Lloyd's of London – Written evidence (SCG0022)

Lloyd’s is submitting this letter in response to the Financial Services and Regulation Committee’s call for written evidence into the secondary international competitiveness and growth objective given to the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) under the Financial Services and Markets Act 2023.

Lloyd’s is a (re)insurance market based in London. All insurance at Lloyd’s is written by Lloyd’s members, organised into 101 syndicates, managed by 52 managing agents. In 2023, the Lloyd’s market’s gross written premiums totalled £52.1bn. The business written in the Lloyd’s market is primarily non-life (re)insurance.

We are supportive of the secondary mandate that the Financial Services and Markets Act 2023 introduced for UK financial regulators to advance economic growth and international competitiveness, and welcome the new remit letters issued by the Chancellor to the FCA and PRA this month that call for the greater embedding of the mandate in the regulators’ policymaking and supervisory responsibilities. We believe the mandate is important in fostering a culture of innovation and reasonable risk-appetite that is integral to growth of the UK’s financial services sector.

Lloyd’s enjoys a collaborative and constructive relationship with regulators and government. Lloyd’s has been pivotal in assisting Government respond to recent systemic events, from fronting the Live Events Reinsurance Scheme as the UK recovered from the COVID-19 pandemic, to the establishment of the Black Sea Grain initiative to prevent potential famine due to the Ukraine / Russia war, to providing insurance solutions around the rescue of a tanker (SFO Safer), preventing potentially one of the largest environmental disasters in history. On this precedent, we always stand ready to work with the government now, and in the future, to prepare for, and to mitigate the worst effects of, other events with systemic and large-scale impact.

Regarding our own approach as a regulator of the Lloyd’s market, we have established a principles-based oversight regime that directly mirrors the ambitions of the regulators in creating a wider principles-based regulatory system in the UK that can promote innovation, growth and competitiveness, while upholding strong supervisory standards.

Moreover, the PRA, both in its recent decision to lower 15 managing agents’ supervision categories, as well as its close work with Lloyd’s on developing London Bridge – a new platform at Lloyd’s that enables investors to access our market through using insurance linked securities – has taken noticeable steps in reducing unnecessary duplication within the London insurance market, which is a positive for the growth and competitiveness of the wider industry. We are fully supportive of such measures and hope to see more such initiatives in the future.

We hope that our answers to the questions below are helpful to the Committee. We would be happy provide further written detail on any of these points should that be necessary.

1. What opportunities or changes should be prioritised in order for the regulators to meet their secondary growth and competitiveness objectives effectively?

Regulators engaging with firms regularly is essential. The PRA and FCA have both demonstrated aptitude in doing so, particularly in the FCA’s its recent review of wholesale insurance markets, and the PRA’s industry expert groups for the Solvency UK changes. FCA colleagues approached Lloyd’s and other industry stakeholders a year ago to discuss how to improve UK wholesale insurance market regulation, noting that they wanted to address industry concerns about disproportionate requirements in UK wholesale insurance regulation.

Moreover, the FCA has held a range of workshops and discussions with industry stakeholders since August 2023 to inform the policy options set out in the FCA’s Discussion Paper (DP24/1), which contains positive proposals and helpfully invites some open-ended comments from firms. This policy reform process was open, transparent, and informed by industry feedback throughout – we encourage the FCA to continue to approach its work in this way which will be to the benefit of meeting the new secondary mandate.

Lloyd’s did not agree with the FCA’s initial proposals to publish details about enforcement proceedings at a very early stage in enforcement investigations. While we are supportive of the FCA’s overarching desire to introduce more transparency to its enforcement investigations, the risks and costs associated with the early publication timeframe proposed were very likely to outweigh the benefits in increasing transparency, making the proposals disproportionate. We recognise the FCA has considered feedback from industry following consultation with stakeholders, and look forward to reviewing the revised proposals.

The PRA and Lloyd's both regulate the Lloyd's market and work closely to do so, supported by a Cooperation Agreement. The PRA have stated their intention is to continue to leverage Lloyd's oversight work and move to more collaborative work on oversight. We have already seen the tangible benefit of this in the announcement of the PRA's reduction of the regulatory category, and by extension, the intensity of its oversight for 15 managing agents. The work on an Authorisations Pilot, whereby Lloyd's is collaborating with the PRA to design a more efficient process to enable managing agents to receive authorisation and begin trading in a significantly shorter period, is another example of attempts to reduce duplication and supervisory burden. The PRA showing a high level of interest and being proactive in supporting the pilot. Along with its close work with Lloyd's on developing London Bridge, we think this shows good willingness from the PRA to promote growth and competitiveness and it will reduce unnecessary duplication in the financial services sector.

