Written evidence submitted by the London Market Group

Introduction

The London Market Group (LMG) welcomes the opportunity to contribute towards this inquiry and would welcome the opportunity to set out our thoughts in additional detail by providing oral testimony to the Committee.

The London Insurance Market leads the world in providing specialty commercial insurance, with $110bn of Gross Written Premium in 2018 held in the Market on behalf of customers across the world, making it one of the UK's major export industries. This international business and foreign investment come to the UK because we have a unique market which pools risk and capital and is not replicated anywhere else in the world. The key strength of the London Market is its ability to provide clients with global policies to cover all of these risks.

The success of the market is key to maintaining the UK's competitive position and will play a significant role in growing our exports and delivering increased levels of foreign inward investment as major financial organisations seek to participate in the London Market.

In May, the London Market published its third *London Matters* report, a regular piece of analysis undertaken by the London Market Group to assess the health of the market and its global position. It's latest findings include:

A major force in the UK economy, contributing £37bn to UK GDP in 2018, up from £32bn in 2015. This represents a quarter of the City of London's total GDP

A major employer, employing 47,000 skilled workers not only in the City of London, but across the United Kingdom.

One of the most productive sectors in the UK, with a full-time equivalent (FTE) contribution to GDP more than four times the UK average.

Playing an important and often under-appreciated role in strengthening the resilience of local economies after catastrophic events, with claims payments resulting in $181bn of investment across the world since 2015.

Responsible for $110 billion (re)insurance business, via over 350 firms and with business derived from over 200 territories.

Bigger than all its nearest rivals combined - Zurich, Bermuda and Singapore - and has over 60% and 52% market share of the global aviation and energy markets respectively, and over one third of the marine market.

Income from North America (US and Canada) increased 6% between 2010-2018, meaning it replaced the UK and Ireland as the biggest source of income. It was also the fastest growing region during the period.

Emerging markets are increasingly seeking cover for more complex risk. This should provide the London Market with opportunities for such business.

The points below summarise our position:

We welcome and support a number of elements of HM Treasury's Future Regulatory Framework (FRF) Review consultation and have also recommended a number of further reforms to the Committee, that we believe would ensure that the London Market remains competitive within the global marketplace and fully contributes to the UK's economic prosperity in the future. We believe these will be of interest to the Committee:

- We welcome an **activity-specific approach to regulation** which allows for public policy considerations to be part of the regulatory framework - such as promoting the export value of financial services business and encouraging inward investment as part of the UK's future international trade and investment strategy;
- This is also an opportunity to **recognise the differences between industries, such as the services they provide and the nature of their clients and customers** within the broader financial services sector;
- **A more proportionate approach to individual sectors within the insurance industry and the type of client they serve would help contribute to the UK's economic recovery by boosting competitiveness and making the market more attractive to international investors;**
- Given the increased powers that the UK regulators will have it is very important that the Government **strengthens the accountability framework** regarding their decision making. We would specifically like to see **an earlier, more formal and more meaningful consultative role for industry, particularly in the policy development process of the regulators;**
- We strongly urge the Government to consider how **international competitiveness considerations can have a more prominent role within our regulatory framework.** This will help to send a positive message that the UK is an attractive place for new investment and trading opportunities and is not incompatible with strong, proportionate regulation;
- The UK must continue to be a **welcoming and open market for overseas firms** seeking to trade in the UK. This is particularly vital for the London Market, given that over 66% of capital in the market is from overseas and much of it from Europe; and
- We welcome the commitment within the consultation to **maintaining the UK's alignment to international regulatory standards** and continuing to be a leading country in the development of those standards. Clients and investors in the London Market see adherence to these international standards as a benefit of doing business in the UK.

Response to the Consultation questions

Q1. How can the UK financial services sector take advantage of the UK's new trading environment with the rest of the world?

Commercial insurance and the London Market will play a leading role in the UK's future trade success. The strength of the UK commercial insurance market is that it is truly international. Its success is driven by international trade and encouraging foreign direct investment.

Without commercial insurance, international trade and commerce becomes impossible: planes cannot take off, ships cannot leave harbour and major infrastructure does not get built.

The industry is one of the UK's most successful export industries:

- For specialist lines, the London Insurance Market is bigger than all of its competitors combined – Bermuda, Singapore and Zurich.

- It attracts large commercial business via over 350 firms and with business derived from over 200 territories around the world.
- A major employer, employing 47,000 skilled workers not only in the City of London, but across the United Kingdom.

