Daryl Collins
Chief Operating Officer Unit
Prudential Regulation Authority
20 Moorgate
London
EC2R 6DA

4 May 2016

Dear Daryl,

AFM Response to Consultation Paper CP10/16, *Regulatory fees and levies: rates proposed for 2016/17*

1. I am writing in response to this consultation paper, on behalf of the Association of Financial Mutuals. The objectives we seek from our response are to:

   - Comment on the proposals and highlight a discrepancy in the approach that creates a disproportionately higher cost for smaller mutuals.

2. The Association of Financial Mutuals (AFM) represents insurance and healthcare providers that are owned by their customers, or which are established to serve a defined community (on a not for profit basis). Between them, mutual insurers manage the savings, pensions, protection and healthcare needs of over 30 million people in the UK and Ireland, collect annual premium income of £16.4 billion, and employ nearly 30,000 staff[1].

3. The nature of their ownership and the consequently lower prices, higher returns or better service that typically results, make mutuals accessible and attractive to consumers, and have been recognised by Parliament as worthy of continued support and promotion. In particular, FCA and PRA are required to analyse whether new rules

[1] ICMIF, http://www.icmif.org/global-mutual-market-share-2013

impose any significantly different consequences for mutual businesses[2].

4. AFM is pleased to respond to this consultation on behalf of its members; we have restricted our comments to the general fairness of the allocation of costs rather than the scale of the budget overall.

5. The main shortcoming of PRA's approach to budgeting is that the budget is established without direct reference to the work that PRA expects to undertake. In the past, FSA would generally publish its business plan for the next 12 months alongside the draft fees consultation, as FCA does now. This makes it easier for external stakeholders to reconcile costs for each sector against the activity being undertaken, and therefore to assess value for money and fairness. Without knowing what activities PRA is planning it is very difficult to comment on the apportionment of costs for 2016/17.

6. The consultation also implies (in paragraph 1.9) that the fees a firm pays will vary according to the number of fee payers: this further indicates that PRA's costs are relatively fixed irrespective of the number of feepayers, and therefore that costs do not vary according to the amount of work to be undertaken. This impression is further reinforced by the approach to Solvency 2 implementation. The consultation proposes that the costs of implementation are normalised in the future: indicating that the work was treated previously as neither specifically for implementation, nor as a Special Project.

7. The two paragraphs above suggest fees are set according to the number of staff PRA employ, and do not take proper account of the amount of work to be undertaken, or its allocation across sectors. With an annual budget of over £250 million this appears to be a very crude approach, and supervisors would reasonably question this approach if a firm allocated costs in such a rudimentary fashion.

8. There is also a significant flaw in the logic that increasing the fees across all firms in fee blocks A3 and A4, by the amount of the Solvency 2 'special project' fee, is fair. These fee blocks include a number of mutuals with gross premium income of less than £5 million, but more than the level for the minimum fee: £5 million is the lower threshold for inclusion in Solvency 2.

9. Previously insurers outside the scope of Solvency 2 did not pay the additional Solvency 2 SPR. Under the proposed allocation approach for 2016/17, non-directives with income above that which applies to the

[2] Financial Services Act 2012, section 138 K: http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted

minimum fee will now see their fees increase pro-rata by around 12% more than other insurers. This will include some mutual insurers, and the assumption that this replaces the fee and costs incurred for Solvency 2 implementation, implies there is no expectation of a commensurate increase in regulatory activity to match it.

10. This means the statement in paragraph 7.5 is invalid, as small mutuals in particular would witness a disproportionate increase in fees. We regret that PRA continues to disregard its obligations under FSMA s138K, as we have pointed out regularly in recent consultation responses. This in turn undermines the statement in paragraph 7.2, as it increases barriers to survival and expansion for smaller organisations, contrary to PRA's secondary competition objective.

11. We suggest that PRA establishes a single fee rate for all non-directive insurers, at the level of the minimum fee. This will also ensure any further fee increase, designed to reflect higher PRA costs for regulatory reporting (where proven, and above the incremental costs to fees brought about by incorporating the Solvency 2 Special Project Fee into business as usual), is not passed on to non-directive insurers that are outside the scope. As per paragraph 1.12, we will reflect on this further if, as proposed, PRA consults on reporting costs later in the year.

12. We would be pleased to discuss further any of the issues raised by our response.

Yours sincerely,

Chief Executive
Association of Financial Mutuals