



Department for
Business & Trade

SMARTER REGULATION AND THE REGULATORY LANDSCAPE:

CALL FOR EVIDENCE

This call for evidence closes 11:59pm on 7 January 2024

RESPONSE PROVIDED BY THE ASSOCIATION OF FINANCIAL MUTUALS,
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Section One: Questions on the Landscape of Regulation (Required)

Question 1: Based on your experience, do you think that UK regulators are supportive of the individual businesses they regulate in a way that appropriately balances considerations of consumers and other businesses within the sector more broadly?

Being a regulator is a bit like being a football referee. Some decisions you make are welcomed on one side, others by the opposition. The key challenge is to demonstrate fairness and a capacity to understand both sides, as well as to have a process to ensure decisions are properly informed and that there is an opportunity to review decisions and address errors.

In our experiences within financial services, the PRA and FCA are increasingly delivering on this. There is a strong commitment to regulating appropriately, and increasing investment in well-informed staff to execute their approach well.

Question 2: Please name the UK regulator(s) you engage with most frequently:

Please specify here: Prudential Regulatory Authority and Financial Conduct Authority.

We also speak regularly to a number of other financial services regulators: the Financial Ombudsman, FS Compensation Scheme and Financial Reporting Council.

Question 3: What do you consider to be the most positive and/or negative aspect of how the UK regulators that you engage with operate?

Both PRA and FCA have a very clear operating remit. They invest significant time in working with each other and respecting their specific boundaries.

We have two to three liaison meetings each year with PRA and FCA, and meet them on regular occasions in-between to discuss specific topics. They are showing an increasing effort to engage and better understand our sector; for example, earlier this year we delivered presentation to FCA staff on the sector we represent, and ran the session again with PRA personnel. Both PRA and FCA sent senior speakers to our 2023 conference, and this enabled them to engage directly with firms across our sector.

PRA and FCA also both follow clear rules for formal consultation with industry. This includes the production of a cost benefit analysis, though in the past this has provided imprecise estimates, and we look forward to the influence that the new government-mandated CBA panels will have on their work.

In relative terms, we find the PRA is more approachable than FCA. This is partly because of the smaller number of firms they regulate, but it is undoubtedly true that the operating structure of the FCA means its staff have little practical knowledge of the particular needs of smaller insurers. In particular, when LV= sought to demutualise in 2021, FCA provided regulatory approval for the sale of LV=, without an appreciation of the impact this would have on members of that business.



In 2016, in an update to the Financial Services and Markets Act, the government introduced a clause on corporate diversity, to ensure PRA and FCA took greater account of the impact of regulation on mutuals and similar organisations, across all their activities, not just at the time they consult. We have seen limited evidence of this, and certainly no effort to account for the work they undertake on corporate diversity.



Section Two: Complexity and Ease of Understanding the Regulatory System

Question 4: Based on your experience or understanding of UK regulators, do you find it clear what the overall purpose and objectives of individual regulators are?

We are content that the legislative framework for both PRA and FCA sets out very clear their respective purpose and responsibilities.

This works effectively, though we have seen instances of slow and ineffective hand-offs between the regulators, or duplication of costs. For example, the authorisation process regularly involves a firm seeking approval for an individual from both regulators, and this makes the process lengthy and problematic.

For a recent consultation on Diversity and Inclusion, both PRA and FCA concluded they needed to issue separate consultations, despite the heavy overlap of content. The dual approach has also meant that the projected costs of implementing new rules for both regulators will be around £1.7 billion over three years, which is unreasonable, and is not matched by a coherent set of benefits.

Question 5: Within these overall objectives (as considered in the preceding question), do you find it clear what the specific statutory duties (i.e required by legislation) of individual UK regulators are?

Regulators set out many of these duties in the consultation process, which helps to reinforce how they operate against clear objectives.

Both PRA and FCA are required to issue a Cost Benefit Case as part of the consultation process. However, the legislation does not require them to do so when setting regulatory fees, and as a result we see a much less clear justification of costs or rationale for the work proposed.

