



Industry and Regulators Committee

Corrected oral evidence: Commercial insurance and reinsurance regulation

Tuesday 15 March 2022

11.45 am

Watch the meeting

Members present: Lord Sharkey (In the Chair); Lord Blackwell; Baroness Bowles of Berkhamsted; Lord Burns; Lord Cromwell; Lord Reay; Lord Trefgarne.

Evidence Session No. 7

Heard in Public

Questions 77 - 84

Witnesses

I: Richard Dudley, Global Head of Climate Strategy, Aon; David Sansom, Chief Risk Officer, Lloyd's.

Examination of witnesses

Richard Dudley and David Sansom.

Q77 The Chair: Good morning and welcome to the seventh evidence session of the Industry and Regulators Committee on commercial insurance and reinsurance. It is a pleasure to welcome our witnesses for this session: Richard Dudley, global head of climate strategy at Aon, and chair of the London & International Insurance Brokers' Association; and David Sansom, chief risk officer at Lloyd's.

The witnesses have before them a declaration of Members' interests. This session is being broadcast by parliamentlive.tv. A full transcript is being taken and will be made available shortly after the meeting to make any corrections.

Before we get on to the main topic of the inquiry, perhaps we could touch on Ukraine and the sanctions imposed by the UK Government. As you may have heard, the FCA has told us that implementing these sanctions is a significant exercise, but it is confident that the industry can implement them as it has previous experience.

Do you share the FCA's confidence, and how quickly can you implement sanctions? What will be the effect of Russia being cut off from the London market both immediately and in the longer term? Richard, perhaps you would like to start.

Richard Dudley: Thank you, Chair. I will repeat the comments you heard in the earlier session about the tragedy that is unfolding in Ukraine. As far as the industry is concerned, we are a global marketplace and we are used to dealing in business all around the world. In fact, the team that I just ceased leading at Aon does business with clients in 158 countries around the world, so there is always complexity to do with law and very often with sanctions as well. In fact, we have been very used to that in places such as Iran, Syria, Sudan, Cuba and other territories.

It is not something that we are not used to dealing with. We are geared up to deal with the imposition of new sanctions. Obviously, this is a little more challenging because those sanctions have been changing on a daily basis, literally, since they were first announced. Most firms in the market—certainly my own—would have very well-developed risk and compliance functions that are immediately on top of those sorts of requests.

One of the key areas for us—and I am sure my colleague, David, will expand on this with his Lloyd's of London hat on—is to ensure that these sanctions are consistent across the world. We are dealing with clients from all over the world, and a number of the firms that we have in our marketplace are owned by either US or European parents, so if there is anything that is out of step in terms of those sanctions between the different territories that is where it gets particularly difficult.

As far as the impact of Russia being cut off from the market is concerned, as you put it, in one sense it is not significant in the long term because

the proportion of business that Russia represents directly into the London insurance market is pretty modest.

We are used to a globalised world. We are used to dealing with clients from almost every jurisdiction around the world who are multinationals. Many of them have operations and/or supply chain dependencies inside Russia. The complexity of those and thinking about the impact on their insurance requirements will take some time to evolve, but the direct impact is fairly limited.

David Sansom: Good morning and thank you for the opportunity to give evidence this morning. I would also echo our shock and sadness at events in Ukraine. Because of that, we as Lloyd's have been playing a role quite actively with the Treasury and the UK regulators on a daily basis on the rollout and implementation of these sanctions, but, as Richard and others have said, we are well used to doing this. We have these mechanisms in the market and we have had them in place for many years.

The pace at which these sanctions are being rolled out is unprecedented, so that presents a challenge. Because of that, it is important for our market that we work with government and the regulators to make sure that these sanctions are designed in the right way to have the intent that they are designed for and to minimise the potential risk of disruption and misalignment. That is particularly an issue where the sanctions regime is being rolled out at different paces between the UK, the EU and the US, but it is well within our remit to manage.

On the impact, I have nothing particularly to add to Richard's comments. For our market, we think the direct impact is minimal. As with the broader London market, we do not write a lot of business in Russia or Ukraine. There will be some indirect impact. As a market we write policies relating to cyber risk, aviation and political violence. Those will be impacted by current events, and that will take some time to fully understand, but those remain well within our control and our level of comfort at the moment.

Q78 The Chair: Thank you for that. We now turn to the main subject of the inquiry. We have heard from several witnesses that regulators can be excessively interventionist, sometimes acting almost as a shadow board, requesting a great deal of information and a great number of meetings. Do you recognise that characterisation, and, if you do, what effect does that kind of behaviour have on the London market?

Richard Dudley: The company I work for is called Aon. We are one of the largest global insurance broking firms generally. In my role as chair of LIIBA, the London & International Insurance Brokers' Association, it is worth pointing out that we have about 152 broking group members in total, and about 240 individual firms as membership of that organisation. The vast majority of them are very small; 50% of those firms probably have fewer than 10 people. Certainly, there are only 18 firms of the 152 that have more than 100 people.

