HOUSE OF LORDS

# Industry and Regulators Committee

## Corrected oral evidence: Commercial insurance and reinsurance regulation

Tuesday 8 March 2022

10.35 am

Watch the meeting

Members present: Lord Hollick (The Chair); Lord Blackwell; Baroness Bowles of Berkhamsted; Lord Burns, Lord Cromwell; Baroness Donaghy; Lord Reay; Lord Sharkey; Lord Trefgarne.

Evidence Session No. 4 Heard in Public Questions 43 - 54

### Witnesses

I: Sam Woods, Deputy Governor for Prudential Regulation and CEO, Prudential Regulation Authority; Anna Sweeney, Executive Director of Risk, Operations, and General Insurance, Prudential Regulation Authority.

USE OF THE TRANSCRIPT

1. This is a corrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.
2. Any public use of, or reference to, the contents should make clear that neither Members nor witnesses have had the opportunity to correct the record. If in doubt as to the propriety of using the transcript, please contact the Clerk of the Committee.
3. Members and witnesses are asked to send corrections to the Clerk of the Committee within 14 days of receipt.

# Examination of witnesses

Sam Woods and Anna Sweeney.

Q43 **The Chair:** Good morning and welcome to this meeting of the Industry and Regulators Committee on commercial insurance and reinsurance. It is a particular pleasure to welcome Sam Woods and Anna Sweeney here today. Sam is the chief executive officer of the Prudential Regulation Authority and has an illustrious background in regulation and all matters financial. Anna Sweeney is the executive director of risk operations and general insurance at the Prudential Regulation Authority and also has an illustrious background in that area. Welcome.

I wonder if we could start off with some rather more topical questions and then come to the main topic of our inquiry. What is your reaction to, and what are your concerns and issues about, the implementation of the Government's requirement, announced two or so days ago, that the insurance market should no longer transact with Russia on any new business? It would also be interesting to hear your thoughts on how existing business contracts might be dealt with. I think it was mentioned that initially we were talking about aircraft and space, but marine has been added to that list now, and I suspect the intention is that it should cover all insurance matters and all reinsurance matters, with Russia. Sam Woods, I wonder if you could give us your thoughts.

***Sam Woods:*** Thank you, Lord Hollick, and thank you for having us to the committee. It is a great pleasure to be here. Maybe I can begin on the sanctions more broadly and then turn to Anna Sweeney to bring in the insurance piece.

We, like almost everyone else, are absolutely appalled by the events going on in Ukraine. Over the last two weeks, we have seen it as an important part of our role to be providing technical support to the Government as they decide what the UK's response to those events should be. As it has turned out, the response has very much been heavy financial sanctions in which we are quite closely involved. Our role is to liaise with the Government, firms and other regulators to try to investigate exactly the kinds of issues you just mentioned so that these things can be done in an informed way.

Sanctions began more on the banking side. We had the removal of Russian banks from SWIFT. We had the sanctioning of several banks. We also had in particular the prohibition on dealings with the central Bank of Russia, which was a big step. That was quite a powerful package, very closely co-ordinated with the EU and the US in particular. As you say, we are now coming over to the insurance side, which Anna has been heavily involved in. The only caution I would give, if that is okay, is that this is government policy, which we are supporting. I think we should probably go as far as the Government have so far but perhaps not too much further. I will bring Anna Sweeney in now.

***Anna Sweeney:*** As Sam Woods says, our role has been to provide technical support to the Treasury and other government departments in these discussions, and we have been doing that over the last week or so on the insurance side, in particular in relation to sanctions for the airline, aircraft and space industries. When those sanctions come in, they will apply to aircraft that are Russian-owned, or predominantly for use in Russia. They will also apply to parts that are destined for use in Russia.

You asked about the distinction between new business and existing business. The sanctions are intended to apply to all payments that are related to existing business as well as new contracts. It would be a ban on new contracts but would also apply to payment in relation to claims, for example, for any existing contracts.

**The Chair:** Would that render the existing contract null and void?

***Anna Sweeney:*** Insurers and reinsurers would not be able to pay out on those contracts.

**The Chair:** So the process would be to inform the owners, the companies that have taken out the insurance, that they are no longer insured. For marine insurance that would become available in a register so that ports and other parties that might be interested in using those vessels would be aware that they are no longer insured.

***Sam Woods:*** The theme here is the same across all the sanctions. The intention is in effect to cut off significant parts of the Russian financial system from our financial system, and it will have just the effect that you describe.

It is quite a scramble, of course, to implement these things, and if the Government choose to go further on insurance, which we do not have insight into, there will be those implementation questions to look at. The one reassurance that I could perhaps give the committee, perhaps at the risk of taking a bit of a risk, is this. We have looked very carefully at whether we think these measures are manageable in terms of any collateral damage or impact on the UK financial services sector, and so far we are comfortable that they are.

Perhaps one other point to make is that the biggest economic connection, which goes a bit to your point about marine, is on energy. It is a question for the Government; it is not our responsibility. But if they do something there, that might lead to more action for us.

Q44 **The Chair:** Thank you for that. I wonder if we can go back to our main inquiry. Many of the witnesses we have heard from who are in the industry have expressed frustration at the granularity and high level of bureaucracy that the regulators impose on them. One comment was that you would almost be interested in the colour of people’s socks. Leaving that aside, there seems to be quite a high level of frustration around this, which I am sure you will be familiar with. I would be interested to hear from you, knowing that that is how your regulation is perceived, what steps have you taken to change the style of regulation, or not.

Secondly and rather more broadly, when you do your own 360-degree review—we will come later to who you report to in that sense—what criteria do you use to measure your success, or lack of success, during the year so that you can be responsive and be seen to be responsive to some of these concerns?