Question 6: Do you think that the statutory duties (i.e required by legislation) imposed on UK regulators:

1. Cover the right issues?
2. Are clearly stated in relevant statute, including where supplemented by relevant guidance?; and
3. Are sufficiently consistent across regulators, where this is relevant?

We are content. Regular reviews of the legislation have helped; for example, the FSMA 2023 brought new responsibilities for PRA and FCA to take account of competitiveness and growth. This has provided a welcome change in thinking. We also seen the intervention by the Department for Business and Trade to intervene to withdraw planned legislation via the Companies (Strategic Report and Directors' Report)(Amendment) Regulations, as a firm warning to regulators to take better account of costs and bureaucracy and to deliver more proportionate regulation.



Question 7: As set out above, UK regulators have a remit that is set through legislation and guidance. Which of the below do you consider best applies?

1. Regulators always act within the scope of their remit;
2. Regulators go beyond their remit in a way that may negatively impact the outcomes that they are required to deliver; or
3. Regulators go beyond their remit in a way that supports the outcomes they are required to deliver

In our experience:

Regulators always act within the scope of their remit

Question 8: Do you often have to engage multiple UK regulators on the same issue or area?

1. Yes
2. No

Yes. There is a degree of overlap between the PRA and FCA, which is mostly unavoidable and welcome. However, as mentioned above, it can also add significant costs and delays.

Question 9: Do you consider that UK regulators collaborate effectively with each other and their international counterparts?

We see plenty of evidence of effective engagement between UK regulators.

It is less clear how UK regulators collaborate with international counterparts since the UK left the EU. Prior to that, for insurance, there was regular and effective dialogue on a broad range of issues.

Question 10: Where you engage with multiple UK regulators, do you find it clear which regulator is responsible for a specific issue or area, and how regulator mandates interact?

Yes; in addition to comments above, the Memoranda of Understanding provide an effective basis for engagement between regulators.

Question 11: Do you consider there to be underregulated areas of the economy, or gaps in regulatory responsibility between UK regulators?



We are pleased that FCA has recently extended its responsibilities to include funeral planners, claims management companies and cryptocurrency providers. We consider there are still some potential gaps in the regulation of AI and machine learning.

Question 12: Do you consider that guidance issued by UK regulatory bodies makes the regulatory system clearer and easier to understand?

We do. We regularly respond to consultations from regulators, and one of the main themes we comment on are the unintended consequences of new rules on mutual organisations. We consider this has reduced over time, though we would like to see more focus on: a) proportionality, and b) corporate diversity.



Section Three: Regulator Agility, Responsiveness and Skills

Question 13: Do you find UK regulators to be agile and responsive to new and emerging issues?

We see UK regulators as striving to keep up with developments in the market; especially in relation to artificial intelligence. PRA and FCA both do have projects underway but the pace of change is slow and currently both regulators appear to believe they have all the rules needed to regulate these new forms of business.

During the early stages of the pandemic, PRA and FCA both made helpful and timely changes of approach that gave firms certainty and support in operating under exceptional conditions.

The review of Solvency 2 has proven more lengthy than expected; indeed, it is seemingly taking as long in the UK to deliver changes, than it is in the EU who are exploring similar amendments. For some time there appeared to be disagreement between HM Treasury and the PRA on the scope of changes, and this affected the capacity to deliver meaningful changes for the end of 2023, as originally envisaged.

We would like to see the FCA respond more quickly to emerging trends and problems. In the past, a reluctance to do so has resulted in the Financial Ombudsman Service (FOS) having to deal with an enormous caseload, on a case-by-case basis, rather than for the FCA to take responsibility for resolving issues on a class basis. This makes it much more difficult for firms to predict the right course of action, where FOS is outside the formal regulatory remit and its decisions are made on an individual basis without consideration of the wider environment or legal precedent.

Question 14: What factors do you think work for and against UK regulators' ability to respond sufficiently rapidly?

The clear remit of individual regulators is an enabler for rapid and effective action.

The regular hand-offs between independent regulators, and between them and Government can cause delay.

Question 15: Do you consider the processes that UK regulators have in place allow them to make decisions in an appropriate time frame?

