



Hugh Burns and Christopher Forster
Bank of England
Threadneedle Street
London EC2R 8AH

10 September 2015

Dear Hugh and Christopher,

AFM Response to Consultation Paper CP18/15, *Corporate Governance, Board responsibilities*

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 draft supervisory statement; and
 - Highlight the fit with existing arrangements for corporate governance in mutual insurers.
2. The Association of Financial Mutuals (AFM) represents 47 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.
4. AFM maintains a Corporate Governance Code annotated for mutual insurers². This is based on the UK Corporate Governance Code, with

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

² <http://www.financialmutuals.org/mutual-governance>

annotations only where they are necessary to interpret the code requirements into a mutual business model.

5. Compliance with the Code is a condition of membership of AFM; each year we undertake a rigorous compliance exercise³, and report to Treasury as well as the PRA and FCA on progress⁴. As our reports demonstrate, even the very smallest mutual insurers embrace good practice in corporate governance.
6. In our experience, the 'comply or explain' approach incorporated into FRC's Code and our annotated version, is a very effective way of facilitating proportionality: board directors aim to apply the principles in the code in a manner that is most consistent with their business model and size.
7. We have noticed in recent years increasing intervention by government in the content of the UK corporate governance code. This is intended to reinforce requirements in company law, but in the process of so doing has meant that organisations such as friendly societies- for whom company law does not apply, and whose own legislation often runs many years in arrears- are faced with applying governance rules that are not compatible with the relevant legislation or with their constitution. This is clearly unhelpful, and the PRA risks similar gold-plating of legislation by adopting a one-size fits all approach. It will be important for supervisors to exercise proper discretion in assessing how well firms meet the expectations in the draft statement.
8. That said, we find most of the proposals in the supervisory statement are entirely consistent with the principles in the UK corporate governance code. As such, they reflect issues that are already standard practice within mutual insurers. We do have some specific comments, where the narrative might be made more clear:
 - a. The statement sets expectations on individual directors of PRA- authorised firms, in addition to the responsibilities of the board as a whole. Paragraph 1.5 appears to leave an additional exposure for some delegate-based friendly societies- who often employ members as directors, where the phrasing here might be implied to suggest that directors individually carry the same responsibilities as they do collectively.

³ The questionnaire is housed on a dedicated website, which also provides a range of support and guidance to members: <http://afmgovernance.co.uk>

⁴ At the time of writing this response the 2015 report was being finalised; the 2014 report can be downloaded here:

<http://www.financialmutuals.org/files/files/2014%20Corporate%20Governance%20Report%20copy.pdf>

- b. Paragraph 1.7 indicated PRA will be influenced by the recovery and resolution strategies employed by a firm; as yet the PRA statement on this have been largely restricted to deposit-takers. Solvency 2 covers this area- at least via reverse stress testing, and it is not clear whether this statement implies a different standard/ expectation of insurers, compared to that of the Directive.
 - c. Section 3 considers culture, and in so doing assumes the main levers directors can employ are incentive-related. This seems a very narrow view on managing culture: for example, many small mutuals do not adopt performance-related pay, and adopt a consumer-centric culture.
9. We note that the consultation paper does not include a reference to the impact on mutuals. Given the very different governance arrangements there are in customer-owned firms compared to shareholder-owned, this is a surprising and unhelpful oversight. Equally, the statement recognises differences in governance approach due to nature and size, but does not consider ownership. Our own experience of operating a corporate governance code for mutuals, based on expectations of PLCs, is that some areas fit less well than others. We would wish to see this reflected in the supervisory statement to avoid the risk that PRA is deemed to be acting in an uncompetitive manner.
10. We would be pleased to discuss further any of the issues raised by our response.

Yours sincerely,



Chief Executive
Association of Financial Mutuals