Business comes to the UK commercial market from all over the world seeking coverage for risks which are too large and/or complex for their domestic markets. It comes to the UK because we have the skills and expertise to underwrite that business and an industry with scale and diversity. The risks are mostly overseas but the activity and the capital required to (re)insurer them are in the UK.

Insurance has **significant economic benefits for the UK's international trading partners**:

The London Market can play a critical role in supporting the economic development of countries across the world, growing trade in existing markets and opening new ones and the growth potential is significant:

- Insurance has a positive economic impact: a 1% rise in insurance penetration translates into a 13% reduction in uninsured losses, a 22% reduction in taxpayers' contribution following a disaster and increased investment equivalent to 2% of national GDP.[1]
- The global insurance protection gap remains significant, despite general global economic growth in recent years. The global underinsurance gap is now estimated to be US$162.5 billion, a reduction of just over 3% since 2012.[2] The UK Market can therefore help countries to close these gaps and build their resilience.
- Many (re)insurers in these emerging markets are not sufficiently diversified, have limited skills to manage complex risks, and an insufficient capital base. The UK can help them to spread those risks globally and thereby strengthen their own domestic insurance markets.

The London Market has a strong base from which to build but we must maintain the UK's competitive position, as other international insurance hubs continue to grow.

The London Market Group's research has highlighted that the London Market is in danger of falling behind other growing international insurance markets such as Switzerland, Singapore, Hong Kong and Bermuda.

These markets are seeking to make their regulatory environments as attractive as possible and in some cases actively benchmarking their regulatory regimes against other locations, in the hope of pulling investment away from the UK. Their insurance markets are seeing significant growth – **Singapore has an annual growth rate of 4%, Switzerland 1.7%, Hong Kong 10.2%.**

While the UK's share of mature insurance and reinsurance markets remains stable, more work is needed to gain access to high growth emerging markets.

- The London market continues to perform strongly in established insurance markets, with income from the US and Canada increasing by 6% points between 2010 and 2018, **making North America now the largest source of premium for the UK market.**

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[1] Lloyd's:https://www.lloyds.com/news-and-risk-insight/news/lloyds-news/2018/02/protectionism-a-risk-to-latin-america-insurance-growth

[2] Lloyd's: A World at Risk, 2018

- However, the **UK needs to gain better access to high growth emerging markets** - particularly markets in South East Asia and Latin America – which is vital if the London Market is to maintain its share of global specialty commercial insurance.

- **Asia remains the highest growth market globally but was the region in which the UK has lost most ground** in commercial insurance, mainly to growing regional insurance hubs, most notably Singapore which has seen an annual growth rate of 4%.

- **Growth in competition from overseas**, especially Bermuda, Singapore and Switzerland where governments are supported by regulators who actively promote their insurance markets to clients and investors.

Given this worrying trend of loss of global market share by the London Market it is particularly important that both Government and industry consider what measures can be introduced to reverse this trend, ensure regulation is proportionate, encourage more trading opportunities and crucially promote this UK industry.

Q2. What changes should be made to the UK's financial services regulations and regulatory framework once the UK is independent of the European Union?

There is currently a gap in the FSMA model. It does not allow for Ministers, parliament, and the industry to have a significant enough say in how the regulators operate. Nor does it allow for any early input into regulatory changes and policy decision making, and it contains no mechanisms for censuring the regulators if they fail to follow the policy objectives that have been set for them.

This is not just a case of reforming the formal regulatory rulemaking process, but also a question of considering the regulators' supervisory behaviour, which can have just as detrimental an impact on the industry and the attractiveness and competitiveness of the UK market for investors.

For example, the significant number of 'CEO letters' – as well as 'CRO' and 'Chief Actuary' letters, of which there have been four active letters in the last 12 months requiring operational changes from the market – together with policy statements, thematic reviews, ad hoc data requests and even speeches made by senior officials of the regulators. All of this has created a significant body of regulatory requirements and expectations essentially leading to regulatory modifications outside of the more formal rule book. These expectations have layered new requirements on the industry without appropriate and independent checks and balances, creating a significant burden for firms.

This policy formulation necessarily creates a response requirement within the regulated community, requiring firms to respond as if they are regulatory rule changes, as these communications often reference regulatory action or consequences. There is no prior scrutiny of these communications, they are often published without prior notice and there is no recourse to challenge these measures. This does not create the right degree of transparency or accountability.