There are a lot of very small organisations that would not recognise what you have been hearing. My firm probably would. We are a large, fixed firm, as the FCA would call it. We would expect a high degree of interaction with the regulator. That is fine.

One of the important elements for us is that some of that interaction is driven by us because we want to make sure that we get ahead of any requests we receive and that we are doing all the right things across the quite broad pantheon of different businesses we have in the UK. The business I run is a London market business. We also have a UK retail insurance brokerage as well, which has a different set of consumer characteristics.

For me, it is not necessarily the absolute number of interactions we are having; as I am sure we will get on to in future questions, it is probably the nature of some of the topics that we are having to discuss with them, which, in our estimation, is probably more burdensome than it needs to be.

David Sansom: At Lloyd's, we represent about half of the London market in terms of the business that is written. We have 52 managing agents—those are our insurance companies—and they manage about 100 syndicates. We as Lloyd's are very heavily regulated. That is appropriate because we represent a big chunk of the market. We have a lot of meetings with the regulators, both the PRA and the FCA, and that is entirely appropriate for a firm of our size. If you take the current situation, we are having daily meetings on Ukraine. If you go back a couple of years, on Covid we were having meetings two or three times a day. When things happen and there is regular interaction, for a firm of our size, it is entirely appropriate.

The issue for me is more around what you might describe as the business-as-usual type of interaction. There, perhaps it is less the number of meetings and more the actions generated from them. As Lloyd's we are ourselves a regulator, so we oversee the market. One of our particular challenges with the PRA and the FCA—we work very closely with them—is to avoid duplication on the half of the market that is in effect subject to regulation from three parties, if you count the PRA, the FCA and Lloyd's. We work actively to reduce that. We have had to step back as Lloyd's and ask ourselves some challenging questions on whether we are being overly burdensome, such as whether we need to write that five-page letter to that particular managing agent.

I will draw on a quick example of where we have had to think about this. We recently updated our oversight approach at the end of last year to be more proportionate and to be more risk based. Under our new approach, we are attempting to differentiate businesses in our market. Those that we think are poorer performing or have challenges around government operations or whatever it might be will get more of our attention and focus as a regulator. Those businesses that are better performing will get different conversations on how we can help them to grow. A poorer-

performing business, if it comes to us with an opportunity for growth, will find a more difficult conversation.

As a regulator ourselves, we have had to step back. I recognise the challenge that the PRA and the FCA have on that. One of the questions from our market to us on this approach—it was very supportive—was, “How are you going to apply judgment?” For me, the conversations that we will have around proportionality in future questions come back to having to apply judgment. That is a cultural change. It requires a different way of thinking. It is also entirely possible within current frameworks.

Q79 Lord Cromwell: Good morning. Thank you for coming and for your written submissions, which are very helpful.

It was particularly interesting to hear you differentiate between the sizes, which others have not particularly picked up on, and the degree of complexity and appropriateness of how they are supervised. You have the advantage of having sat at the back and heard the questions put to the two witnesses who sat in those chairs before you, so I am going to try to focus down. You can give me points—or not—for brevity if I manage to pull it off.

The first area is the matter of one-size-fits-all application, and that is a regulation application question. The other is about the wider culture of excessive caution. We have been given examples of captives and the ILS on one size fits all. Can you identify other areas where perhaps unnecessary rules are being applied that we should be thinking about? On the culture side, what practical steps could be taken to enable the innovation that is apparently being stifled by this culture of caution?

Richard Dudley: Thanks for the question. As to other examples, you probably heard a little bit about the general insurance pricing practices review, which was instigated by the FCA—probably fairly, to be honest. One of the things that led to was the enhanced product governance rules that we now see in general insurance in the UK. Those have been applied—or we, as a firm like Aon, are expected to apply them—across every single aspect of our business in the UK.

The pricing practices review was stimulated by a review of the motor and home insurance market where you have a very distinct asymmetry of information between the providers of the products and the buyers of those products. As you heard in slightly different ways from your previous witnesses, most of the businesses we are dealing with, whether they are in the UK or in one of those other 157 countries that I mentioned earlier, are fairly large and certainly quite sophisticated buyers of the products they are purchasing from us.

The other really important point to mention, which you may not have heard already, is that, certainly in my role as a broker, we spend sometimes up to literally the whole 12 months in advance of the action of purchasing a risk transfer insurance product advising the clients on the risks that they face, whether they have fully understood those risks, how

to mitigate those risks, and how to think about ways internally of using their own capital to mitigate that risk, before they then make a decision to buy a risk transfer product. When you have been in a series of advisory negotiations like that with your client for 10 months, to have to conform and go through a series of steps in the enhanced product governance rules just does not make any sense at all. That is a very obvious example of where, for me, there is a one-size-fits-all approach.