In our experience, the regulatory processes in place enable timely decision-making.

Question 16: In the sector(s) that you operate in, do you think there are specific improvements that UK regulators and / or the Government could make to facilitate a more agile implementation of rules and regulations?



As highlighted above, the FOS operates outside general regulatory standards. If they were made a formal sub-division of the FCA we consider this would improve coordination and the effective implementation of standards.

For example, in July 2023 FCA's rules on the Consumer Duty came into effect. However, firms are uncertain how FOS will interpret the standards set down, and this may only emerge over a considerable period. In the past, this undercertainty has fuelled the development of claims management companies.

Question 17: Do you think UK regulators have the appropriate mix of skills to deliver their objectives?

On the whole yes. The FCA has in particular seen very high levels of turnover, and has not always sought to replace people with specialist knowledge of the industry.

Question 18: Do you think UK regulators are appropriately resourced to discharge their duties?

The workforce in the PRA appears to have plateau'd in recent times, and they have set themselves the challenge of growing efficiency. We consider this is right and are concerned at the rapid increases in staff employed by FCA.

Question 19: Do you think existing processes enable UK regulators to test new regulatory reform proposals?

Yes: in financial services, where regulators are exploring more substantive changes or debating the application of regulation into new areas, they will generally issue a Discussion Paper or Call for Evidence at an early stage, which avoids the development of rules too early in the process and before the range of options has been considered. This is followed by a formal consultation as and when there is a clear scope for new rules.

The FCA's new Consumer Duty followed this process well, and as a result provided a coherent set of principles and cross-cutting rules, and also parked issues that would have undermined support for the general principles (including a 'Private Right of Action', which we were particularly concerned about).



Section Four: Proportionality in Implementing Regulation

Question 20: Do you consider UK regulators to be proportionate in the measures they take, e.g. in applying regulations or responding to emerging issues?

In our experience, there is a growing appreciation of proportionality. In financial services, both PRA and FCA reference their commitment to this. However, we consider that reforms that deliver better proportionality are often slow to emerge, as regulators prioritise issues that have the greatest potential impact. For example, where regulators are focusing effort on increasing competitiveness of UK financial services, e.g. through the reform of Solvency 2, they are prioritising work that will simplify the regime to issues that will make large insurers more profitable, in the expectation that this could release sums for infrastructure projects into the economy, as per government policy. In so doing however, they are delaying much needed reform for small firms, and ironically therefore run the risk of reducing UK competition by potentially forcing small, but otherwise viable, firms out of business.

Question 21: In making decisions that involve risk, which of the below do you consider most accurate?

1. UK regulators are too risk averse in their decision making
2. UK regulators achieve the right balance of risk in their decision making
3. UK regulators allow for too much risk in their decision making

Most of the time regulators consider the balance well, or respond to industry feedback constructively. For example, in the early stages of developing the Consumer Duty, FCA has proposed a Private Right of Action, but withdrew this in response to strong industry concerns.

We do see occasions however where regulators impose very high costs/ burdens on firms, without quantifying the benefits that will result, and without considering whether a more cost effective solution might achieve similar aims.

Question 22: Do you consider that individual UK regulators have the appropriate level of discretion when taking decisions that involve risk?

In our experience, UK regulators work well within the legislation that is in place. We have seen tensions of late, as a result of the absence of work on the Friendly Societies Act, which has not been modified since 1992. This places friendly societies at an operational and commercial disadvantage, but it also creates problems for regulators in having to maintain policies and procedures an policy which are more onerous than those for firms covered by the Companies Act.

Question 23: If you are a business or consumer, how does the approach that UK regulators take to risk impact your own decision-making?



We invest significant time and effort commenting on consultations for new rules, and in helping our members interpret rules and in establishing how best to implement them.

Question 24: UK regulators often need to balance delivery across a range of different legislative duties or regulatory requirements, some of which may involve trade-offs. Do you consider that they balance these trade-offs effectively and transparently?

We do.

Question 25: If you are a UK regulator, are there specific areas where you consider it would be beneficial to seek further steer or guidance from the Government?