***Sam Woods:*** Thank you very much. First, I can confirm that the colour of your socks is not a matter for regulatory attention.

We have read a lot of the views that you have heard, and indeed we hear those views ourselves. I will also give you some views, but I wonder if it might also be useful to give you a sense of how much resource we have in this market, because that is fact and you can form your own view on it.

The easiest way to describe it is that we have a front-line supervisory division for the London Market with about 40 people working in it. We have another division of general insurance actuaries who support that work. There are about 35 of them. Probably about half their time is spent on the London Market. You could think that we have 50 to 60 people from the prudential end involved in the day to day supervision of this market. To put that figure into context, the broad definition of the London Market is gross written premium annually of about £110 billion. There is also a narrow definition, which is more in the £70 billion or so. The levy that we impose on the sector, which covers the cost of all those people and any other overheads, is £12.7 million at the moment, which is 0.012% of the amount of premium that is coming in.

Another way to contextualise it is to compare it to what we do elsewhere. Our very largest supervision teams in the PRA are for our biggest banks. For our biggest banks, we have a team of about 20 on a single bank. You can compare that to the 40 that we have in the front-line supervision team for the London Market.

Maybe another way into it is to go to an individual firm. I know you had evidence from Robert Childs of Hiscox, for whom I have great respect. The supervision of Hiscox is carried out within a team of three, which has to cover a number of firms. The allocated supervisory resource to Hiscox is 0.75 of an FTE. I judge from Mr Childs' comments that that FTE is very busy. I have checked, and last year we had 32 meetings with Hiscox—it was all virtual, so there are some definitional issues, but we had what we define as a meeting—so roughly one every other week, I guess. To me, that seems appropriate. It is a big company. It is an important company. Its revenues have doubled over the last decade.

That is how many we have. As to whether that is the right number, I think we are quite lean, and we try to be quite lean and not to ask for things that we do not need. There is, however, the regulatory side of this, and the reporting on that side, where we are having some thoughts about how to take things forward.

I have other things to say but at the risk of going on too long, so perhaps I should pass to Anna.

***Anna Sweeney:*** We ask for information in two different ways. One is the formal regulatory returns, and we have already taken steps as part of the post-Brexit Solvency II review. We are doing that in two phases. We think we have taken out about 15% of that reporting already, and we are coming on to a second phase. Importantly for this market, we have already decided to reduce the reporting for pure reinsurance-only branches, in particular in relation to the capital requirements, which we do not think make sense and which were an integral part of Solvency II but we now have the freedom to remove.

The second type of request that I am sure Robert Childs was talking about was the sort of ad hoc request from the supervisors. There is a regular schedule of what we look for, which we send to the board each year to reconfirm what it looks like. Then there will be ad hoc requests. On sanctions, for example, we might talk to some of the bigger firms to make sure that we understand the impact.

We try very hard to keep those informal requests proportionate and we are always open to a discussion about the best route for them. I know that Robert Childs mentioned some issues with getting copies of their board reports, but that is an example of where we try to use something that they do for themselves rather than ask them to do something directly for us. We try to keep a balance in these things, and we are always happy to have individual discussions with firms about the smartest way to get the information that we want.

**The Chair:** Do you have meetings during the year, or one meeting a year, where you meet representatives from the companies and address these sorts of concerns?

***Sam Woods:*** Maybe I can start on that and also pick up your point about measures.

We have meetings up and down the companies, if you like. It is quite important that the people at the top of these companies are willing to interface with the supervision teams talking to them every day, but we also have meetings at the more senior levels. I have a fixed schedule of meetings with the chairs and chief executives of the largest firms. Anna will have similar meetings with the firms that she oversees. We also have a more formal way of getting feedback from firms. We have a survey that we send them annually to give us feedback on what they think about us. You can immediately see the potential issue with such a survey, but the trend is worth noting. Whatever the noise in the signal at the level, whether things are moving around is worth watching and we do pay close attention to that.

**The Chair:** What has the trend been over the last five years?

***Sam Woods:*** It has been flat. I do not know whether that is good or bad. The level of frustration seems to have been consistent, but the one area that I would pick out is the consistently lower score for how well firms think we co-ordinate with the FCA, so we have put extra attention into that recently. In particular, following lots of quite well-founded points made by the industry, we have come up with this thing called the regulatory initiatives grid, where we and the FCA, and the other main regulators that might touch financial services, are now putting down publicly every six months, "Here is everything that we are up to". Even the process of doing that and creating that picture allows us to look at whether it makes sense in the round. That is one concrete thing that we have done lately.

**The Chair:** What other metrics might you use in your own 360-degree analysis each year?

***Sam Woods:*** I mainly have two. They are very crude, and given the focus of this committee I hope this is a topic that we can develop further.

The bottom line of where our objectives lead us to is an absence of messy failures. That does not mean an absence of firm failures; it is good to have firms coming in and out of the market, and we have that—we have a lot of work going on in winding down firms in quiet ways, which is a good thing to do. But a messy failure, or one where a lot of policyholders lose a lot of their savings, is what we are trying to avoid.

The other measure goes back to the point about efficiency. We have to have an eye to how much it costs to have us. At the moment, we have about 1,340 FTEs within the PRA. The number of individuals is slightly higher because we have some part-time staff. We have a levy of £292 million, and I think we can do the job with that. International comparisons, particularly on the banking side, show that we tend to be a bit lighter than other jurisdictions, but I think we can do it. We need to increase a bit for some post-Brexit reasons, but I do not think we should look to extend that, usually. In the end, the relationship between that cost and whether we have messy failures is at the heart of what we do.

Q45 **Baroness Bowles of Berkhamsted:** What do you understand by proportionality both in regulation and in supervision? We have been told that the regulators take a one-size-fits-all approach between banking and insurance, and between retail insurance, commercial insurance and reinsurance, and that there has been a call for a more proportionate approach.