On the cultural side, it is hard to be specific because I do not have the luxury of having dealt with many other regulators around the world. I know how those regulators deal with others in my firm. We are an international group. I wonder—you heard this from previous witnesses—about the level of cautiousness that we see, and without question, with the risk-averse nature of the way the regulators make decisions, there is no doubt that that is pretty consistent. That is consistent with financial security, stability of the market and so forth. It may well be because of the impact and the run-on that we saw since the financial crisis in 2008 that that has become the pervading culture within the regulatory environment.

We see less obvious examples of where they are genuinely trying to help us to stimulate new product development and to think about the trade position and the role that we play in the export market for the UK. Maybe there will be an opportunity later, but especially with the future in mind there is a colossal opportunity there for UK plc that we will struggle to grasp unless we can get our hands around some of this.

Lord Cromwell: Thank you. David, can I ask you the same question but I would like to add on about the regulatory sandbox of the FCA? You have argued that there is a role for that in the PRA-FCA New Insurer Start-up Unit. I am grasping for good news here. Is there good news to be found there or not?

David Sansom: Yes, there is. I will take the first part of the question first. I will give you another example of a one size fits all, which, by the way, I do not think is pervasive. This is not the case everywhere.

A couple of years ago the FCA and the PRA rolled out a new set of requirements in relation to operational resilience. They developed that across financial services. It was designed really for the banks, because a bank's operational failure is an immediate issue for the industry in a way that it is not quite for an insurance company because of the longer timeframes involved. This regulation and these requirements were, in effect, a one size fits all rolled out across.

If you take the insurance sector, specifically the London market, that essentially means that insurers have to deal with a set of regulations designed for someone else. The point here is that if you step back and say, "Should insurers or London market insurers manage their resiliency?", yes, of course they should, but that could have been achieved under the current requirements. There are plenty of rules in the rulebook that talk about the adequacy of systems and controls in relation

to operations and operational risk. This is not something that required a two-year consultation or rolling out of a set of requirements. If you are running a business, the risk is that you end up doing something to tick a box that does not connect to a real way that you are managing resilience in your organisation, so it is a very good example of what you are referring to.

In looking for some good news and talking about the sandbox, we are a big supporter of that. As you may know and we have put in our evidence, at Lloyd's we have set up our version of that, which we have called a syndicate in a box. This is a way to get an innovative, accretive new business into our market. We set that up a couple of years ago. I think we have had five successful syndicates in a box.

Through that, we have created limitations on these businesses. They have to be of a certain size. They cannot write long-tail, catastrophe-exposed business. Because they are lower risk, we can reduce some of our requirements that we as Lloyd's place on top of new syndicates, and we have a much shorter application period. We work with them to achieve that shorter period.

This is not a soft touch. The businesses in the sandbox have three years. If they demonstrate a track record of performance, they graduate into a full business in our market. If not, they are out. We are a big supporter of that, and we think, equally, that the PRA, looking at its mobilisation unit, gives a big opportunity. Some of the businesses that we have successfully tracked through are exactly the type of innovative businesses that we want more of in the market.

Lord Cromwell: If you can be unbiased, if I am an innovator, am I going to be keener to get in your sandbox or the FCA's one?

David Sansom: That is a difficult question to answer. The answer effectively may be both.

Lord Cromwell: That is very diplomatic.

David Sansom: Again, that comes back to our challenge in managing the duplication point. I would not say as a regulator that we have fully cracked this yet, but that is our attempt to do so.

Lord Cromwell: Thank you very much, both.

Q80 **Lord Trefgarne:** We have heard concerns about delays in regulatory processes, particularly relating to the appointment of case officers. Do you feel that the regulator has the capability to meet its service standards? Following on from that, if you are unhappy with the level of service you receive from the regulators, would you support increasing fees to enable more investment in resources?

David Sansom: Certainly, from a Lloyd's perspective, that is not a particular issue for us in terms of the case officers that apply to us because we are such a large business and we tend to get more of that

attention when we need it from the regulators in managing our applications.

Do I think they have enough resources to do that? I would say yes. What I think they could do—you heard this from some of the previous witnesses—is be more targeted on a risk basis in how they apply their applications. If you take the applications of senior managers, those are processed by a different department in the FCA and the PRA—an authorisations department. They are not the day-to-day supervisors. They are not close to the business in the way that the supervisors are. I think they could do more to sit down with the supervisors at the start of the process and say, “Do we really need to go for a full process with this individual?”, because as a supervisor they may have seen this applicant two, three, or four times in the industry beforehand. There are better ways they can apply their current set of resources.

On fees, it is clearly a loaded question to ask a regulated firm whether the fees should go up. I do not think that they should. As Lloyd’s, we also provide a levy on the market. We do not increase that levy. We have not increased it in my time at Lloyd’s. We are very conscious of having to oversee the market with the resources that we have for which the market pays. As a regulator ourselves, we recognise that you have to supervise with what you have. On that basis I would not support a fee increase.