N/A

Question 26: In general, do you consider the approach that UK regulators take to requests for information to be proportionate to any burden they may impose on you?

1. Yes
2. No
3. N/A

Question 27: Do you ever receive duplicative requests for information from the same or multiple UK regulators? (i.e., requests asking for essentially the same information)?

1. Yes
2. No
3. N/A



Section Five: Process and Governance

Question 28: Do you consider that UK regulators have in place the right governance structures to deliver the best outcomes? If not, how can they be improved?

The recent introduction by PRA and FCA of CBA Panels will improve transparency and accountability on the costs/ benefits of new proposals. This is welcome.

Question 29: Do you consider that UK regulators use digital systems in their interactions with you in an efficient fashion? (e.g. data transfer or other digitised methods)?

Financial regulators have enhanced systems in recent years, and we are not aware of any operational shortcomings.

Question 30: Do UK regulators sufficiently communicate the processes they follow to make decisions?

1. Yes
2. No
3. N/A

Question 31: Are you provided sufficient opportunity to input into decision making by UK regulators processes (e.g., via consultations, workshops etc)? If not, how would you suggest improving the process?

We actively review all relevant consultations. At times we see these refer to prior engagements with industry, and note that as a small trade body we are inconsistently invited to participate in these. As a result, we often face an uphill struggle to change regulators' minds after they have consulted and where they are reluctant to make substantive change.

Question 32: Do you consider the processes that UK regulators follow deliver reasonable outcomes?

Mostly.

Question 33: Do you think UK regulators treat those that they regulate consistently?

Inevitably the greater focus is on large businesses, where the risk are greater. This can lead to attempts to fit rules made for banks into other businesses, and sometimes this leads to an imperfect set of requirements. For example, the Senior Manager and Certification Regime, created



in response to the banking crisis in 2008, requires other businesses to develop roles which may be costly and less relevant to their business model.

Question 34: As a business, do you think the process to challenge a UK regulator you interact with is sufficiently clear, robust and fair?

We do.

Question 35: What steps, if any, do you think could be taken to further improve the effectiveness and clarity of the reviews and appeals processes?

Greater attention to post-implementation review of new rules would help demonstrate the approach taken yielded measurable benefits and that the costs to industry were proportionate with that.



Section Six: Regulator Performance

Question 36: In your experience, have UK regulators that you interact with delivered on their stated objectives in that interaction?

Yes.

Question 37: Do you think UK regulator performance reporting is proportionate, objective and transparent?

We would like to see a more expansive account of the work the regulators do. For example, how they have delivered their responsibility for avoiding barriers to corporate diversity, and how the allocation of funds they budgeted for has been matched by the allocation of resources in the following year's business plan.

For example, following rapid increases in fees to insurers in recent years, the sector is on trajectory to pay more fees to FCA than the banking sector does. This does not appear to be consistent with the amount of work devoted to insurers, who are reducing in number; hence, the lack of transparency on how the budget was spent means it is not possible to verify that fee rate increases are commensurate with the way resources have been allocated.

In relation to corporate diversity, we find most of the regulatory rules have been written with a single business model in mind (the PLC model), and this places mutually-owned businesses at a competitive disadvantage, either because the rules require them to act like a PLC would, or because the rules do not lend themselves to mutual businesses, or because there is limited proportionality adopted so that compliance costs have a high base.

Question 38: Do you think UK regulators report on the right set of criteria and metrics to monitor their performance and ensure accountability?

See response to Q37.



Section Seven: Concluding Questions (Required)

Question 39: If you could suggest a single reform to improve how UK regulators operate, what would it be?

That all regulators are tasked with giving a true and accurate account of the costs of regulation to business, and that they more effectively quantify the benefits that their rules deliver to society, including the actions they are taking to reduce bureaucracy.

Question 40: Are there any examples of international approaches to regulation that you think set best practice that UK regulators could learn from?

Members of AFM tend only to operate in the UK, and so we have limited practical knowledge of regulation outside the UK. Our experience of UK regulators, in financial services at least, is that they aim to be progressive and imaginative, and that they are focused on the optimum position for the UK economy.