We also believe that the development of a UK specific framework also offers the opportunity to **undertake a consolidation of the different sources of regulation**, which are located in different places and require significant institutional knowledge to navigate. Currently regulations affecting the London Market can be found in multiple sources including the FSMA legislation, various statutory instruments, the onshored EU legislation, the regulatory rulebooks of the FCA and PRA and supervisory statements.

Consolidating this and placing all the information, categorised by market sector, and accessed via a '*one stop shop'* section of the regulators' websites, would not only be a straightforward way of reducing burdens on firms seeking to find, understand and comply with all the necessary regulation but also make it easier for overseas firms seeking to do business within the UK.

Solvency II Review

Solvency II has brought significant benefits and strengths to the London Market – particularly Pillar II risk management - such as a strong balance sheet; networks of international licences that facilitate access to markets and the ability to write global programmes; and an internationally well-regarded system of regulation that encourages transparency.

We therefore do not support wholesale changes to the regime but would like to see certain refinements to the UK regime and for some of the unnecessary requirements, specifically regarding processes on calculation and validation of capital requirements; reporting requirements; and treatment of branches of overseas firms - to be scaled back to what is actually important to clients, supervisors and firms.

The PRA has the ability to do this within the current framework and without compromising its own compliance with the regime or the prospects of a subsequent equivalence ruling with the EU.

Making wholesale amendments to the UK's implementation of Solvency II could seriously reduce the likelihood that the EU will find the UK to have an equivalent third country regime. This will be important for harmonising reinsurance market access across the 27 member states.

The UK should avoid market fragmentation, ensuring that it continues to work towards international regulatory convergence, which eases cross border trade of (re)insurance services. This is something highly valued by international clients coming to the London Market. An exercise to re-design the UK's insurance solvency system will require UK insurers to embark on new and potentially large programmes of operational and systems change. We believe that there is little market appetite for this.

International Competitiveness Duty for the regulators

As the UK takes up a more global role outside of the EU, regaining sovereignty over its regulatory rule book gives us the opportunity to ensure that the UK remains the world's global financial services hub, facilitating business and creating growth across all four nations. We believe this is best achieved by ensuring that our regulators are mindful of our competitive position globally, through an international competitiveness duty for the regulators. We have elaborated upon this argument in answer to question 12.

Q3. What should the Government's financial services priorities be when it negotiates trade agreements with third countries?

The future UK trading regime should seek to encourage open markets for large commercial risks., building on the UK's strength as an open economy attracting international investment and talent. This can be achieved by seeking to ensure the removal of local restrictions, mutual recognition of rules and standards, and greater regulatory cooperation.

- The **UK Government should take the opportunity to develop an approach to third countries based on the concept of cross-border (mode 1) access** for services under the General Agreement on Trade in Services (GATS).
- **The regime should be outcome-based and trade should not be prevented by technical regulatory divergence** between the UK and other third countries if the achieved outcome of the regulation is the same.
- The **UK should be proactive in opening up international insurance markets** based on mutual market access, home state supervision and no host state financial requirements.

The challenge is that many economies have in place local restrictions on the amount of reinsurance that can be bought from overseas providers and prevent entirely the UK Insurance Market providing primary insurance.

The Global Reinsurance Forum (GRF) regularly reviews and compiles information on trade barriers to the provision of commercial insurance services across borders. The **GRF has identified 45 major territories**[3] around the world which have either implemented, or are in the process of implementing, barriers to the transfer of risks through global reinsurance markets. Many of these countries and territories are target markets for the UK. The barriers identified by the GRF include:

- **Requirements for UK reinsurers operating on a cross-border basis to localise their assets**, preventing the firms from transferring and spreading risk on the basis of a competitive, level playing field across borders.
- **Restrictions on foreign ownership** of subsidiaries and other barriers to the establishment of branches, subsidiaries and operations. This restricts the ability of insurers to deliver their full economic benefit by providing local underwriting expertise and direct services to transfer risk out of domestic markets on an open and competitive basis.
- **The use of discriminatory and anti-competitive mechanisms** such as systems of 'right of first refusal', and compulsory, subsidized or monopolistic governmental mechanisms limiting the competitive ability of UK insurers to operate on a level playing field.

Much of this does not necessarily need a formal free trade agreement and the UK Government and regulators can make progress now by using the full range of tools available to them, in the form of Financial and Financial & Economic Dialogues, High Level Talks and regulatory working groups, that it has with target markets, to take forward these discussions and promote the insurance market.

The UK Government therefore needs to work with the industry and representative bodies such as the London Market Group, to present a case to reduce these barriers which focuses on the value that the Market can deliver for those countries and their businesses.