Richard Dudley: I agree with a lot of what David’s remarks contained. I would add two things.

On the question of delays in authorisations, I am not sure it is down to a lack of resources. David’s comments are absolutely right in terms of them being a separate department, not necessarily conjoined with a supervisory department and necessarily understanding who some of the people they are seeing are and/or some of the firms they are being asked to authorise those people for.

On resources at the FCA, we see quite a lot of turnover. Obviously, I cannot talk about the PRA; we are only regulated by the FCA as an intermediary. Certainly, at the FCA, we quite often see turnover in staff and turnover in the people who are supervising us as Aon and/or the people in those authorisation teams. Whether that is a symbol of a lack of resources or too much change in how they execute or use those resources, I could not tell you because I am not as familiar with the inner workings of the FCA. That is one of the things that we see.

On the fees side, there is no question that, if you add together the physical fees we pay in the UK, combined with what we would add into that in terms of management time and the processes and the resources that we have to recruit, employ and maintain to follow the governance expected under our regulatory framework, it is probably the highest cost of any of the major jurisdictions that we deal with globally. That, for me, does not justify an increase in the fees.

Lord Trefgarne: What if they increase the salaries? If you increase the

fees, you could then increase the salaries and perhaps they would stay longer.

Richard Dudley: They could. That is one option. The other option—perhaps we will get on to this—is how they could think about the proportionality of the fees they are looking at, the investigations that they launch and the supervisory reporting that they expect from us. As I mentioned, are the product governance rules really applicable to every element of what we are dealing with, particularly in the London market? Quite a lot of resources and time could be freed up by them being more targeted in how they actually go about that process.

Q81 **Lord Burns:** We have discussed with various witnesses the opportunities that Brexit might provide for charting our own course. We have heard from the regulators and industry that, basically, the industry is not seeking wholesale changes to Solvency II; it sees a lot positive there and there is a lot good about it. But we also hear that there is some desire to see government and Parliament take more ownership for how the arrangement actually operates. Do you share those views?

David Sansom: Essentially, yes. We would not support wholesale change to the fundamentals of Solvency II for the reasons you have heard. That robustness around governance, risk management and capital adequacy is a competitive advantage for our market internationally. On Solvency II—others have said this—as the London market, we are less focused on the areas that have been discussed on the matching adjustment and the risk margin.

The two areas I bring out specifically, on reporting and the bureaucracy in the use of internal capital models, are big opportunities for our market. There are certain aspects of that Solvency II review that we are very keen that the Government and the regulator look at.

If I might touch on the internal model example just to bring it alive a little, that is an important mechanism for firms in our market to set their own risk-based capital. It is particularly important for our market because of the specialist, commercial nature of the business that we do. It is not well suited to a standard formula approach. Every business in our market—all 52 managing agents—has a Solvency II internal model, and we as Lloyd's have an aggregate one. We go through that approval process with the regulator. If I had to pick one process, it is our most burdensome.

We as an organisation, and as an executive responsible to the board, or our council in our case, have to demonstrate to them that we have a robust and valid capital model. The regulator then effectively repeats that whole process and does not feel able to rely on us and our robustness in our own validation activity to achieve that same level of certainty. They have said that they will look at that under Solvency II. It is generated less with the interest compared to some of the other areas you might have heard about. That, along with the reporting, is a big opportunity.

Lord Burns: We heard from the regulator that it is open to discussing regulatory improvements with Lloyd's to improve competitiveness, but that some of this was down to you. We heard from you about some of the changes that you have been making to this. Do you see much prospect for helpful discussions with the regulators on those issues?

David Sansom: There is a huge opportunity for us. We work with the FCA and the PRA under a series of co-operation agreements. That governs our interactions as regulators on our half of the market at Lloyd's. We have said this year that we will revise those. Those give us an opportunity even within the current construct to change the way we do things.

You asked more broadly about the opportunity. I will give another example to bring it to life. Under Solvency II, the PRA effectively designates firms into two buckets—Solvency II and non-Solvency II. It is only really the very smallest insurers that end up in the non-Solvency II bucket. That gives an opportunity to think about a much broader approach. You have heard of other jurisdictions such as Bermuda that have a multilicence approach, which enables them to differentiate between the type of businesses, whether it is a captive up to a full reinsurer, and the way they apply those different licences. That is an example of the type of broader thinking that could be possible within the current framework.

From our perspective, our key aim is to reduce duplication. We have those co-operation agreements and we have a big opportunity to look at that.

Richard Dudley: Just to remind the committee, my role is as an intermediary. Our concern on the prudential regulation side is to make sure that we are offering our clients capacity with insurers that are solvent and going to pay claims, and with insurers that can work with us to design products that are appropriate for those clients. I do not see that there are any major requirements to change Solvency II in that regard.