The post-Brexit transition to UK based rulebooks in financial services has progressed more slowly than we would have hoped, and this has meant that changes intended to make the UK economy more competitive are taking longer to achieve. For example, the review of Solvency 2 is a combination of transposing rules and considering amendments, and the progress by the PRA has been slowed by the combination of the two, and the need to wait for (often delayed) legislation to gain the relevant powers. As a result the UK reform progress is not happening more quickly than changes in Europe, and some of the proposals are less ambitious than those achieved by EIOPA.

Whilst other jurisdictions, such as Singapore, have a highly regarded financial services regulatory structure, we are not convinced that importing standards from elsewhere will lead to demonstrably better approaches.

Question 41: What is the best designed regulation you face, and why?

In 2018 Association of Financial Mutuals (i.e. 'we'), launched a revised 'AFM Corporate Governance Code'. This is self-regulation as opposed to statutory, but is designed to take account of good practice on corporate governance elsewhere, including FRC's 'UK Corporate Governance Code', the Companies Act (especially s.172), and PRA's 'Board responsibilities'. It also seeks to interpret this good practice to best fit the various business models of our members, and seek to deliver it via a series of high-level principles. Members are required to account for how they have adopted the principles in their report and accounts, on an 'apply and explain' basis, which encourages them to be expansive on their approach to good governance, and good outcomes for their key stakeholders.



Question 42: Are there any further points you would raise about regulation, including the functioning of the regulatory system or any recommendations you have on the stock of regulations from the Government which should be removed or reformed and modernised?

We support government's drive to reduce bureaucracy on firms, and encourage further development of this theme, where it might reduce unnecessary costs and provide stronger protection to consumers.



Section Eight: Closing Questions (Required)

Question 43: In what capacity do you interact with UK regulators or regulated businesses? (Please select the most appropriate option that represents you, and respond according to your primary responsibilities)

- Regulated entity (i.e. business)
- Consumer
- Regulator
- Academic or think tank
- Other

If you selected other, please specify here: TRADE ASSOCIATION

Question 44: If you are a business, how many employees do you have?

- 1 – 9 employees

However, our response is provided on behalf of all our members, who between them have a workforce of around 6,000.

Question 45: Please name the Sector(s) that you operate in - you may wish to reference [Standard Industrial Classifications](#)

Financial and Insurance activities

Question 46: If you are a regulated business, how much as a percentage of turnover does demonstrating compliance with regulation cost your business?

- Not Applicable

However, we are responding on behalf of all our members and we estimate that regulatory costs currently amount to:

- More than 5% and up to 10% of turnover



Costs to our members include:

- Direct levies from PRA, FCA, FRC, FSCS and FOS
- Staff employed to maintain compliance of regulatory standards
- PRA and FCA's Senior Manager and Certification Regime
- Incremental training costs for employees to meet regulatory rules
- Implementation cost for new rules: e.g. the FCA's Consumer Duty, finalised in 2023, was estimated to have implementation costs for all regulated firms of £2.4 billion, whilst the proposals for PRA and FCA on Diversity and Inclusion rules are estimated by the regulators to cost industry £1.7 billion
- Additional external costs: for example, the external audit costs associated with a small insurer being classified as a Public Interest Entity have been calculated at £33 per policyholder a year

If possible, please provide more specific figures on the cost of compliance with regulation here. Compliance costs may for example include costs of staff responsible for engaging with regulators, responding to requests for information and demonstrating compliance.

Compliance costs may for example include costs of staff responsible for engaging with regulators, responding to requests for information and demonstrating compliance to the regulator. It is these costs we are concerned with, rather than the costs of delivering the policy intent of the regulation.

Question 47: What is your name, or the name of your organisation?

Martin Shaw

Association of Financial Mutuals

Question 48: What is your e-mail address (optional response)?

martin@financialmutuals.org

Question 49: We usually publish a summary of all responses, but sometimes we are asked to publish the individual responses too. Would you be happy for your response to be published in full?

- Yes