I accept that in part you have started to answer that question in reply to Lord Hollick, but how do you approach proportionality within the regulatory framework and the supervisory actions? Can you give examples of considerations of proportionality affecting a decision or a judgment? Also, can you give us an example of where you apply less than regulators in other jurisdictions? We seem to hear plenty about where you apply more, but if you are using judgment, are there examples of where you are applying less?

***Sam Woods:*** Thank you very much, Baroness Bowles, and it is very nice to see you. You make the right distinction between regulation and supervision. Perhaps I could say a brief word on regulation and then pass to Anna Sweeney on supervision, particularly as it attaches to the London Market, which I think will bring the topic alive.

On regulation, on the insurance side it is true that broadly we have one regulation that covers everyone, which is of course Solvency II. That is not completely true, because we have a non-directive firms regime for the really tiny firms, but everyone else is subject to that one regime. There are some issues with the regime, of course, which we are looking to tackle, but we have found that the regime is broad enough to cover the various different sectors of insurance that we have here in the UK, which in a way is quite remarkable, because what goes on in the London Market is very different from what is going on on the life side.

When it comes to ways in which that regulation is biting perhaps uncomfortably, those issues seem to be more on the life side. We could get into those issues if you want to, or in another session.

We do, though, try to apply that in the way we run the regulations through supervision in a proportionate way. There are some non-insurance examples, but perhaps I could turn to Anna Sweeney for how we do it in the London Market.

***Anna Sweeney:*** Thank you very much for the opportunity to explain. This is a common question from the insurance sector overall.

It is important to say that at the heart of our supervisory approach is thinking about business models and the markets within which firms are operating and then thinking about the risks that they pose. Clearly, the business models and the risks that apply in the London Market are different from those that apply to a retail general insurer, let alone a life insurer or a bank. We focus on very different issues and we think about our approach in that context.

You asked for some examples. I could talk through a couple and would be happy to expand on them to the extent that would be helpful. In the London Market, I would start is that a lot of the firms are global, international firms with platforms in multiple jurisdictions. We very deliberately decided to set out a branching regime that allowed that kind of corporate structure. Our focus on requiring subsidiarisation was limited to large retail operations in the UK. We think that allows these firms to operate efficiently and allows the market to spread risk efficiently.

Given that branching focus, we also recognise the value that the home supervisors give to the jurisdictions, so we adapt. We have arrangements in place whereby we state how we split our responsibilities, and we make sure that we share information with the home regulators, and vice versa, so that we are not duplicating unnecessarily.

The structure that I describe on sharing risk relies a lot on the ability to reinsure within groups and across groups. We take a different approach when thinking about London Market firms and how much reinsurance we would allow and where we would expect collateral or other forms of mitigants to manage and balance the risk. We take a different approach for wholesale reinsurance firms than we do for retail, consumer-based firms where the compensation scheme is exposed.

A fourth example is the way we work alongside Lloyds, given its unique nature, to make sure that we are not duplicating unnecessarily what we do and what they do. Lloyds is a regulated firm, but it is also a regulator itself, so we need to make sure that we are not both trying to get at the same point unless we think there is value in both of us asking in a different way to test it.

That is a small number of examples. We could give other examples if it would be helpful.

Q46 **Baroness Bowles of Berkhamsted:** Thank you. It would be quite nice if you wrote to us, possibly with a little more detail. You say that you take a different approach, and I would like to know what that means in practice. What do you do that is definitely less than you would otherwise do, or what do you definitely not do? You may not be able to answer this question here, but if you write to the committee with perhaps a bit more detail, that would be helpful.

You assure us that you already take a different approach, but then we hear from the industry that it does not feel as if that is the case. We have no evidence on the difference, so I will give you the opportunity to write on that, because you might need to prepare more carefully what you think you can and cannot say. I do appreciate that.

Moving on, do you accept that there are areas where the industry is still subject to rules that need not apply to them. What are the lighter touches that you are applying to commercial insurance and reinsurance transactions, because they do not require the same protections as retail insurance? Indeed, pointing out that difference is a fundamental part of Solvency II. I would like to know exactly what has gone on there. I think Sam Woods just mentioned capital, but what else in the behaviours and contacts and how you supervise is different?

Another example that we constantly hear about, and this relates more often to new business, I think, is that everybody gets a 250-page questionnaire to fill in, no matter their size, and 250 pages of questions is quite a lot. Even if you are allowed to put "not applicable", you still have to go through full compliance and legal checks to make sure that "not applicable" is right. What happens at the other end when that questionnaire comes in? How quickly is it looked at and who is looking at it? What would be the penalty for accidentally putting "not applicable", but there was a bit that was applicable but had been overlooked? This is very much in the mind of industry. I would find 250 pages of questionnaire quite gruelling to fill in, especially if I was dealing with new business and was newly seeking authorisation.

***Sam Woods:*** Maybe I can start and then pass to Anna Sweeney on the new entrants, because she has been closely involved in some of the work on that, including on one very large new entrant. We are very happy to write on the examples that Anna was talking about and we will do that.

Coming to your other points, which are somewhat related, the first is about how industry feels about supervision and regulation. One very important aspect of proportionality is supervisory resource. A lot of the London Market firms might have half a person, but the largest, say the life insurers, would have a team of more like 10, which obviously makes an enormous difference to how it feels on the ground for those being supervised. That is a very important aspect of proportionality, and I think it makes perfect sense for us to do that. I think that half a person, or whatever, should be vigorous and should pursue what they are meant to do, but it obviously makes quite a big difference to the intensity of the supervisory side.

