By email to: SolvencyIIReview@hmtreasury.gov.uk

HM Treasury
1 Horse Guards Road
London SW1A 2HQ

15 July 2022

AFM Response to HMT consultation on its review of Solvency 2

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 their consequences for members of AFM;
- Highlight concerns about the limited proportionality in the proposals.

About AFM and its members

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 over £20 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 impose any significantly different consequences for mutual businesses[2] and to take account of corporate diversity[3].

[1] ICMIF, https://www.icmif.org/publications/market-insights/market-insights-uk-2016 with updates from EY and AFM
[2] Financial Services Act 2012, section 138 K: http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted
[3] http://www.legislation.gov.uk/ukpga/2016/14/section/20/enacted

AFM comments on the proposals

4. We welcome the latest consultation on the review of Solvency 2. The Solvency 2 Directive has provided a cross-European standard, and a vital safeguard during uncertain times; the focus on policyholder protection has avoided any significant failures amongst UK insurers.

5. However, this protection has come at a cost: UK insurers are over-burdened with regulatory expectations, many of which have been ineffectively transposed from the rules for deposit-takers, that in turn were implemented in haste after the financial crisis. Regulatory costs have soared, and this has accelerated the move away from pure insurance operations by the biggest players, and which has contributed to the shrinkage of the insurance sector. In the US, Oliver Wyman reports that banks, insurance companies and asset managers, which accounted for 90% of financial services industry value 10 years ago, have seen a precipitous fall to 65% today[4]. The balance is made up of technology and financial infrastructure companies, which in the US as well as the UK enjoy a much less capital-intensive regime. The structural change in the insurance sector is likely to be similar in the UK, and reform is important therefore to address those anomalies, and as a result to ensure the market remains competitive and for it to work in the best interests of all consumers.

6. The proposals in the consultation plot an imaginative course for how the insurance sector in the UK can thrive post-Brexit. It is vital that the government achieves the right balance between removing unnecessarily burdensome aspects of Solvency II, whilst maintaining a proper degree of policyholder protection. If that balance is found, the proposals offer potential benefits both to the UK insurance market- from lower costs and greater competitiveness; and to the UK economy- from the injection of new investment into infrastructure projects.

7. We agree with the positive view the consultation offers on a post-Brexit insurance market in the UK. Much relies however on even-handed and effective implementation: whilst these proposals set out plans for a lower cost of operations for the UK insurance market outside the EU, the benefit is severely tempered by a significant rise in PRA's fees for insurers, which have increased by 20% since the UK's withdrawal from the EU in early 2020.

[4] https://www.oliverwyman.com/our-expertise/journals/state-of-financial-services.html?utm_source=exacttarget&utm_medium=email&utm_campaign=sofs&utm_content=23-may-2022&utm_id=cmp-13626-l8l8c1

8. For most mutual organisations, higher regulatory costs are not matched by the savings offered via the reforms proposed in this consultation. Higher PRA costs must be passed onto policyholders, which in turn means raising charges or reducing benefits. Hence, early implementation of changes that benefit the whole UK insurance sector and their policyholders will be vital, to offset the higher regulatory costs we have seen so far, and which contradict efforts to demonstrate a Brexit dividend.

9. The consultation does not provide an expected implementation date for the proposed changes to the risk margin and matching adjustments. If the expectation is that the changes to Solvency 2 form part of the Financial Services and Markets Bill, as set out in the Queen's Speech, then given regulatory rule changes and transition, full implementation could take until 2024. We would encourage Treasury and the PRA to explore what changes to the current regime can be made in order to realise some benefits for year-end 2022.

10. Our response focuses mainly on the commentary in Chapter 5 of the consultation, where there is greatest scope for proportionality, and for benefit to AFM members and their customers. We are disappointed that the consultation has given such little consideration to reform beyond the risk margin and matching adjustments. This is particularly the case given that in paragraph 1.8 of the 2020 Call for Evidence, Treasury commented that it is 'particularly important to ensure an appropriate regulatory system that meets the needs of small and medium-sized insurance firms, including new entrants to the market, thereby boosting competition'[5].

11. It does not feel like this consultation addresses this, and whilst PRA has indicated it will consider a simplification of the regime for smaller insurers 'after the completion of the government's current review', it is disappointing that this was not considered relevant to the current Treasury review, and also that this pushes out those '*particularly important'* changes out to 2024/25[6].

[5] www.gov.uk/government/publications/solvency-ii-review-call-for-evidence
[6] www.bankofengland.co.uk/prudential-regulation/2022/april/pra-business-plan-2022-23

12. We have responded to the specific questions raised in the consultation below, and would welcome the opportunity to discuss further the issues raised by our response.

Yours sincerely,

Martin Shaw
Chief Executive
Association of Financial Mutuals

AFM responses to questions raised in the consultation

Question 2.1 How would a reduction in the risk margin for long-term life insurers toward the bottom or top of the 60%-70% range impact on:

- policyholders and their level of protection; and
- insurers and their reinsurance, investment and product pricing decisions.

The performance of the UK insurance sector, both during the pandemic, and in the 2008/09 financial crisis, with no marked failures despite the volatility of the situation, is evidence of the strengths of the sector, both financially and operationally. However, we consider there is currently a greater degree of caution built into the Solvency 2 regime than is needed to provide policyholder protection. For mutual insurers, the level of capital held is often much greater even than that required by regulators, due to the conservative approach taken to managing a business where there is no recourse to shareholders in the event of a shortfall in capital.

In our opinion, a more effective basis for setting the risk margin would be universally welcomed by insurers. The consultation highlights just how sensitive changes in the amount of capital required are to changes in the level, methodology and adoption of the risk margin.