When you hear from the UK life industry, as David mentioned, about their desire for change in Solvency II, I can understand that completely. I also think there is an indirect benefit if that change is executed because it will enable them to invest and probably think about underwriting some of the longer-term investments that are required, particularly in things like the net-zero transition for some of the new technologies, particularly on the energy side, which is difficult to do under current solvency requirements.

The only other point I would make from our perspective is that we are a global marketplace; it is not just Europe and the UK. In fact, the majority of the business that comes to the market is from the US. A lot of business is from Australia, Canada and other parts of the world as well. Our goal is to make sure that we continue to have that global access. We operate in terms of being able to work with European firms to bring business into the market.

We had to come up with some new business models to do that following Brexit, which are governed by some recommendations expressed by the European Insurance and Occupational Pensions Authority. That is something that we need to maintain consistency with. I actually think it is an important topic for international trade negotiations to make sure that we can maintain that global access. To do what our market is good at and to use the expertise that exists here in a way that does not exist in other marketplaces, we have to be able to have access to those overseas markets, including Europe, and not just Europe.

Lord Burns: We heard in the previous session that the practitioner panel arrangements we have here fall somewhat short of some of the arrangements there are now in other jurisdictions in bringing issues to the surface that are emerging within these frameworks and that might be capable of being amended. We do not have the right level of transparency. We do not possibly have the right people on the panel to make that work effectively. Do you have sympathy with that view?

David Sansom: I sit on one of the practitioner panels. I suppose they may have their own view on the quality of individuals who turn up. There is an important point here on how these panels and the general consultation that happens with industry could be made much more effective. The experience of sitting on these types of panels and going to the regular briefings with the PRA and the FCA is that it can feel very much like a download. It is the regulator saying, "This is what we are going to do".

There is a real opportunity to engage more actively and earlier in the process so you are not simply sitting there receiving what the regulator is going to do as an information-sharing exercise, but you are able to really help them develop the policies and say, "Hold on a minute, you might want to think about doing this a different way." When you look at other jurisdictions, in my understanding, they try to have that earlier engagement. As someone who sits on these panels, it can feel a little bit as if it is slightly after the event and you are simply being informed of what the decision is.

Lord Burns: You are being informed rather than consulted.

David Sansom: Yes.

Richard Dudley: I do not sit on these practitioner panels. Earlier you mentioned the word "transparency"; there is a lack of transparency for most of the industry about what goes on before, during and after these practitioner panels. I just think there is a lack of transparency in the process.

Baroness Bowles of Berkhamsted: Before we get on to my question, I would like to pursue a little further the issue of policy formation and where you have two of the practitioner panels. In the previous session, it was observed that there is no UK participation now in the policy formation that happened in the EU, but the regulators make reference to

the IAIS and the role that the UK plays in that. The IAIS, as I understand it, does not have the same level of publicity and conferences where all parties engage as happens in the EU; as you have just explained, all we get instead is the secret panels. Do you think that there need to be more public conferences in which there is substantial involvement by more parties than merely industry and regulators?

David Sansom: Thank you, it is a good question. I would agree, from a public perspective, that getting more engagement and getting that engagement early on would be helpful. I feel that as a practitioner and as a representative of the industry we should be engaged earlier and more actively in the process.

To your challenge, if there is more visibility and transparency around that process, we can take broader and greater soundings across the industry as a whole in how we are representing into those conversations. One of the aspects naturally on those panels and in those consultations is that it tends to be the bigger firms that are involved. There are trade bodies that represent the smaller organisations. Generally, the industry is pretty good at aligning on a set of views, but as a regulator you might want some different perspectives.

Baroness Bowles of Berkhamsted: My experience is that you do not need to have a common view, but you need to know what does not work for others. Unless you have more public discussions, I do not see how we are going to get to that.

Richard Dudley: To add to David's point, this is the perfect time to be addressing this. I have recently been asked to take on a new role as the global head of climate strategy for Aon. It is about trying to make sure that we as an industry, and Aon as a firm, can play our part in providing products and services that will enable two things. One is to mitigate the existing effects of what is happening to the climate—you heard a little about that in the last session—and, secondly, to think about how we can play our role to accelerate and enable those capital flows that are required to develop all the new technologies, not just in the energy industry but in plenty of other industries besides.

We are going to have to think differently to do that because a number of these technologies are new. Our industry is used to generally looking in the rearview mirror to price risk by taking data and applying actuarial techniques to it. That is a generalisation, but that is generally how we do it.

We might want to think about the tenor of our insurance products, for example. Some of the new investments that are being made in the carbon capture industry and things like that are very long term, and they do not want the instability that might be associated with an annual policy renewal in an insurance product. It is about how we can think through that and how we can embed that in a way that is more akin to other sources of capital.

Those are all things we need to think differently about, and we will not be able to do that unless we are able to have an open debate in advance on how the regulatory principles will be applied. So I would support what you are saying there, Baroness.