On the regulatory side, we do not have the scope to disapply regulations at the moment. We cannot simply say we do not think that bit of Solvency II is relevant to some firms; it is important that we apply it proportionately to all.

Having said that, there are areas within it where we do things quite differently. Anna has mentioned the branches. We are cutting reporting requirements on branches. We also do not believe—this may sound like a rather extraordinary thing for me to say—that a capital requirement for branches is a particularly useful thing, and we are interested in removing those because the branch is not itself a separate entity. That is quite a significant step that we are interested in.

There are special cases—insurance-linked securities and captives—where we might be a bit more in this space. We may come on to those in other questions, so perhaps I will leave those for now. Perhaps I could pass to Anna on new entrants and what we do there.

**Baroness Bowles of Berkhamsted:** Just before you do that, Sam, you gave a proportionality figure as being the number of supervisors engaged, so if you have only half of a supervisor's time engaged, they can ask fewer questions but that might not feel less to the firm involved, because half a supervisor working on five people is just the same as five working on 50 people in a larger firm. The point is how long it takes to answer questions; the time taken per capital, if you like, in the supervised firm.

***Sam Woods:*** That is a fair challenge, but, looked at from our perspective, Parliament has given us a statutory objective to look into the safety, soundness and policyholder protection for these firms. There is a certain minimum, and if you go below that you are simply not doing that job. Having said that, that minimum can be lower. To give you an example from a different sector, for the credit unions—we have around 400 on the latest count—we have a single team of eight that oversees them all. We are in a reactive-only mode for almost all of them.

There are parts of the sector where we do that, but the sorts of firms we are talking about here in the London Market are a lot more significant than that, and I do think that it is appropriate for us to have less resource on the big firms. I fully accept your broader point that at some level there is an inefficiency in regulation for the smallest firms, that there is a certain kind of unit cost of being regulated that can bite more on the smallest firms. Indeed, it has been a frustration for us in Europe which you will be very familiar with from your former roles, that we have not been able to be as proportionate as we would like, particularly on the banking side.

I guess this is for another day, but one of the first things we are doing post Brexit is developing a simpler regime for little banks because we think that will be good for competition, but we also think, by the way, that that will be good for safety and soundness, which is motivated by exactly the point you are making. I will bring Anna in on the new entrants.

***Anna Sweeney:*** One of the biggest areas of questions that we get from the market is about how responsive we can be to new entrants in particular in this market, because of the need to respond quickly to price changes. Being able to set up a new firm or a new ILS structure on the back of the way price movements have happened across the wholesale market is an essential way of the market reacting, and we want to be helpful on that.

We have authorised a number of firms over the last few years. We have a set of reporting instructions and information requests and we try to make sure that it is applicable to the business that we are talking about. In this market, we have authorised a new firm, from start to finish, within the three-month window, which we think is a reasonable period in comparison with other markets. We did that in a proportionate way, recognising the fact that firms in this market, as opposed to new start-ups perhaps in banking or on the retail end, tend to come with the capital.

Capital is not the issue. The issues are other elements that need to be completed, whether that is some elements of governance or systems and reporting, that kind of thing. We have tried to adapt our approach to this sector to be able to assess the risk which that poses and to take a practical route. If there is a firm coming in with a much larger amount of capital than they would directly need for the business, can we think about that in a proportionate way and allow some of those other elements to be introduced in a slightly more gradual way? We have successfully done that, and I anticipate that we would be able to do so again for other new entrants.

**Baroness Bowles of Berkhamsted:** So your proportionality is dependent upon having lots of capital.

***Anna Sweeney:*** No, sorry. That is a particular feature of this market. That is the way this market functions. In other parts of the insurance sector, as indeed in the banks, the challenge for the set-up is different and you need more of the licence in order to be able to get the set-up. That is a very London Market feature. For other elements of insurance, we are committing—and I think the Minister mentioned this in a recent speech—to looking at introducing a different approach to the regime that would allow lower capital requirements precisely while the other elements of the business build up. I am just trying to make the point that there is a differentiation between the London Market and other parts of the market.

**Baroness Bowles of Berkhamsted:** It sounds like there is more to be done there, but it has not been at your instigation; it has been at the Minister's instigation.

***Sam Woods:*** I do not think that is quite fair. We have had our competition objective since the PRA was created and we have done a lot under that. This is an idea brought across from the banking side that we think may have some relevance to the insurance side.

Is there more to do? Absolutely. I do think that this proportionality area is a potentially rich area for us post Brexit, because we have a greater degree of freedom, but with the rider that if we have been asked to check whether a firm is safe and sound, we ought to do so.

Q47 **Lord Cromwell:** Good morning and well done on getting your blow in first about resources and the changes you are making.

I will pick up a little bit on the last topic before I get to the main question I wanted to ask. Is it fair to say that start-ups in the UK still suffer from a requirement to emerge fully formed in terms of governance and capital? Or do you think you have cracked that?

***Sam Woods:*** Let me bring in Anna again on this, but here perhaps is a way to think about it. I think we ought to expect there to be a base level because, after all, once a company has authorisation, somebody can buy a policy from it and they are on the hook. However, we apply those requirements in a proportionate way to smaller firms. That is true for new entrants, but it is also true for firms that are already in the market.

To give you a topical example, we have supervisory expectations of firms in relation to climate change, and I think it is appropriate for us to have some of those as long as they are consistent with our remit. In the end, we expect a much fuller and more credible answer from a very large insurance company than we would expect from a very small one. That is how we try to achieve that. Anna, do you want to say a bit more on the new entrants?

***Anna Sweeney:*** It is probably quite important to think about the different types of new entrants, because they have different needs. The example I was talking about in response to Baroness Bowles was a large, well-established team that came with credibility from previous businesses, obtained capital from a range of institutional investors, with their ideas and a business plan, and therefore, because they had that capital—that would be typically the way a new reinsurance or wholesale insurance business would be in a start-up mode—what we had to do was to make some judgments about the proportionality of the non-capital requirements because the capital was more than comfortable.

