

Alexander Zaremba
Prudential Regulation Authority
20 Moorgate
London
EC2R 6DA
January 2019

Dear Alexander,

AFM Response to PRA CP28/18, Regulatory fees and levies, 2019/20

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 proposals as they affect AFM members; and
 - Put forward a potential fairer and more proportionate approach to the proposals on weightings applied to life insurers.
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 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 businesses² and to take account of corporate diversity³.

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>

4. We agree with the proposal to better align the fees paid by insurers with the level of risk posed to PRA's objectives, as well as the quantity of work expended by supervisors and policy teams on them.
5. We responded in detail to CP16/17 and expressed concerns that the proposals would result in a significant increase in the fees of some of our members, which was not justified by the work being undertaken by PRA or the risk presented⁴. Those proposals were based on changes to the weighting of premiums and liabilities and we considered the weightings proposed at the time were not sufficiently tested.
6. We were pleased therefore that PRA agreed to revisit its proposals. We agree with PRA that there is scope within the fee structure to better reflect the potential risk provided by different businesses. There are many ways of doing this: for example, for new businesses, the extra work in authorisation is covered in special fees; for larger firms by scaling fees to size; whilst for long-established businesses- particularly closed life books- risks can often materialise within the back book.
7. Altering the weightings between premiums and liabilities in fee calculations is therefore a relatively simple but valid way of adjusting the fee. We agree with PRA that there is no obvious merit in adjusting weightings for general insurers. We also agree that the significant number of life offices writing little new business, but which hold sizeable liabilities, means that current fees may not reflect the risks those businesses present to PRA's objectives.
8. The new proposal for traditional life companies in this consultation is to move from a weighting of 75% premiums and 25% liabilities, to 60:40 respectively (this compares to a weighting proposed in CP16/17 of 50:50). This will dampen the effect of changes in fees compared to the proposals last year, but it is disappointing that PRA has not presented evidence to support why 60:40 is a better ratio than 75:25, or anywhere in-between. For example, in what way does PRA allocate extra supervisory time to life companies with larger liabilities? How does that correlate to Cat 4 and 5 firms, who receive little or no direct supervisory attention?
9. To illustrate, given two friendly societies with GWP income of £10 million, one with BEL liabilities of £50 million and the second with BEL of £200 million, the first would pay PRA fees in 2019/20 of £2,670, and the second £4,620, or 73% more (as per the figures provided in

⁴<http://www.financialmutuals.org/files/files/AFM%20response%20to%20consultation%20on%20PRA%20fees%20and%20levies.pdf>

paragraph 2.13). This compares to a current uplift of 40% based on size. It would be helpful if PRA had quantified how much extra work it currently undertakes therefore, as intuitively and based on our experience of supporting smaller insurers, the differences are not apparent, and certainly not to the degree of 73% higher fee.

10. We conclude that whilst a significant change in weighting may be apparent for larger, high risk insurers (eg Cat 1, 2 and 3 insurers), it is not proven for smaller, lower risk insurers (cat 4 and 5). We therefore suggest that unless PRA has evidence to support the change, it retains the current weightings for cat 4 and 5 firms, which already impose a significantly higher fee level for firms with a large back book (as per the example in paragraph 9 above).
11. Similarly, for the proposals for unit-linked business, whilst we accept that there is generally a lower underwriting risk compared to with-profits (though other risks might be greater), we would like PRA to have set out evidence of how it has quantified that unit-linked business should be weighted 0.65 times that of with-profits.
12. With regard to the proposals in chapter 3 for fees for part VII transfers, we consider the fees should be set at a level that reflects the amount of work undertaken by PRA. There may be exceptions, where PRA has encouraged a white knight to transfer in some or all of the business of a very small organisation, and where a fee of £20,000 may (with all the other attendant costs) make the transfer unattractive. We welcome PRA's thoughts on this in their Policy Statement.
13. We are responding separately to the FCA on their proposals to changes fee weightings for life companies.
14. We would welcome the opportunity to discuss further the issues raised by our response.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'MS' followed by a stylized flourish.

Martin Shaw
Chief Executive
Association of Financial Mutuals