HOUSE OF LORDS
Industry and Regulators Committee

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6 April 2022

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Economic Secretary to the Treasury
HM Treasury
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Dear John,

Commercial insurance and reinsurance regulation

Thank you for giving evidence to the Committee on 31 March 2022 as part of its inquiry into commercial insurance and reinsurance regulation.

Our inquiry raised a number of important issues around the regulation of the commercial insurance and reinsurance provided through the London Market, one of the UK's most important industries, representing 23 per cent of the City's GDP. We were pleased to hear that the London Market continues to thrive despite the increasing market shares of competitors such as Bermuda and Singapore and that the regulatory regime itself is highly respected. However, we heard differing views on whether an apparently inflexible application of that regulatory framework is a barrier to future success, the view of much of the industry, or part of the attraction of a stable, world-leading market, a view outlined by the regulators and your own evidence.

In particular, we heard that the industry is concerned that the regulator takes a one-size-fits-all approach to commercial insurance and reinsurance, requiring London Market firms with sophisticated clients to comply with unnecessary consumer protection requirements that are aimed at the retail insurance sector. The industry argued that this is sometimes due to rules being applied too generally across the sector, but alternatively can arise when regulators are insufficiently clear on the scope of regulation. We heard that this lack of proportionality can hinder the development of new forms of insurance in the UK, such as insurance-linked securities, due to delays in the UK's regulatory processes, where other jurisdictions have found greater success with fast-track methods and a more welcoming regulatory environment.

Industry witnesses also described what in their view is a very demanding regulatory regime, involving a significant body of requirements and large numbers of information requests – requests not always appropriate to the firms receiving them – and meetings with the regulator, particularly when compared with other jurisdictions. They also argued that the regulators take a risk-averse approach and operate very bureaucratic systems, contrasting this with other

jurisdictions that manage to operate high regulatory standards in a more pragmatic, business-friendly way.

In particular, industry witnesses highlighted that regulators in other jurisdictions, notably Singapore and Bermuda, seek to support new businesses through difficult and complicated regulatory processes by means of collaborative, open dialogue. This was contrasted with the approach of the UK regulators, who were said to be more likely simply to point new businesses to a website and ask them to make their own judgement on the requirements.

This difference in approach was also described in relation to stakeholder and practitioner panels that the regulators operate, with witnesses suggesting that these panels – particularly in the case of the FCA – are selected by the regulators and meet in relative secrecy, with meetings often consisting of the regulator outlining its approach rather than taking on feedback from stakeholders. It was pointed out that the Monetary Authority of Singapore has an advisory panel consisting of senior business leaders and academics to whom the regulator can put policy questions, providing the benefit of this expertise in the development of policy. The UK industry would likely benefit if UK regulators would adopt a similar and more collaborative approach.

Despite these concerns, we recognise that it is important to distinguish between dissatisfaction with the outcome and dissatisfaction with the process; in those cases in which the industry did not secure its preferred outcome, this is not always necessarily a sign that the process was poorly run.

The PRA and FCA stated that they aim to act in a proportionate manner and take into account their impact on the industry. However, it is understandable that they focus on their current statutory objectives, which prioritise safety and soundness and make no reference to competitiveness. The industry's proposed solution to the issues they outlined is a competitiveness objective for the regulators, encouraging them to be less cautious and requiring them to give greater thought to their impact on the industry. However, many industry witnesses argued that the Government's proposal for a secondary competitiveness objective for the financial regulators, which you set out in your evidence to us, may be insufficient to bring about the necessary cultural and operational change, with many arguing for a primary competitiveness objective.

The PRA and FCA argued in favour of a secondary objective, suggesting that this would allow them to take competitiveness into account without compromising the safety and soundness of the financial system. Witnesses from the regulators suggested that they would try to take competitiveness into account when assessing the impact of new rules. However, some from the industry argued that this mindset constitutes part of the problem, suggesting that a competitiveness objective should require the regulators to review the entire stock of regulation currently in place in order to ensure that high standards are maintained in as efficient a way as possible, rather than only focusing on the additional impact of new regulations.

Many industry witnesses called for clear metrics to be set out around how this objective is to be achieved alongside some form of annual reporting to drive cultural change within the regulators and to allow others to hold them to account. We heard suggestions that this could include comparing numbers of new applicants, entrants, flows of capital and services to the UK market with other regulated territories each year, reviewing UK regulators' performance

relative to other major regulators, and monitoring the UK's performance against international metrics.

We share the PRA and FCA's view that the primary objective should continue to be the safety and soundness of firms. Indeed, we agree with those who emphasised that a robust and rigorous regulatory framework contributes to the both the competitiveness and the reputation of the London Market and would be concerned at any initiative which could unintentionally dilute this.

We also agree that there are strong arguments in favour of adopting a secondary competitiveness objective but note that this alone may be insufficient. It is vital that the concerns regarding the inflexible and sometimes unnecessarily complex processes require a broader reassessment of regulatory culture. There is a need for current rules to be applied more proportionately and efficiently and objective-setting for staff at all levels to support this. The FCA and PRA should regularly review their rulebooks to ensure that they are maintaining high standards in the most efficient way possible to enable the competitiveness of the UK financial industry; such reviews should focus on the scope for more efficient and proportionate as well as less cumbersome and mechanistic engagement between regulators and industry. The PRA and FCA should consider formalising such reviews on a regular basis.

Open and transparent communication with industry is also important. Regulatory stakeholder panels should be fora for two-way dialogue, allowing the industry to provide its views on regulators' performance as well as providing the regulator the opportunity to communicate its own plans. This communication should include opportunities for constructive challenge from the industry concerning policies under consideration and also explanations of the underlying reasons for adopting various policies and not only their content. Discussions in stakeholder panels should also be more transparent and public, allowing those who are not panel members to be aware of the content of the discussion. The PRA and FCA should regularly look at other successful financial centres to develop and sustain best practice.

Regulators in other jurisdictions have some form of competitiveness objective; this shows that others believe that there are ways of adding such an objective to regulators' remits without compromising safety and soundness. In the event that regulators were to be given such an objective, we share some of the concerns expressed by industry witnesses that without objective criteria for success it would be difficult to hold the regulators to account for meeting the objective. There is a risk that it could be ignored or have no material impact on the operation of the regulatory framework, due to the current risk-averse culture within the regulators.

Consequently, we recommend that alongside introducing a competitiveness objective for the PRA and FCA, it will be essential to establish clear criteria and appropriate performance measures. The evidence we heard suggested that industry practitioners have some ideas for what such measures might be and would be a useful source. Publicly disclosed performance criteria would provide an opportunity for both the Government and Parliament, through this

Committee and others, to monitor performance and hold the regulators to account.

We welcome your agreement on the importance of strengthening the role of parliamentary committees in holding regulators to account as they are granted greater rule-making powers. We will consider issues of remits, responsibilities, performance measurement and accountability more generally in our forthcoming inquiries and look forward to your response to outline the Government's thinking in this area.

I have sent copies of this letter to the Chief Executive Officer of the Prudential Regulation Authority and the Chief Executive of the Financial Conduct Authority.

Yours sincerely,

Lord Hollick
Chair of the Industry and Regulators Committee