For the other end, the more traditional start-ups, we have the new insurance unit, which is designed to help guide people through the application process. There, capital genuinely is a question. Our ability to flex the capital requirement will not be in place before legislative changes are made, because it comes directly from Solvency II and we cannot fix that bit of it until the legislation goes through.

On the other elements, we have tried to be helpful and talk to firms so that we are not a faceless bureaucracy and they do not know how to approach us, and in other areas we have also been able to take a more judgment-based approach. For example, how many non-executive directors is enough? What do you need at the beginning? What do you need as you build?

It is probably also worth pointing out that, certainly in the general insurance sector, there are lots of routes to establishing new business. There is, for instance, the managing general agent route, where there is no capital requirement because it is using other sources. There are alternatives, and we and the FCA have worked hard to reach out to those businesses.

**Lord Cromwell:** I am sure you are very approachable. You seem to be very approachable and I am sure all your teams are.

On the competitiveness point, a theme that has emerged from some of the evidence we have taken is that there is an almost cultural overcautiousness, if that is good grammar, in how the rules are applied and a discouraging approach to new services, new firms. One answer to that is, "They would say that, wouldn't they?" but let us take two specific examples.

One is insurance-linked securities, which a lot of effort went into establishing and which one of our witnesses described as "withered on the vine". Another example is captives, which I think Sam referred to earlier. In your view, why do we not have thriving markets for those two?

***Anna Sweeney:*** We, alongside the industry and the Government, invested time and effort in setting up the ILS regime, and there have been seven approvals and 11 issuances, but that is clearly fewer than other jurisdictions and fewer than we would like.

Given that the regime has been in operation for a number of years, we have been talking to the industry and thinking about how we can learn from what has happened, and indeed what has not happened, over the period. It is very clear that the concerns essentially are not dissimilar to what we were just talking about—the speed of review and the ability to respond to those rapidly changing markets and bringing capital at those points.

It may be worth pointing out that all there is with ILS is a contract. We do not have governance or any of the other elements to look at. Therefore, the effectiveness of the protection that is given through those kinds of transactions is based on the effectiveness of that contract. We have been focusing on how robust those contracts have been in protecting the insurers and ensuring that the three core requirements are met.

It is probably also worth pointing out that we have had a number of quite complex transactions brought to us rather than all very simple ones, and the ability for both the industry and for us to turn this into a thriving regime has been a little challenged by that. However, we have learned a lot through those contractual reviews, and we are now looking to evolve our approach and processes in particular for the most wholesale, short-tail general insurance transactions. We are looking to continue discussions on this with industry in the immediate future, and we will make any amendments public as soon as we are in a position to do so.

**Lord Cromwell:** So is the crude picture that we have in our minds unfair—that in Singapore, Bermuda and the US there is a welcome mat, while in the UK it is a locked door? What are they doing differently from us if it is not a sort of cultural caution?

***Sam Woods:*** That is not a wholly accurate description, but there is something in it in the sense that we have authorised seven, as Anna says—we have not had many withdraw. But are people really bringing things forward? Do they perceive that we are open? We think we are, but there may be more to be done to get that message out, and maybe the committee’s investigation could be very helpful in that regard.

However, there are some differences. Comparisons are made. Bermuda is a giant market that has authorised something like 81 over the last few years, but Singapore is interesting because it got going a little bit after us and has authorised 13. There may be a number of reasons for that. From talking to our colleagues there, one reason may be that they have had more standardised types of insurance-linked securities to deal with, which makes it a bit easier.

There is another quite big difference, and I have checked this because I wanted to make sure that it was right. My understanding is that, at the moment, if you apply in Singapore, the fees of all your advisers, lawyers and the structurers and so on are paid for out of a fund run by the MAS . We do not have such a fund for paying adviser fees. To me, that would seem an inappropriate thing to do in the London Market—it obviously must make sense in Singapore—but I imagine that has a significant effect and I think it is worth highlighting. Would you like me to say a brief word on captives?

**Lord Cromwell:** Yes, thank you.

***Sam Woods:*** Captives are interesting, and it goes back to Baroness Bowles' question about whether we apply all the regulations to everything.

A pure captive is where all you have is a company setting up a structure in effect within itself to manage its insurance risks. That strikes me as genuinely different from an insurance company, and that difference has been recognised in some other jurisdictions. Guernsey is interesting. The capital standard for an insurance company here is a one in 200-year shock. In Guernsey, they make it a one in 10-year shock, which obviously is much, much lower, if you are a captive.

They are ideas worth looking at. If, between government, Parliament and us, we decide that it is a priority for development, we might need a few more staff to make it happen. The only caution I would add is that you have to be very careful about the boundary issues, because you also have captives that are pooling risks from several companies. That sounds to me a bit more like an insurance company. It may be a mutual insurance company, but it is an insurance company all the same, and you have other captives that work mainly for the company that owns them but also do a bit of third-party. There have been some issues in our jurisdiction with the reg-arb around their boundary. Those would be things to look at.

Q48 **Lord Cromwell:** Thank you. Finally, you mentioned one or two statistics and you said that we have not had many withdrawals. Can you tell us how many? Do you keep statistics on new entrants and withdrawals and compare them? Talk us through a little bit about why people are withdrawing. Is it because they give up the unequal struggle, or they thought they were going to the Post Office? What was it?

***Anna Sweeney:*** On ILS, I think we have had three formal withdrawals, but there will be some that have an informal conversation with us and then do not feel that they can go ahead. It is almost always about speed. I think that is true on the authorisations, and here. I think we have shown on the authorisations bit that we can do it within a timeline that I think is reasonable and is within the ballpark of what others do.