We also support the PRA's aspiration to increase confidence that firms can exit the insurance industry with minimal disruption, in an orderly way, and without having to rely on the backstop of an insolvency or resolution process.

However, we do not believe that requiring solvent exit planning for insurers in the terms proposed by the PRA (CP2/24) is a competitive measure in the context of the Lloyd's market. To implement such a proposal would only serve to duplicate and complicate the equivalent mechanism which already exists and is regularly used, and which takes account of both the potential for solvent exits and for the market's unique characteristics.

Applying the PRA's proposals to the Lloyd's market is also likely to produce only more cost, with no associated marginal benefits, and would therefore be disproportionate. Moreover, and most significantly in the context of this consultation, introducing such requirements would damage the competitiveness of the Lloyd's market: managing agents would need to undertake additional duplicative requirements compared with firms outside of the market, facing higher running costs without any obvious additional benefit. As such, the current proposals *should not* be applied to the Society of Lloyd's, its members or managing agents.

Lastly, we would also like to comment briefly on Solvency II reporting and its relation to competitiveness. While we are strongly in favour of previous HM Treasury feedback that they would work with the PRA to enable changes to the Solvency II rulebook to ease burdens on regulated firms by reducing reporting and administrative requirements, having carefully reviewed the PRA's final rules on how to adjust Solvency II reporting requirements, we do not believe they go far enough to achieve HM Treasury's core objective of reducing the reporting burden. This is in contrast with, for example, the European Union's stated desire to reduce reporting by 20%.

When considering HM Treasury's stated aims for the Review of Solvency II and the regulators' new competitiveness mandate, we think it would be a shame if the UK did not seize this opportunity to be more ambitious in materially streamlining Solvency II reporting and crafting a Solvency regime that is better tailored towards the unique features of the UK's insurance sector.

5. How effectively have the FCA and PRA consulted or engaged with industry in relation to the new secondary growth and competitiveness objective?

We welcome the PRA's original commitment that the mandate would have a "material influence" on its policymaking. We envisage that following the new remit letters issued by the Chancellor, a more proactive and strategic approach will be required to embed the competitiveness mandate within the PRA's policy making and supervisory responsibilities.

The way in which supervisory teams require firms to demonstrate compliance with a rule often has a great impact on competitiveness. In responding to the new remit letters, the PRA should not just consider its policy making function, but also review whether their supervisory processes (e.g. the time it takes to process regulatory authorisations, or the culture of supervision) are designed to advance UK competitiveness.

We would suggest the following measures to boost competitiveness more generally:

- **Early consultation**: In keeping with the PRA's commitment to ensure early engagement with firms on policy issues, we urge the PRA to discuss or consult at the start of the PRA's policy development phase, as soon as the PRA has decided that a change in policy is needed. The Solvency UK subject expert working groups were an example of good practice, and we support a similar approach when consulting on major policy changes in the future. External stakeholders would be better equipped to provide helpful feedback on policy proposals if they could respond to those proposals at an early stage in the policy development cycle.

- **Practitioner Panels:** We welcome the PRA's proposals to "facilitate wider information sharing" from Industry Practitioner Panels. We encourage the PRA to consider allowing other designated technical experts within the firms of Panel members to sign NDAs with the PRA and thus be free to discuss selected Panel proceedings with Panel members. This will enable Panel members to bring a wider range of expert technical views to Panel meetings and strengthen the PRA's policymaking process.

- **Regulatory culture**: We welcome the PRA's drive to shift its regulatory culture, including by launching internal training on how to deliver more competitive regulation. Since proportionate supervision is a necessary precondition for delivering a more competitive regulatory regime, we urge the PRA to ensure that the training sessions focus on proportionate supervision just as much as competitive policymaking.

- **Cost benefit analysis (CBA)**: Rigorous CBA, conducted at a phase in the policy cycle when there is still an opportunity to change the direction of policy, is essential. We agree with the feedback that the PRA has received to date, that CBA should consider the costs not only of regulatory measures, but also the cumulative costs of all new regulations entering into force in a particular time.