Baroness Bowles of Berkhamsted: Do you think that we are still tapping into the public engagements that go on in the EU? They were not closed to EU people. They are public and they are for ever having people invited from other jurisdictions, the US and elsewhere. Are our industry and our regulators still utilising those, or have we turned our back on them?

David Sansom: I am happy to comment on that. To prepare for Brexit, we as Lloyd's set up an insurance company in Brussels. Many others in the market have done the same thing. To your question, those organisations, those subsidiaries, are well embedded into their own local regulatory jurisdictions. In our example with the Belgian regulators, our Belgian insurance company is actively engaged in the dialogue with them, and through them to other bodies such as EIOPA. To the extent that the market is an international market, has a European presence, has changed that as a result of Brexit and set up those mechanisms, we are still able to engage and indeed influence through those discussions.

Baroness Bowles of Berkhamsted: Does that feed up to how you deal with the UK aspects of things?

David Sansom: It does.

Q82 **Baroness Bowles of Berkhamsted:** I will go on to what I was supposed to ask, which is to do with the competitiveness agenda. It is highly likely that it is going to end up as a secondary objective rather than a primary objective. Do you support that? Are you concerned that the London market may lose its reputation for stability and soundness if such an objective leads to weaker regulation? Perhaps you should say whether you think it would lead to weaker regulation or not.

In that context, in the previous session there was the suggestion, probably mainly regarding the PRA, that it operates, essentially, as a no-failure regime, although that is not what the regulators tell us. Do you think that, essentially, it is operating as a no-failure regime, and, therefore, how would a secondary competitiveness requirement sit alongside that?

David Sansom: We support the objective, and even as a secondary objective it can be made to work. I do not think there is a direct trade-off between competitiveness and robustness. Certainly, I do not think that the London market would be less robust if that objective were applied. Again, I will share some of our own perspectives at Lloyd's because we also have dual objectives. We supervise our market, but we also have to promote it, so we are aware of that need for balance. I think it is a balance; it is not a zero-sum game.

I have an example to bring it to life. Richard mentioned climate discussions. I had a discussion with an international regulator a couple of weeks ago, and in the first half of the meeting they asked how we as Lloyd's were managing our climate risks. The focus was very much on risk management and risk mitigation. In the second half of the meeting, the same team then switched tack and asked me what Lloyd's was doing to encourage the innovation of more green finance and green insurance in their jurisdiction. There are regulators, and we would be one of them, who have dual objectives, and I think those can be balanced.

Certainly, we would not say, and I would not say, that we relax our prudential, or indeed our conduct, robustness. It means we have to exercise more judgment. Back to some of my earlier comments, it means it is harder than just following down the tick list. That brings us back to the conversations we have had around culture and how that needs to be different.

Richard Dudley: I agree with David's comments. I do not think the addition of a competitiveness objective will weaken the regulatory system in the UK. By the way, a weaker regulatory system is not what the industry wants either. As I mentioned, especially in our London market, it is a global marketplace, and we have to be competitive in the development of products and services for that marketplace. To have the regulator specifically tasked with making sure that they bear that in mind is really important. You have heard that, I am sure, from many other witnesses across the industry.

It is not that unusual either. You see that in other regulators around the world. One of the key things is not just the fact that there is an objective but we need to make sure there is clarity in exactly how the regulators will implement the objective and how they will be held accountable against it. Plenty of benchmarks and sector metrics are already used globally that we could probably take from quite easily without having to reinvent the wheel.

For example, the World Economic Forum and the OECD have plenty of metrics that they track for different jurisdictions about the number of start-ups, the flows of capital, and the number of products and services that are being developed. FINMA, the regulator in Switzerland, is required to report once a year not just on market stability but on the competitiveness of the Swiss financial services industry. In Australia, the regulator there, APRA, has to report once a year under what I think they call the regulator performance framework, which is less about international competitiveness and more about some of the other topics we have been discussing, which is the burdensome nature of regulation or otherwise. They have some very specific statistics that they have to report against, which they get from the companies that they regulate. There are some very obvious examples from which we could learn.

Baroness Bowles of Berkhamsted: Thank you, that is very useful, because my follow-up question was going to be about how this is going to be operationalised within the work of the regulators, the metrics that we

should use to judge and how to be held accountable. Is a discussion in their annual report sufficient? I think the answer to that is not a bland discussion.

We have talked about it being a matter of balance, and there is a fear that as a secondary objective it is not even going to get into the scales. There is a big, heavy, one side in the scales, which is stability, and nothing else is ever weighed against it. You have already mentioned some. It might be quite helpful if you could provide us with a full list of all the metrics that you know about from other places and which ones might be most useful in the UK. Again, if they say they have done it, how are we going to hold them accountable to that?