What I have just described is about looking again based on what we have learned, and to see how we can do that while still providing the level of review that we feel we need to. As Sam says, Bermuda has had 20 years of this. We are trying to build it up, but that will require the industry to have some confidence that we will do what we say we will do within the time, and that is what we are trying to work on.

***Sam Woods:*** If you look across the waterfront, we have had authorised 41 new entities during the life of the PRA since 2013—23 insurance companies, 11 managing agents and seven ISPVs that we have just been talking about. We have had six withdrawals. I suppose the question is: does that 41 seem like a reasonable number for the size of our market? It is quite hard to answer that question in a way, but there is a flow. Might there be scope for more? I think the answer is probably yes.

Q49 **Lord Trefgarne:** You have already touched on some of the relationships with the overseas competitors—Switzerland, Singapore and Bermuda, for example. Do you have a good relationship with them? Are you in constant touch? We are given to understand that their response is somewhat crisper than yours and that maybe there is room for improvement.

***Sam Woods:*** We have very good, very regular contact with all those regulators. In our world, the ECB and the Fed are the largest regulators that we deal with, but of course that is not on the insurance side. The others that are probably most relevant to this discussion are the monetary authorities: the Monetary Authority of Singapore, as you say; FINMA in Switzerland; to some extent maybe the HKMA; and the BMA, in Bermuda.

We are in constant touch with all those authorities about regulatory and supervisory things, but we also do a bit of what I think you are touching on here, which is to try to share information about our approaches, about fintech, about how we use data, the authorisations approach to ILS, and things of that kind. We do of course learn things from them in that regard. The most recent example has been on the Swiss side, where, with them being outside the EU, were able to move ahead of us on simpler requirements for little banks. We had a look at what they have done and we have folded some of that thinking into what we are currently consulting on. I am sure that we can learn more, but we do learn.

Q50 **Lord Burns:** Good morning, Sam and Anna. It has been mentioned many times this morning that prudential insurance regulation is to a large extent based on Solvency II. We have been told in various sessions that the UK had an important role in developing Solvency II. Does this mean that, post Brexit, the EU is now the primary driver of insurance regulation? Are there opportunities to tailor our regulatory regime more closely to the circumstances of the London Market?

You also hinted there are some aspects of Solvency II that are a bit of a problem for us. We are interested in knowing how far you favour continuing to maintain a similar regime to the EU, and where the opportunities might be to make changes that are more appropriate for London.

***Sam Woods:*** We have been absolutely clear throughout the withdrawal of the UK from the EU that we have no desire to be a rule taker and just have our rules simply landed on us from the EU. That would be a very unhealthy thing for the UK market, and a number of members of the committee have said similar things in various different places.

Having said that, there is no point diverging for the sake of diverging, so the question for us is to what extent we want to tailor that regime to work better for our market. This is the first kid out of the blocks regarding post-Brexit reform, along with the simpler regime for little banks in the form of the Solvency II review that we are currently undertaking. The governance of that review is slightly complicated because we imported all the laws in the EU form, so some of the rules are in our rulebook and some are with you here in Parliament for government to make recommendations on.

Broadly, there is a distinction here between the London Market and maybe the GI side generally, and the life side. We have two quite big things that we want to change: one is the risk margin, which, particularly for life products, is too big; and one is the matching adjustment, which is really only relevant for annuity books where that needs to be strengthened to some degree. The industry is very much in favour of making changes, although, perhaps unsurprisingly, there is not perfect alignment on what those changes should be.

I will invite Anna in on the London Market side, but the market seems less keen to make changes, because, I think, they find the regime less troublesome but also because of their interest in securing equivalence at some point in the future.

***Anna Sweeney:*** It is helpful to distinguish between life and general insurance, as Sam has. In general insurance, even the domestic ones, the firms broadly think that the regime is okay. They have invested a lot of money and time in it and they do not want to change it.

Sam has talked about the life changes. In the wholesale market they have the same attitude about having invested all that time and effort in it, but, more fundamentally, because they are firms that trade overseas—often, they are part of bigger groups—they want things to be as aligned as possible across borders. In this case, they have always said in response to all the questions, whether from the Treasury or from us, about changes to Solvency II that they do not want to see them.

On the very specific ones, we have already mentioned branch capital. We do not think that is a sensible construct and we have dealt with that for purer insurers where we have the ability to do that. We are looking to deal with that for the other branches going forward. We have also talked about reporting, but, broadly, the industry is not asking for change—the opposite, really; it is asking to keep it as stable as possible so that, if the EU were to consider equivalence, they would have it.

**Lord Burns:** Briefly, to the extent that you want to make changes, what are the processes that we have to go through, and how far is this for you, for the Government, and involving legislation?

***Sam Woods:*** This is a complicated question in relation to the Solvency II review because of the way the rules have been spread across primary and secondary legislation and our rules. To make these changes will require legislation, because there is no sense in doing some bits and not others. Partly because of the way the rules are spread across, it is also not particularly logical.

We are heavily engaged with the Solvency II review, which is a government-led review. The main issues of contention are on the life side, and a particularly lively debate about the matching adjustment and quite how that needs to be formed going forward.

Q51 **Lord Sharkey:** Good morning. My question is about the reintroduction of a competitiveness objective. Helen Thomas, writing in the *Financial Times* in an article headlined, "Bad ideas don't die. They merely hibernate", pointed out that we have tried this before and we abandoned it in 2012. Andrew Bailey said in 2019 that we had tried this and it did not end well for anyone, including the FSA. He went on to say that regulation should work in the public interest rather than entrenching the position of the established industry of the day. Have you changed your minds on all this?