[3] https://www.grf.info/publications/barriers-to-trade

Q4. Should the UK open its financial services markets to external competition from countries outside of Europe, or should the UK maintain the current regulatory barriers that apply to third countries?

The UK regime provides a robust, sensible and proportionate regime for dealing with third-countries. The restrictions to foreign participation in the London Market are non-discriminatory and exist to ensure that firms cannot operate without sufficient approval and regulation.

Government should be mindful that most jurisdictions will seek reciprocal benefits. The UK has a relatively strong commercial presence in insurance, so the benefits of market liberalisation in the sector may appear a little one-sided. However, one of the benefits of the UK and particularly London, is the fact that the large specialty risks both domestic and international come to London. This means new entrants can leverage expertise here rather than deploying additional talent in a number of dispersed jurisdictions which makes it an attractive location in which to grow business.

The UK should be proactive in promoting the opening-up of international insurance markets based on mutual market access, home state supervision and no host state financial requirements. The London Market is a substantial net exporter of services, so it is very much in the UK's national interest to maintain open markets worldwide. This will ensure that London Insurance Market firms can continue to meet and respond to overseas commercial insurance and reinsurance needs either on a cross-border basis or by way of local branches.

Q5. What skills and immigration policy will the UK financial services sector need once the UK has left the European Union?

The unequalled pool of global talent and expertise assembled in the UK is a major competitive advantage for the commercial insurance industry. To retain its status as the leading global centre, the UK needs continued access to the best talent, a mixture of home-grown, from across the EU and from the rest of the world. Future UK immigration policy should be designed to broaden the future pool of international talent that the industry can access. It must also facilitate intra-company transfers of staff between different locations around the world.

In particular, EU nationals working in the London Insurance Market should be reassured that they will be able to continue to remain in the UK post Brexit, whilst new talent should not be deterred from coming to the UK by the uncertainty of their future status. The UK must not impose quotas or other barriers which inhibit the movement of the highly skilled and diverse workforce the London Insurance Market requires to work effectively on an international basis.

Q6. How can Government policy and the UK regulators facilitate the emergence of FinTech and new competition; develop new areas of growth for the financial services sector; and promote the UK as the best place to incubate new financial technologies and firms?

Clients come to London because of its ability to design products to meet their complex requirements for global risks. They also look to London to create new solutions designed to cover their emerging risks. This ability to design and develop new approaches – which the London ecosystem in uniquely structured to support – requires a flexible regulatory approach.

To help achieve this we would like to see an expansion of the FCA's Sandbox approach to regulated activities by the PRA, which would make the UK a more attractive place to develop new products and services, by both existing and new entrants to the market. This would create a conducive and contained space where innovations at the edge of, or even outside of, the regulatory framework can be tested. This is an approach we believe would have benefited and sped up the development of an Insurance-Linked Securities market. Such an approach would bring down costs of innovations and reduce barriers to entry, while allowing the UK regulators to collect valuable information prior to approval.

We believe there are a range of activities that the regulators could undertake to evidence their commitment to maintaining the UK as an attractive and competitive place to do insurance business:

- **Regular benchmarking** of the UK's regulatory regime against other key financial services locations.
- Playing an **active role in enhancing the reputation, competitiveness and future sustainability** of the UK as a world leading financial services centre – similar to the duty of the Swiss regulator FINMA[4].
- The regulators should also be expected to consider their role in **encouraging inward investment to the UK**, perhaps through a dedicated inward investment unit to provide more proactive support and guidance to overseas firms seeking to come to the UK and trade within the London Market.
- **Reporting requirements** which require the regulators to evidence how they have contributed to maintaining the UK's competitiveness internationally.

Q8. What role does Parliament have to play in influencing new financial services regulations?

We welcome the scrutiny function provided by the Committee, as well as the former House of Lords Financial Affairs Sub-Committee and now the work of the House of Lords EU Services Sub-Committee.

While both committees do consider financial services as part of their remits, we note there is now an absence of a Committee (or sub-Committee) specialising and focusing exclusively on financial services. We would welcome the formation of either a joint Commons and Lords Committee, or a dedicated Sub-Committee to the Treasury Select Committee, to consider financial services more regularly and in greater depth. A new financial services committee could provide a more focused forum for ongoing scrutiny of the work of the regulators.

