



Alivia Kratke and Alan Murray
Bank of England
Threadneedle Street
London
EC2R 8AH

31 May 2016

Dear Alivia and Alan,

AFM Response to Consultation Paper CP13/16, *Solvency 2: remuneration requirements*

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:
 - Comment on the approach taken in the consultation, and reinforce the need for a proportionate approach.
2. The Association of Financial Mutuals (AFM) represents insurance and healthcare providers that are owned by their customers, or which are established to serve a defined community (on a not for profit basis). 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 £16.4 billion, and employ nearly 30,000 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 take account of corporate diversity in discharging their regulatory principles², and to analyse whether new rules impose any significantly different consequences for mutual businesses³.
4. AFM is pleased to respond to this consultation on behalf of its members. Our members are committed to maintaining high standards of governance, and as customer-owned businesses, are acutely aware of the need to account

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

² <http://www.legislation.gov.uk/ukpga/2016/14/section/20/enacted>

³ Financial Services Act 2012, section 138 K: <http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted>

transparently for all expenditure incurred, and in particular to be transparent in relation to remuneration practice.

5. All AFM members undertake an exercise annually to assess their compliance against the UK Corporate Governance Code, as annotated for mutual insurers, which includes a section devoted to remuneration practices. This means there is broad support and acceptance of standards in this area, albeit that for many of our members, the levels of overall remuneration and variable pay are very low in comparison to other parts of the financial services industry.
6. Our 2015 report on compliance with the Code reiterated that performance-related elements of remuneration do not form a significant proportion of total pay for most mutuals⁴. We also produce a regular report on remuneration in the sector, and this provides transparent information on senior roles within our member companies, confirming the lower level of bonuses, and of overall remuneration⁵.
7. Given this, and the lower risks inherent in the business of our members, we do not consider that mutual societies present any obvious systemic risk to PRA's objectives that would be sensibly addressed by complex or punitive remuneration requirements. We consider that deferring bonuses, where base and overall pay is relatively low, would make recruiting competent staff more difficult for our members.
8. We recognise that PRA has sought both to interpret the Solvency 2 Directive requirements for the UK insurance industry, as well as to align the regime with that for banks and other deposit-takers. We found the rationale for this alignment to be inconclusive, and as a result some of the proposals are unclear and subject to different interpretations.
9. In particular, the consultation recognises proportionality requirements carried over from the Directive, and combines these with de minimus thresholds in CRD, but does not coherently address the different audiences that this creates. We would ask PRA to be a lot clearer in the next consultation or policy statement. For example, our interpretation of the text is that:
 - a. the introduction to the draft Supervisory Statement confirms the statement is relevant to all Solvency 2 insurers; but
 - b. PRA indicates later than the remuneration requirements in the consultation apply to cat 1 and 2 insurers only; and
 - c. for smaller insurers, the remuneration requirements in the Directive still apply ("PRA expects all Solvency 2 firms to comply with the remuneration requirements of Article 275"); and
 - d. for in-scope individuals, where pay is below £500,000 and bonuses less than 33% of base salary, there is an exemption from the deferral rules.

⁴ <http://www.financialmutuals.org/files/files/2015%20Corporate%20Governance%20Report.pdf>

⁵ <http://www.financialmutuals.org/files/files/Remuneration%20in%20the%20Mutual%20Sector%20Final.pdf>

10. However, the consultation is not wholly definitive in setting out this view, nor does it clearly set any expectations for firms that drop out of the proportionality, or which of the proposals are disapplied. It is the same position for individuals treated as de minimus.
11. In our assessment, AFM's Solvency 2 members need to apply the article 275 requirements only⁶, which refer to the maintenance of a remuneration policy that is appropriate to the nature, scale and complexity of the firm: this is because all our current membership falls outside cat 1 and 2. There were two individuals in SIMR roles with total remuneration above £500,000 in 2015, but as their organisation is not cat 1 or cat 2 risk, the deferral requirements in the consultation do not apply.
12. We would appreciate clarity from PRA in the final supervisory statement that their expectation is the same as we set out above. This is particularly the case as some of our members have taken a different view on what PRA's intention is.
13. Consistent with our position, we have not commented on the specific requirements in the draft statement, though we consider that the application of banking derived rules to insurance does not take account of the differences in business model, especially as they apply to short-term general and health insurances.
14. We would be pleased to discuss further any of the issues raised by our response.

Yours sincerely,



Chief Executive
Association of Financial Mutuals

⁶ <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L:2015:012:FULL&from=EN>