***Sam Woods:*** No. We have the same view as previously, but it is perhaps a bit more nuanced than you might have picked up from those statements, in two respects, and there is also a reason for it being more nuanced. One is an extremely important distinction: the distinction between a primary and a secondary objective for the PRA. I have always thought that the primary objective to promote competitiveness would be a mistake for the prudential regulator, because if it is primary you have to trade it off, to understand the tensions , with your other objectives. I do not think it makes sense to trade off competitiveness issues against safety, soundness and policyholder protection. That is a bad idea from a financial stability point of view.

I also think it is bad for competitiveness itself, because people bring their money to London partly on the grounds that they think it is well regulated and that the rules are clear and fair, but also for the less often stated reason, which is that we invest very heavily upstream in rule-making processes in Basel and the insurance equivalent called the IAIS, which is chaired by our colleague Vicky Saporta. Your influence in those fora and your ability to fashion rules in a way that make sense are definitely diminished if you appear with primary competitiveness objectives.

The crucial thing about a secondary objective is you are neither required nor allowed to do things that damage your primary objective purely in order to pursue with the secondary. That is an extremely important distinction, and in that context we could make a secondary objective work well. The second part of it is a lot depends on exactly what the objective says. There is quite a big difference between an objective to facilitate the long-term growth and competitiveness of the UK economy, including for financial services, say, versus an objective to promote the competitiveness of UK financial services firms. The former is fine, the latter would not be so fine.

Just to finish on this point, the reason for a tiny bit of nuance in this is that we are going through a process whereby the Government propose to push down to us as the regulator quite a lot of rule-making functions that, in a European context, were made with political input of various kinds, and some members of the committee have been very much involved in that process in the past. It is not completely unreasonable for the Government to say that if those functions are being pushed down in that way they should require us, as the regulator, to have in our mind some of the sorts of things we might have had in our mind were we keeping those powers more at a political level. That is why it is reasonable to do something.

**Lord Sharkey:** Would you like to add anything to that, Anna?

***Anna Sweeney:*** No. That is a good explanation. I am not sure I can add at this stage.

**Lord Sharkey:** When it comes to secondary objectives, and there are lots of them around, I always wonder how they are operated. How would you operationalise a competitiveness objective if it were a secondary objective?

***Sam Woods:*** The first thing that we would do, which we are having a trial run of in a different way now, is to establish for all rule-making whether a rule that we are making affects the objective in any way, whether it promotes it, whether it is bad for it or whether it is neutral for it. That is quite a formal process that we have to go through, and we will reveal what we think about that for consultation so that people can get stuck into it. I am quite sure that if we are given the secondary competitiveness objective, that will be something that the industry goes to a lot.

It is a trial run in the sense that you in Parliament have already given us the power to bring in the latest slab of Basel 3.1; this is on the banking side. We were not given a new objective in that, but we were given a "have regard to". That is weaker, but procedurally you have to go through a similar process. We are doing that at the moment.

That is one piece. The other piece is again more of a practical one. Having just exited the EU, we did not always get exactly what we wanted in the way the rules were fashioned. There will be a process here for many years of going through it and saying that we want to maintain standards at least as stringent as the ones we had when we were in the EU, but asking whether there are things here that we should change to make this work better for our market. In practice, there will be quite a lot of going around lifting up rocks and looking for things.

**Lord Sharkey:** What kind of metrics would you need or put in place to measure any progress against a secondary objective?

***Sam Woods:*** That is a very good question to which I have no convincing answer. What I expect we will do is what we do for our current secondary objective, which is a competition objective as distinct from competitiveness. We will produce an annual report. Whether that is required by law or not, it would be a sensible thing to do, so we can say, "Here are things that we've done".

My instinct is it will be quite hard to boil it down some metrics of a management information kind, but if we can do some of that, we will. We will also add more, "Here's what we have done and here's how we think we have impacted the objective".

Q52 **Lord Blackwell:** We made the distinction between regulation and supervision, and you have been arguing for the regulations that you think are appropriate and proportionate to the London Market. A lot of the comments we have had may bear more on the way those are implemented, the level of interaction, the speed of response and the cost of bureaucracy involved in dealing with the supervision.

The case was made to us that the expense ratios in London are higher than in other markets, and that was partly blamed on the supervisory approach. I know that all your supervisory teams work hard and do the best they can. If you compare the PRA with supervisors in other jurisdictions, is there a case to be made that, rather than having 40 people, you would be better off having 20 people who are higher skilled and able to take more informed judgments, rather than people who are having to follow the rules and ask more questions to get to the answers?

***Sam Woods:*** Anna may want to come in too. When you do these cross-jurisdictional comparisons of staffing—they are quite difficult to do on the insurance side—it tends to indicate to us that, if anything, we are at the lighter end. The IMF has just published its FSAP, which is a review of what we do, and it takes an interest in this. It consistently says, and we politely disagree on this point, that we should have more boots on the ground and that we do not have enough supervisors out there in firms checking stuff. That is the view of the IMF.

As I say, we think that we can do this in the fashion in which we pursue supervision in the UK, which is intended to be very much forward-looking and judgment-based and relies on interaction with the senior management at firms to some degree. Is that the same as saying that 40 is the perfect number for the London Market, could it be a bit lower or a bit higher? No. Could we halve that and still credibly say that we are overseeing the market—including, by the way, to the home regulators who let their firms operate here and expect us to be keeping an eye on the London end of it to some degree? I am not sure that we could, to be honest. Anna, what is your view?

***Anna Sweeney:*** On the resourcing point, it may be helpful to do like-for-like comparisons with other parts of the sector. For a medium to large firm in this market, we would have about half a person on it, as Sam said. If it were a bank, we would probably have about five people on the team. You can see a rough comparator. We have quite a lot of very experienced people in our specialist functions. We have people with 20 or 40 years of sectoral experience. I take it as a bit of validation, if painful for us, that our ILS team has been poached by the industry.

