Alexander Zaremba
Prudential Regulatory Authority
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20 May 2022

Dear Alexander,

AFM Response to consultation CP4/22 on regulatory fees and levies: rate proposals for 2022/23

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:

   - Highlight our concern with the sharp increase in fees in the proposals, and the consequences for AFM members and their customers.

About AFM and its members

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 £19.6 billion, and employ nearly 30,000 staff[1].

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[2] and to take account of corporate diversity[3].

[1] ICMIF, https://www.icmif.org/publications/market-insights/market-insights-uk-2016
[2] Financial Services Act 2012, section 138 K: http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted
[3] http://www.legislation.gov.uk/ukpga/2016/14/section/20/enacted

AFM comments on the proposals

4. We welcome the opportunity to respond to this consultation. We have done so in good faith, to seek a dialogue and to better understand the cost pressures that the regulator faces.

5. We previously highlighted an error in the tariff data, and were pleased that PRA was able to amend that quickly. We also note that, as of 13 May, the PRA website page was still linking to the 2021/22 Business Plan.

6. We note the 9% increase in the Annual Funding Requirement this year, though with some uncertainty about pension funding, this could increase further. The increase in the funding requirement is matched by a 7% increase in headcount within the regulator. We think the drive to recruit new staff is concerning, as it does not suggest the regulator is able to raise levels of productivity. Indeed, much like the call by the government to address excess staffing in the civil service, we are concerned that there is a complacency in PRA about hiring new staff and expecting industry to pay.

7. This is particularly so at a time when the cost-of-living crisis, rising inflation and higher interest rates, as well as an expected increase in claims and lapses, are already providing a substantial pressure on costs for firms. For mutuals in particular, higher regulatory costs can only be paid for by raising prices, or reducing benefits/ service to customers.

8. Sadly, the inexorable rise in the cost of regulation is not matched by the number of fee payers. The limited capacity of the insurer start up unit to establish a viable basis for creating new insurers means that, as existing insurers exit the market, consumer choice becomes constrained, and the level of competition falls. It appears the unit has overseen the launch of only a handful of new insurers in four years, and we are concerned that the PRA business plan appears to suggest that more funding is devoted to the start up unit. Iit would be useful to know how PRA will remove barriers to the creation of new insurers- particularly for new mutuals.

9. In our response to last year's fees consultation, which posted an even more eye-watering increase in fees for general insurers of 13%, we summarised that rapid increases in the fees, coupled with a reduction in the number of firms regulated, meant that on average each fee payer was paying 36% more to PRA than they had in 2016. This year's consultation shows a further reduction in insurance fee payers, meaning that on average now each fee payer is paying close to 50% more than

six years ago. We consider this would be unsustainable in any commercial business, and in relation to PRA's 'have regard to' issues, we consider the proposals will:

a. reduce the competitiveness/ attraction of the UK as a place to do business;
b. make it more difficult for small mutuals to thrive and survive;
c. stifle growth and add to the already significant bureaucracy firms face; and
d. curb innovation, by failing to create an environment by which new entrants can enter the market.

10. In response to our query on the impact of higher fees on mutuals in 2021/22, in its Policy Statement PRA confirmed: "The PRA does not consider that the increase in fees is disproportionate for insurers or mutuals in general, but will continue to consider the impact of fees on different sectors." We would appreciate clarity on any action taken by PRA to support this commitment.

11. PRA also promised that they would "continue to review the methodology it uses in allocating costs to fee blocks, with a view to consulting on any changes in the future." We would value an account of what action PRA has taken over the last 12 months to achieve this, given that a range of techniques have been in use across industry for many decades.

12. As we also suggested last year, there is no evidence provided in the annual report or business plan of the extra activity that will be undertaken across insurance to warrant the increase. The PRA would do well to remember that it is the Royal Mint that has a license to print money, not itself.

13. We would welcome the opportunity to discuss further the issues raised by our response.

Yours sincerely,

Martin Shaw
Chief Executive
Association of Financial Mutuals