The new Committee - perhaps comprised of members of both Houses, ideally drawn from members of the Treasury Select Committee and the EU Services Sub-Committee - could look in detail at specific pieces of financial services regulation. We would propose that the Joint Committee or Sub-committee have the following powers and attributes:

- **More regular scrutiny of senior figures within the regulators on specific policy considerations** and regulatory changes as well as the more general strategic discussions that currently take place.
- It would also **need to be resourced with expert staff and advisers to aid parliamentarians with the technical input that would be needed** to properly hold the regulators to account. The support that the US Government Accountability Office[5] provides to Congressional committees, as set out above through annual audits of financial services regulations and

[4] FINMA Annual Report 2019

[5] U.S. GAO - Financial Services Regulations: Status of GAO Recommendations to Enhance Regulatory Analyses and Interagency Coordination

their efficacy, could be a resource that would be helpful to UK parliamentarians and could perhaps be delivered through the UK National Audit Office.

- The committee should **establish an annual review of the performance of the regulators** against the public policy priorities that have been set for them and make recommendations to the Government, particularly where the committee has concluded that objectives have not been met.
- Inquires of the committee should **ensure that regulatory action is consistent with the public policy goals set out in the legislation**. This would give key stakeholders a parliamentary forum in which trade-offs between financial services regulatory policy and other public policy goals could be properly considered and debated.
- **Pre-legislative scrutiny of certain financial services regulation** could also be a valuable role to allow for proper scrutiny of any major new regulatory proposals and complement the existing processes for scrutinising and approving secondary legislation within both Houses.
- We believe it would need **some power of intervention over the regulators**, which could at least require them to publish specific information such as impact assessments and cost/benefit analysis, to allow for further scrutiny and evidence to be considered before a decision is implemented.

Q9. How should new UK financial regulations be scrutinised?

While we understand the Government's desire to delegate powers to financial regulators, it is crucial that sufficient accountability frameworks are in place to ensure decision-making takes into account the broader context of the global trading environment, particularly in respect of innovation, consumer demand and competitiveness.

New scrutiny mechanisms must also have the ability to challenge the regulators if it can be shown that regulatory changes would be detrimental to the UK market, contrary to their statutory or public policy objectives or out of step with international best practice.

HM Treasury's FRF Review consultation document suggests a number of options for adapting stakeholder engagement with the policy making process and we have given our views on how they should be reformed:

- **Significant reform of statutory panels:** London Market Group member associations do participate in one of the statutory panels, the Practitioner Panel. However, the Panels are essentially controlled by the regulators, as they set their terms of reference and the scope of their meetings. They must have far greater independence from the regulators, and the power to undertake far more detailed and expert scrutiny of specific areas of regulation, as well as additional powers to allow them to hold the regulators to account and ensure that regulatory changes are fully justified. The Panels must also be required to engage more closely and regularly with the industry and its representative bodies. Currently decisions are taken behind closed doors. In the future the Panels should be required to produce publicly available agendas and minutes of its meetings to bring greater transparency and accountability to their deliberations.

- **Introducing more systematic and independent review of regulator rules:** In order to be effective these *ex-post* reviews would need to be evidence based and would need to allow for recourse or challenge if it was felt that the conclusions of the ex-post review were inaccurate or lacked the necessary evidence base.

- **Greater scrutiny of international engagement undertaken by UK regulators:** The UK should also continue to engage with multilateral regulatory bodies such as the International Association of Insurance Supervisors (IAIS) to develop common international principles for insurance regulation. Now that the UK has left the EU, it is important that it adopts an even more visible position within the key global standard-setting bodies, continues to be a leader in these bodies and works to help continue to build international standards and approaches to regulation. We would like to see a more effective and systematic mechanism for holding the regulators to account in international discussions, particularly to ensure that the regulators have discussions with industry representative bodies at an early stage in the process. We would also suggest that the engagement of HM Treasury in these international fora should be increased to help ensure greater accountability.

Industry representation and input

A dedicated forum for domestic regulatory changes and to ensure an ongoing and formal dialogue between Ministers, HM Treasury, the regulators and industry. For such a forum to be successful and to ensure proper and meaningful industry engagement, we would ask the Government to consider the following attributes:

- The forum should have the ability to proactively raise issues directly with Ministers and officials regarding the impact of proposed regulation and regulatory policymaking, before it takes effect.
- The forum would also allow the industry to bring forward proposals for market development and new initiatives to expand the UK financial services offer. For example, the London Market Group would be keen to discuss regulatory reforms to make the UK a more attractive location for captive insurance companies.
- The forum should have sight of and the ability to comment on major proposed regulatory changes prior to those changes coming into force.
- It should have access to data and impact assessments produced by the regulators to justify proposed regulatory changes and the ability to comment on them.