Richard Dudley: That is a question for government and Parliament. You are right that just reporting on those statistics would not be good enough necessarily, perhaps in a similar way to the fact that they have to appear in front of the Treasury Select Committee as it stands, and then when they go away again not much will happen after that. The level of accountability and the teeth in that accountability are really important perhaps in a way we have not seen to date. Whatever the measures are, the ability not just to enforce the measurement and the reporting of them but to explain why they have not met certain targets that might be set by Parliament and the Government will be important too.

Baroness Bowles of Berkhamsted: The only measure at the moment is a hot seat in the Treasury Select Committee interrogation, wriggling around for a couple of hours at most and then going away again. Do you think that there should be issues that, if they do not meet up two years in a row, people go?

Richard Dudley: This links to one of the other questions that you have been discussing, which is the role the regulators think they have, not just in following a secondary objective of competitiveness but the dedicated resources that they have. You have heard from other witnesses about the way that is approached in places such as Bermuda and Singapore, where there is much more of a collaborative approach not just between the teams within a regulator, some of whom are specifically asked to challenge their own teams to make sure that that competitiveness agenda is maintained and constantly refreshed, but in the way those teams interact with the government organisations in their relevant territories, with advisory boards and/or other representatives from the industries they regulate in the way that we discussed a little earlier. Those would all be part of the same set of goals for me as opposed to just a point-to-point set of accountabilities.

David Sansom: The conversation with your previous witnesses about setting individual objectives really is important, particularly for senior managers in the regulator. Whether the overall objective is primary or secondary to be embedded, it needs to be set in individuals' objectives. For all of us as senior managers in our businesses, going back to the earlier conversation, we have objectives. If we do not meet them we are

accountable for that. In that sense, the regulator should not be any different.

To your question of whether that means they get just a two-hour difficult conversation once a year, no, I do not think it would. That would be a much more regular conversation with their senior managers and their accountable executives as to how they were meeting those objectives. That could be applied down through the levels of seniority. It would not just be the top senior managers.

Baroness Bowles of Berkhamsted: I see where you are going. Does any of that exist at the moment, to your knowledge? If not, would that be sufficient to bring about the culture change that we have been talking about?

David Sansom: It would certainly help with that cultural change. I am not sure, frankly, to what extent that already exists within the PRA and the FCA, and they would probably have to answer that. That is how you embed cultural change. It is back to the adage, "What gets measured gets done", and it is around embedding those within objectives.

Baroness Bowles of Berkhamsted: That is probably the motto—"What gets measured gets done". Therefore, it must be measured and reported on, and changes made if it does not measure up.

David Sansom: Yes.

Q83 **Lord Blackwell:** As you have heard, a lot of the evidence has been about how some of the regulators in other territories are nimbler and more responsive. In particular, we have heard about specific examples of the ILS and captives markets being inhibited in the UK because of the regulatory approach. Do you agree with that assessment on ILS and captives? Are there other examples you can point to of products or services where the regulatory approaches inhibited the UK? Is it fair to compare the UK with other jurisdictions? Is there anything unique or distinctive about London that means it is inevitably going to be a heavier regulatory burden?

David Sansom: I will touch on ILS. You have heard a lot about this, so I will not repeat the issue and the statistics, but I will share our perspective at Lloyd's. We set up an ILS structure recently with the PRA. It approved it. That enables us to bring ILS investment into our Lloyd's market. The good news bit of the conversation is that we worked very actively with the PRA to set this up. I agree that its intention is to support and develop this. When you look at the experience of investors who have had conversations with us through this process, you get back to the same set of basic challenges about how burdensome that process is.

Just to bring that to life a little, those investors in the UK in an ILS structure like the one that we have at Lloyd's are required to produce, in effect, a full set of application documents right at the start of the process, almost as a gateway into the process, in contrast to other jurisdictions that would have a summary. In those other jurisdictions, throughout the

process they would develop the rest of the documentation. That allows the regulatory bit of the process, the development of the business plan, and the core application documents to take place in parallel to the rest of the workstreams—getting the capital in place and getting the investors lined up—whereas in the UK a lot of that has to happen at the start to get that big tranche of documentation.

An approximate estimate would be that, under the UK model, that adds an additional eight to 10 weeks of process, and that, of course, has a cost. Particularly for these types of deals, speed is so important. That is an example of the type of process changes that could be made, possibly learning from some of the lessons from other jurisdictions. I do not think those other jurisdictions would say that they have a less robust regime to get into the door, but they might work more actively and earlier with the application investor in the process to get them through it in a more efficient way. That would be some of our experience.

Lord Blackwell: Are there other examples, apart from ILS and captives, where you have found that a regulatory regime in the UK inhibits development of new products or services?

David Sansom: We touched on it earlier in the conversation around climate and the transition towards net zero. One of the mechanisms we have set up at Lloyd's is an incubator—a lab—to help those types of ideas and businesses develop. We tried to give those innovative businesses access to the market—to underwriters and the brokers, and to us at Lloyd's as the overseer.

