consultations on the non-directive regime- to start from first principles of the regime for non-directives, rather than by comparison with directive firms, or indeed the SMR for deposit-takers. It is also important that each regulator does not seek to claim proportionate savings in their approach singularly, if the combined effect of each regulators requirements in total is not reduced, compared to the current regime or that of directive firms.
13. We do not agree that the approach proposed facilitates competition, or that it is 'potentially beneficial to new entrants' as stated in paragraph 4.10. It is now 20 years since the last regulated retail mutual was established, which is a clear indication that the current rules applying to small insurers do not attract new entrants.

14. We are replying separately to the FCA on the proposals in their consultation. All our consultation responses are available to download via the AFM website, and we would be happy to provide a copy of the FCA response if necessary.

15. We would be pleased to discuss further any of the issues raised by our response.

Yours sincerely,



Chief Executive
Association of Financial Mutuals