More broadly, we would suggest the following changes could be made to involve industry and strengthen the policy making approach of the regulators, thereby further strengthening the accountability mechanisms on the regulators' actions:

- Regulatory changes tend to be made on a piecemeal basis, with cost/benefit analysis undertaken solely on the basis of each individual change, without taking into account the cumulative costs that industry faces. To strengthen accountability, we would like to see **UK regulators publish cumulative cost/benefit analyses of the impact of regulatory changes**, so London Market firms can best understand the total costs for ensuring compliance.
- **Regulatory changes should be 'packaged up' to come into force on set dates of the year.** Given the London Market is led by brokers and based on a subscription model, considerable time and resources are needed to negotiate system and compliance changes across the market. Having a set number of days when regulatory changes come into force would ensure London Market firms can become compliant with new regulations more easily.
- In order to be effective ***ex-post*** **regulatory reviews need to be data-driven and would need to allow for recourse or challenge** if it was felt that the conclusions of the *ex-post* review were inaccurate or lacked the necessary evidence base.
- **Industry must be involved more formally in regulatory consultations.** Regulators should commit to meet and discuss regulatory changes – and the potential impact of them - with

representative bodies before publishing formal consultations and in advance of any regulatory change.

Q10. What progress has the Government and regulators made in facilitating key financial services equivalence agreements with third countries; and would an alternative mechanism serve the interests of the UK market better?

In terms of developing its own regime for post-Brexit commercial insurance trade the UK should actively push for greater market access, regulatory dialogue and the removal of trade barriers; ensuring that domestic regulation and competition are sufficient and proportionate to achieve prudential goals, without sheltering anti-competitive and discriminatory regulation.

The open nature of the London Market means that using an equivalence framework as a tool to manage reinsurance trade with other third countries - through a regulatory measurement as a condition for market access - is not the preferred solution.

Instead, the assessment should be outcome-based; it should assess to what extent the respective third-country regulatory and supervisory framework achieves similar and adequate regulatory effects and to what extent it meets the same objectives as the UK. Trade should not be prevented by technical divergence between the UK and other third countries if the achieved outcome of the regulation is the same.

Importantly, engagement with third countries should be conducted on a case-by-case basis, in respect of the intricacies of territories' commercial insurance regulations. For example, in many cases, Free Trade Agreements (FTAs) may not be the most optimal tool and the UK Government should use the full range of tools available, including economic and financial dialogues, regulatory cooperation, multilateral trade talks and market promotion.

We would instead suggest that the UK regime seeks to have the following high-level structure, the details of which can then be further negotiated with individual countries depending on the specific nature of those discussions and markets:

- **Reducing local presence rules and granting market access rights:** Brokers and insurers should be able to trade freely cross-border, allowing brokers to have direct contact with clients in third countries and carriers to write business on a cross border basis.

- **Home state supervision:** Building agreements on international prudential standards should allow UK brokers and (re)insurers trading overseas to rely on home state supervision.

- **Regulatory cooperation:** There should be mutual transparency and cooperation between home state regulators, provided that such cooperation does not prevent either party from diverging, nor allow such divergence to act as an immediate trigger to loss of recognition.

- **Dispute resolution mechanisms:** Disputes should be settled in a dispute settlement mechanism by an independent tribunal as is included in most modern FTAs. This will ensure financial market stability and investor protection. For this reason, we support many of the UK Government's proposals within the Framework for the UK-EU partnership: Financial Services, published in August 2018.

A regime built on this structure would allow the UK to cooperate with other countries and businesses that achieved similar regulatory outcomes reached in a similarly transparent manner. Ultimately this could provide countries with a growing (re)insurance demand for access to the

London Insurance Market and its world class expertise in developing and managing large and complex policies. While this may not lead to the formal convergence of international regulatory regimes, we believe it will help to promote recognition of approaches based on achieving similar regulatory outcomes.

Q12. Should the mandate and statutory objectives of the financial services regulators change to include wider public policy issues?

International competitiveness

The emergence of new centres of capital in places such as Singapore, Dubai and Miami and has significantly increased the number of markets able and willing to write risks that previously might have had no choice but to go to London. While these new centres do not currently have London's depth of knowledge or expertise, they are a lot cheaper to operate in. Over time our concern is that these new centres will become far more viable alternatives and compete for premium, putting further pressure on London's share.