There is more that regulators could do—we talked about the sandbox—with those types of incubators and innovation mechanisms to support business, in particular around green innovation. I mentioned the example of the other international regulator that challenged me on what more Lloyd's was doing to help them in their jurisdiction. If I compare that to a conversation with the UK regulators, I do not think I have had a conversation where they have asked me what products and services we are developing and what they can do to help. The conversation has all been around, "How are you managing the climate risk?" That is a critical part of it, but it is only half of the conversation.

Lord Blackwell: Richard, do you want to comment?

Richard Dudley: I will, thank you, but less so on the ILS side, on the prudential side. Things like the insurance-linked securities market are important not just in and of themselves; they are symbols of the attractiveness of our regime for the supply of capital, which in turn provides balance sheets, which can then provide protection against risk, which is what my colleagues and I are interested in for all our clients around the world. It is very important to think of it in the context of the whole ecosystem and not just a single new idea that somebody had. It is a very important part of the overall provision of capital.

On the point that David made at the end, take Bermuda as an example. As we speak, there is a risk summit in Bermuda at the moment, which is being held by the Bermuda Business Development Agency. It is not their regulator, but the regulator is present, as is the Premier of Bermuda, to talk with industry representatives from all around the world, including from here in the UK, about how Bermuda is thinking through the next stage of where it sees its business environment going and the opportunities that exist for international firms in Bermuda. It is holding a similar summit in May specifically about climate, where all those constituents will be equally represented and all will be speaking on panels together in a way that you do not necessarily find in the UK.

That is another example where you see a more pragmatic and collaborative approach across the firms that are being regulated, the regulators themselves, the Governments and international development agencies as a collective, as opposed to all doing their own thing.

Lord Blackwell: Can I ask you the question I asked in the previous session? To what extent is the regulatory approach here a function of the quality and experience of the people in the supervisory teams? David, you have referred a number of times to the need for judgment in good regulation. Judgment requires people who have the confidence and knowledge to cut through. If you do not have that, you tend to fall back on detailed information requests and not being precise about your questions in case you get them wrong. Do you have any views on whether we would be better served with fewer but higher-quality people in the regulatory teams?

David Sansom: I think it is about judgment. I do not think it is a case of fewer and higher quality; it is a case of higher quality all round. That goes back to experience. From our perspective, thinking about our supervisory team, we have a very experienced team. It is a mix of individuals who have been at the regulator for some time, so they understand the regulatory process. We have ex-industry practitioners, including some who have recently come in from industry having had quite a long career in industry who are now supervisors. The revolving-door idea that we talked about earlier exists, and we get the benefit of that mixed team.

As I said, when we have had to step back ourselves and think about how we can apply more judgment, we have had to recognise that it is cultural, and it will require some mechanisms—things like training—just to help people think a little differently.

Back to the conversation on the objective, having that competition objective will allow supervisors to apply a broader lens to their conversation. It might be the case that they feel a bit limited because of the structure of their current objectives. That might free up the conversation a little bit. That would have to be reinforced through the obvious things like training and development. I do not have a broader concern around the capability. It is just a case of that cultural shift.

Lord Blackwell: Would you like to add to that, Richard?

Richard Dudley: I have only one point to add. You talked about a revolving door in a positive sense there from David, but there is also one that is less positive, certainly for us when we are regulated by the FCA. We quite often find that the case officers or the people who are regulating us change on a very regular basis. On one level we understand that, of course, because you do not want the supervisor to become too familiar with the firm they are supervising, but at the same time it means that we quite often have to go back to the beginning almost every year to explain ourselves in a way that we feel we have done a number of times previously. I do not think that is necessarily a quality issue. It might be part of the culture that exists within the FCA at the moment, which we talked about earlier, which is fairly risk averse generally.

Q84 **Baroness Bowles of Berkhamsted:** I want to come back with one quick question. Do you think that the regulators perceive lack of growth and not being able to build your books quickly enough as a risk that then challenges their primary objective?

Richard Dudley: That is a really good question. If you took the competitiveness objective to an extreme version of the argument, you would argue that without it you might not have a sustainable market, full stop, which underlines the comment that you are making. I honestly do not know how the regulator thinks about it from an FCA perspective. We do not interact with the PRA at all. David, do you want to comment on the PRA?

David Sansom: It goes back to some of the previous conversations we have had about the mindset of the conversations. Again, I will use the example of the international regulator that asked me the two questions in the one meeting. It comes back to having that properly embedded.

To the suggestions that there are separate competition units in the regulator, although that certainly will help in the development of things like a new captives regime, it is the front-line supervisors who need to have both sets of the conversation. It is not just, "How are you managing the risk?", and then a separate team comes in next week to say, "How are you getting on on innovation?" It is joining up those two aspects in that front-line supervision that is important.

The Chair: Gentlemen, that brings our session to an end. I would like to say thank you very much for what has been a very interesting and stimulating contribution this morning and this afternoon. With that, I can say that the meeting is now closed. Thank you.