If it is all right to talk about something that is not directly regulation, the expense ratios in the London Market are a big part of the problem, but I am not sure that regulation is the biggest part of that. The brokerage fees and acquisition costs are by far the biggest differential, if it is all right to point that out.

Q53 **Baroness Donaghy:** Good morning. Pursuing the theme that we had from witnesses about the grass always being greener, I am interested in your comments just now about resourcing, because it was one of the common complaints that we had from witnesses, particularly in relation to the appointment of case officers, that sometimes there was a built-in delay of three months before that happened.

You took some pride in the fact that the organisation is lean but perhaps not mean. Do you really think you can continue your current work on your existing resources, or do you think there is a cultural issue about project management and pushing a project from beginning to end rather than a processing kind of behaviour? Do you think there is something in the criticism that we have had from witnesses? The witnesses were very keen to say that it was not about the ability or intellectual capacity of the organisation. They were all quite consistent about that, which probably reflects the fact that you have had some poaching from them.

There just seems to be something in there about the way a project is driven, and whether there is some cultural thing built into the organisation. Would you like to comment on that?

***Sam Woods:*** Yes, thank you. On the question of experience, I checked how old our staff are, because I saw that there was some complaint about age. On the latest figures I have, 52% of staff are aged over 40, which sadly includes me and Anna, and 80% are aged over 30, so there is not much in that. It is a hub-and-spoke system, so you will naturally have people who are running a moderately large firm, and they are expected to be able to forge a relationship and deal with the people running the supervision team who will often be earlier in their careers.

On the complaint about casework, there is one very specific area where our performance is a long way south of what I, and I am sure Anna, would like it to be. This is in relation to the timeliness of the approval of senior managers. Our timeliness in meeting our own timelines was until a little while ago always at the high 90%; we almost had them all done in time. One hundred per cent is unrealistic, because you always get some peculiar case or something happens. More recently, unfortunately more than one-third of our cases have been taking longer than that.

I do not wish to pass the buck, and I cannot because I am on the FCA board, but there is one overwhelming reason. When the senior managers certification regime was broadened out beyond banks and insurance companies, there was, unsurprisingly, an enormous bow wave into the FCA of the number of applications they get to approve. That has caused delays at the FCA end, which knocks directly on to us because the dual regulator firms have to find their place in the queue. The team at the FCA and the FCA board have been very focused on that. We have been discussing it, and some concrete steps have gone in within the last couple of months that will help move that forward.

You are probably hearing a bit of frustration about whether we are quick enough generally on things that firms want us to do, but you are also probably picking up frustration about the timeliness of that process. That does need to get better, and we are on the case.

**Baroness Donaghy:** I will just press you a little bit on the culture of project management actually driving something forward, which I asked you about.

***Sam Woods:*** I have never worked in an organisation, or ever seen one, that had a perfect score sheet on project management. Anna, do you want to talk about some of the things that have come in, maybe not the specifics but how we deal with things on a project basis?

***Anna Sweeney:*** For big projects, we use the disciplines that you would expect. I think what we are talking about here is how that gets translated to the transactions that happen on a day-to-day basis and what the real cost is for that. When I have been talking about speed, I have been talking about that very clearly in the context of the capital coming in and it being able to get to that starting point, whether that is on ILS or new firms, and that is a very specific requirement for the London Market.

On the general point, Parliament sets some mandatory statutory timelines by which we have to do things, and we work hard to manage within those. There is a peak and trough element about the firm-driven demand that we need to manage in the proactive risk assessment work that we are doing. We could always be better at this kind of thing, but we do have management information. Sam hauls people in to talk to him if they are missing deadlines. We had a bit of that a few years ago, but the record since then has been quite positive and all supervisors are incentivised. Everyone has an objective to ensure that they are delivering within the timelines that we agree.

***Sam Woods:*** I am conscious of time, but there a small tension that Anna mentioned that is worth being aware of. There are broadly two things that we do. One is stuff that we think we need to do in order to assure ourselves about safety and soundness in firms and policyholder protection, but there is also quite a lot of work that we have to do that is reactive to firms. Firms decide that they want to buy each other or move a book around the business in a Part 7 and all that. We try to be very responsive to that, but there is a bit of a tension too. Our lives could be completely swamped by all that activity, and then we might not be doing the things that we need to do for ourselves. We are sometimes balancing off a bit what we are trying to do with what firms are trying to do. That is not a bad place to be in, but it is perhaps a natural tension.

Q54 **Baroness Donaghy:** Finally, would you ever consider increasing the levy to enable more investment in resources?

***Sam Woods:*** The answer is yes. We are currently doing it in a very specific way. As a result of Brexit, we have a far bigger role as a rule-maker, so we are staffing up in our policy area, not in Anna's area but in our policy area; not enormously—we do need some more heads in there to allow us to do effectively what the European Commission used to do. That is one quite big area.

Beyond that I have tended to resist the idea that we should always be adding staff, because supervision is a bit of a judgment. We could use 80 people in the London Market and would find stuff for them to do, but it is not needed. Where we might need staff in a more limited way would be if we were given this secondary competitiveness objective and we wanted to pursue particular things.

We talked about captives earlier. We would not want to haul people off doing important supervisory work in order to develop a captives regime. We would probably need to add a small number of heads to do things like that. I think that would be relatively small beer.

**The Chair:** Thank you. We have gone over time a little but thank you very much indeed for your contributions. You are going to send us some further examples on Baroness Bowles' question and that will be helpful. Thank you.

***Anna Sweeney:*** Thank you very much.

***Sam Woods:*** Thank you.