It is the London Market Group's belief that **international competitiveness should have a more prominent role within our regulatory framework**. The London Market Group believes that the regulators' statutory objectives should be expanded under the new framework.

The London Insurance Market is a truly international, export driven industry, attracting large commercial and specialty business from over 200 territories around the world. The London Market's strength lies in encouraging inward investment. Over 66% of the London Market's business relies on foreign capital. The London Insurance Market needs to ensure it is the most attractive and competitive place globally to retain existing clients and keep attracting new business.

International insurance and reinsurance hubs in Bermuda, Switzerland and Singapore are **regulated by bodies mandated to promote their domestic markets, ensure they are attractive places to do business and promote the reputation of those markets**. These markets are seeking to make their regulatory environments as attractive as possible and in some cases actively benchmarking their regulatory regimes against other locations.

- In Switzerland, the **Swiss Financial Market Supervisory Authority** is required to take "*into account the repercussions for the sustainability and international competitiveness of the Swiss financial centre.*"[6]
- The **Monetary Authority of Singapore (MAS)** works to ensure that Singapore's financial services industry remains competitive by engaging with governmental agencies and financial institutions "*to promote Singapore as both a regional and international financial centre*." To facilitate this the MAS may draw upon a Financial Sector Development Fund to develop regulatory and infrastructure systems.
- The **Hong Kong Monetary Authority** has a duty to promote Hong Kong as an international financial centre through market development initiatives that strengthen the international competitiveness of Hong Kong's financial services.[7]
- In Bermuda, part of the mission of the **Bermuda Monetary Authority** is, "*to protect and enhance Bermuda's reputation and position as a leading international financial centre*."[8]

[6] https://www.finma.ch/en/finma/activities/regulation/
[7] https://www.hkma.gov.hk/media/eng/publication-and-research/annua-report/2017/05c_About_the_HKMA.PDF
[8] Bermuda Monetary Authority: https://www.bma.bm/the-bma-s-role

Differentiated regulatory approach

We believe a **more stratified and proportionate approach to individual sectors within the insurance industry and the type of client they serve would be beneficial and aid UK international competitiveness**, with separate models for personal lines, commercial lines and reinsurance which reflected the nature of the risks of these different sectors. Individual consumers and SMEs will still need consumer like protection but large corporate clients who have their own professional brokers and advisers need much less.

We would welcome a regulatory approach which recognises the nuances between the different insurance markets that operate within the UK and allows the regulators to develop regulatory models which can better support these valuable markets, allowing them to deliver wider benefits to the UK economy and international investment.

As part of deepening the activity-specific approach, we would welcome further consideration of recognising within the public policy considerations for the regulators, **the distinction between commercial insurance and reinsurance brokered and underwritten in the London Market, and personal lines business**, which differ significantly in nature and could have different regulatory objectives.

The commercial insurance market, including the London Market, is of a fundamentally different character to that of the domestic life and pensions market. Clients seeking insurance for large risks are significant firms with strong risk management capability who either employ internal expertise or procure reliable external advice. Clients' interests are almost always represented by professional brokers throughout London Market placements. This enables them to make an informed choice as to their insurance provider and the structure of their programmes.

The London Market is also more international in character, bringing clients and investors from across the world into the UK. Its strength lies in its concentration of capital and expertise which draws business to London from around the world. This ensures the London market makes a material contribution to the UK's exports and in encouraging inward investment into the UK. Much of this investment comes from EU entities - over 66% - who choose to do business in London. That capital and expertise is mobile, the international insurance market is highly competitive and the impact of regulation is inevitably a factor in both the perception and the reality of the UK as a place to do business.

Below we have set out three examples of how the UK regulators' current 'one size fits all' approach is affecting competitiveness and investment in the London Market.

- **Conduct risk and regulation of London's commercial specialty intermediary market:**

In interpreting its current FSMA objectives the FCA makes almost no distinction in the way it supervises a London market specialty broker serving a corporate client, from the way it supervises a retail insurance broker dealing with an individual's domestic and motor insurance requirements. As the FCA's own Wholesale Insurance Broker Market Study in 2019[9] demonstrated, corporate clients seek specialist broking services because they recognise that the advanced expertise housed within broking firms can assist them in reaching the optimal outcome for their risk management programme and deliver the right value for any insurance purchases they may make as part of that programme. These are not consumers in need of protection in the way that individuals or SME

[9] MS17/2.2: Wholesale Insurance Broker Market Study - Final report (fca.org.uk)

customers may be. In particular, we believe that the nature of London's commercial specialty intermediary market must be better recognised and reflected within the statutory framework and the FCA's future objectives, to ensure that a proportionate level of regulation is undertaken. Finding a structured, risk-based and proportionate solution that works for brokers operating in specialty markets is critical to the whole of the London Market's continued success.