- **International co-operation**: We welcome the PRA's commitment to working with international regulators, and, where appropriate, making equivalence assessments. Following the success of HMT, PRA and FCA in negotiating the Berne Financial Services Agreement, we encourage the PRA to also pursue mutual recognition assessments where appropriate. Furthermore, we encourage the PRA to engage with a range of industry and government stakeholders when gathering information about the UK's international competitiveness.

As a regulator ourselves, we understand the complexities involved in delivering regulation that is robust, prudent, and competitive, and welcome the PRA's efforts to achieve this objective. We believe that our experience in delivering a supervisory framework that protects and promotes the Lloyd's market has given us a unique perspective on how to navigate these issues.

In particular, as part of our new way of overseeing the Lloyd's market – our shift to a principles based system of oversight - we looked to differentiate how we oversee firms through a risk based approach. Firms that meet and outperform the requisite standards are given further support to grow and innovate while firms outside of our robust standards receive the appropriate regulatory scrutiny and guidance. In this way, we aim to foster an approach that cultivates sustainable innovation and is contributory to the market's long term competitive advantage.

In particular, our tracking of innovation in the Lloyd's market is utilised significantly by providing discrete platforms that host different kinds of innovative products, and monitoring the successes of products on those platforms

The Innovation ICX is a new Lloyd's risk code that syndicates in the Lloyd's market can use to write up to an additional 2% of Syndicate Business Forecast GWP of innovative business. We report annually on the amount of GWP written annually under the ICX risk code.

6. **In delivering their secondary objective on growth and competitiveness, what opportunities are there for the regulators to help to promote and support innovation in the financial services sector? How effective has the FCA's regulatory sandbox been for supporting greater innovation in the financial services industry?**

We welcome the PRA's commitment to using its rule-making powers in a way that is supportive of "innovation" (CP27/23 para 2.8). However, we note that the PRA does not see innovation as one of the three ways in which it can best influence UK competitiveness – those methods are "capital allocation", "ability to sell", and the "ability to attract" capital (CP27/23 para 2.17). We would urge the PRA to keep a close eye on how far its regulations are impacting the levels of innovation taking place in the UK's financial sector, since the success of competitiveness strategies ultimately comes down to how far they promote innovation. While we appreciate innovation is not directly under the PRA's control, regulators can 'nudge' firms to consider their innovation strategies.

We fully support the PRA's commitment in the CP to draw on "practical supervisory experience" when trying to further the competitiveness mandate. Supervisors have a unique standpoint from which to promote innovation. For example, if senior supervisors were to ask firms about their innovation strategies, and how regulation could support innovation, in PSMs, they would prompt firms to consider their innovation strategies and gather information about how regulation can spur innovation. Such information could then inform regulatory policymaking efforts.

We would encourage supervisors to report annually (qualitative reporting) on the key learnings about innovation that they have taken from their conversations with firms and explain how those conversations informed policymaking.

As stated the previous answer, at Lloyd's, we track innovation in our market by providing discrete platforms that host different kinds of innovative products, and monitoring the successes of products on those platforms. 'Innovation ICX' is a new Lloyd's risk code under which syndicates in the Lloyd's market can write additional innovative business of up to an additional 2% of Syndicate Business Forecast GWP. We report annually on the amount of GWP written annually under the ICX risk code.

Additionally, "London Bridge" is a new platform at Lloyd's that enables investors to access our market through using insurance linked securities. Investors noted that they were finding it difficult to set up insurance linked securities in the UK because it was hard to get regulatory approvals for them. We worked successfully with the PRA to create pathways to authorise insurance linked securities at Lloyd's, and new investors are now accessing our market through these innovative products. This is a great example of how regulators can support innovation and attract new investment to the UK's financial sector by ensuring smooth regulatory authorisations.

Finally is the Lloyd's Lab, a successful technology accelerator and our innovation hub, which brings together InsurTechs and start-ups with underwriters, brokers and investors.

We recognise that we need to nurture later stage innovators as well as start-ups. That's why, once firms have graduated successfully from the Lab, they can still base themselves at the Lab, or at Lloyd's offices in New York and Singapore, free of charge, for as long as they want, and attend several networking events with insurers. The Lab is now on its 11th cohort and previous graduates have gone through the full journey to partnering with market participants.

We know that regulators are exploring creating a similar UK "scale box" to further support innovation and look forward to hearing more about this vital initiative.

29 November 2024