- **Regulation of overseas reinsurance branches**: The reinsurance market, which sees many overseas firms coming to the UK to create a branch to do business within the London Market. The PRA chooses to treat pure reinsurance branches similar to direct insurance branches which goes beyond the requirements set out in Solvency II. This includes duplicating requirements already set by the home state regulator of the reinsurer. The clients of this reinsurance branch are other insurance companies and the branch is fully protected by the Group company. Given the cross border nature of reinsurance we are concerned that continuing such an approach will make the UK less competitive and we will lose further ground as a centre for the reinsurance market.

- **Captive insurance companies**: Captives[10] writing risks of their parent or of entities that are part of the group are also treated like insurance companies with no recognition within the UK's regulatory system of the low risk that they present to the financial system. Due to this approach no company has chosen to set up a captive in the UK despite our extensive financial services eco system. This includes many UK public sector bodies such as Transport for London, the Corporation of London, the Nuclear Decommissioning Authority and Network Rail which have all chosen offshore locations for their captives due to the uncompetitive position of the UK. In contrast a number of jurisdictions, including EU jurisdictions such as Ireland, take a proportionate or 'differentiated supervisory approach'[11] to these low-risk companies reflecting the nature of the risk that they are writing.

Q14. How can the balance between lighter touch regulation and prudential safeguards be best secured?

The London Market Group is **NOT** seeking a reduction in UK regulation or a dilution in UK regulatory standards. We believe that Solvency II, a system which the UK was instrumental in developing, should continue to be the basis of UK insurance regulation to avoid damaging market fragmentation.

International clients and investors see adherence to these standards as a benefit of doing business in the UK. A client will come to the London Market because they can get the global insurance cover they need for commercial activities such as aviation, shipping or global property portfolio in one market from the world's leading experts.

Q15. How should consumer interests be taken into account when considering potential regulatory changes?

As outlined in response to question 12, we believe a **more stratified and proportionate approach to individual sectors within the insurance industry and the type of client they serve would be beneficial and aid UK competitiveness**, with separate models for personal lines, commercial lines and reinsurance which reflected the nature of the risks of these different sectors. Individual

[10] Definition: a captive is an alternative to self-insurance in which a parent group or groups create a licensed insurance company to provide coverage for itself.

[11] [Central Bank of Ireland, Corporate Governance Requirements for Captive Insurance and Captive Reinsurance Undertakings 2015]

consumers and SMEs will still need consumer like protection but large corporate clients who have their own professional brokers and advisers need much less.

This distinction is recognised by many of the international jurisdictions the London Market operates within such as the EU and US states. Large commercial risk is recognised within the EU's regulatory framework, including the Solvency II legislation[12], and is also a distinction made by many US states within their regulatory regimes, with similar concepts known as 'industrial risk' and 'sophisticated commercial buyers'.[13]

The concept of a 'professional client' is also well recognised, with a clear and consistent definition provided within the FSMA framework, the regulatory handbooks[14], and the on shored EU legislation.[15]

We would also point the committee to the consumer research[16] published as an appendix to the FCA's Wholesale Insurance Broker Market Study in 2019, which highlighted that sophisticated clients who understand the complexity of specialty insurance markets, understand the specialist expertise that they get access to by hiring a broker and are clear how and how much they pay their broker and consider it excellent value for money.

These examples emphasise that many key jurisdictions, as well as the UK, acknowledge that firms writing risks for commercial clients for sophisticated corporate clients, do not require the same regulatory measures as those products and services designed for a retail client.

The London Market Group

The London Market Group is the only body which speaks collectively for all practitioners in this significant market, representing the views of insurance brokers, those insurers and reinsurers operating within Lloyd's, and branches of overseas insurers and reinsurers operating in London – reflecting the full extent of the Market.

This submission reflects the perspectives of the International Underwriting Association of London (IUA), the Lloyd's Market Association (LMA) and the London & International Insurance Brokers' Association (LIIBA) and Lloyd's of London.

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[12] Article 13
[13] Locke Lord: Surplus Lines - Locke Lord LLP
[14] COBS 3.5 Professional Clients, FCA Handbook
[15] Article 4(1)(10) MIFID