Recent research by actuaries and consultants OAC for AFM reviewed the Solvency and Financial Condition Reports of 27 AFM members and other small insurers[7]. OAC assessed the total risk margin for all companies in the review, and the impact of the proposed reform, as per the following chart.

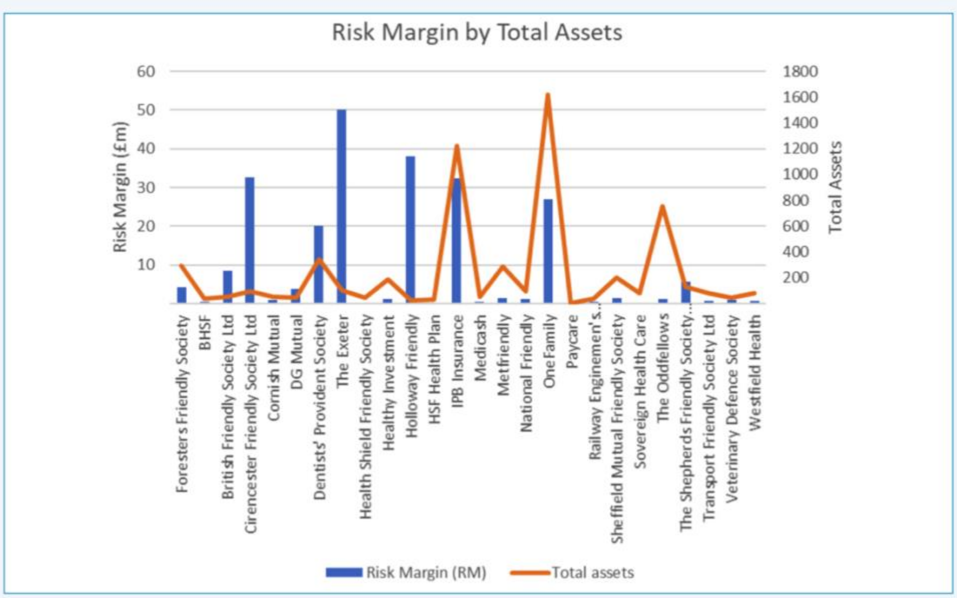

Chart 13:
Risk margin compared with Total Assets (£m)

Scottish Friendly Assurance Society Ltd, with assets in excess of £5bn, has been excluded from Chart 13 to allow a more proportionate comparison for the majority of the group analysed.

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[7] https://financialmutuals.org/wp-content/uploads/2022/06/SFCR-Analysis_2021.pdf

The total risk margin across the sector is £280m, with £190m relating to life business (incorporating health insurance contracts written as long-term business). On average, the risk margin is 20% of own funds for life businesses, and 4% for non-life. There is significantly variability though, with a range of 2% to 49% amongst life businesses.

The Treasury consultation, coupled with PRA's recent discussion paper (DP2/22), states that the proposed reforms could result in a reduction in the risk margin of around 60% for long-term life business and 30% for non-life business. On this basis, and assuming 45% reductions for composites, this could reduce the risk margin for the population included in OAC's report by £150m.

That is a welcome reduction for small businesses, though as inferred above, the impact will vary considerably. Indeed for some businesses the consequences may be negative.

To illustrate, some AFM members and other smaller life insurers sell shorter term life business, such as Group life protection. In these cases, it has been predicted that the Risk Margin would materially increase as a result of the revisions to the approach being explored[8]. Moreover, with closed books in run-off, the life sector could be negatively impacted if the outstanding durations are sufficiently low. For a large insurer, the gains on the Risk Margin will outweigh the losses, but for some small businesses the net impact could be negative. In a recent meeting PRA indicated that the reforms should leave no-one behind, but it is important the review takes account of any unintended or negative consequences.

The boundary between the review of Solvency 2, and other prudential rules has a significant impact. PRA supervisory statement SS4/18[9] sets the requirement for firms to have a solvency risk appetite in excess of 100% of Solvency Capital Ratio (SCR) coverage; the expectation is that this excess capital buffer is set on a "1 in X" basis, where X is typically 10 or 20 years (as opposed to the 1 in 200 years on which the SCR is based). As a result, the PRA expectation adds a further capital buffer onto the capital buffer implied by the SCR – often leading to companies setting themselves the target of holding (say) 150% of SCR. The PRA will monitor performance against this heightened buffer, and taking a strong interest if solvency dips below this level.

We think it is conceivable that if the Solvency 2 review of the Risk Margin leads to a 20% improvement (say) in a firm's SCR coverage ratio, the PRA could use SS4/18 to get the firm to push up its solvency risk appetite, to absorb some or all of the 20% gain. Since the solvency risk appetite is a private calculation, it would

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[8] See WTW analysis presented to the ABI, page 68, link here

[9] https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2018/ss418)

be difficult for a firm to resist this. We think it is important that the reform process builds in safeguards to resist this, or the use of other regulatory tools, to diminish any benefit from the reduction in the Risk Margin.

Question 2.2 How would a reduction in the risk margin for general insurers of 30% impact on:

- policyholders and their level of protection; and
- insurers and their reinsurance, investment and product pricing decisions.

We agree that the calibration will need to be different for general insurers, for the reasons described in the paper. And as we highlight for short term life contracts, they would also benefit from different calibration to long-term business.

Question 2.3 Do you agree that a modified cost of capital methodology should be used to calculate the risk margin?

We agree, for the reasons set out in the consultation.

Question 2.4 Is there any further information about actual transfer values of insurance risk that should be taken into account when finalising the calibration of the risk margin reforms?

The consultation references the consequences of a change to the Risk Margin on other aspects of risk management in an insurer, and the general additional benefit that would result. This includes the impact on reinsurance, the capacity to take advantage of the Transitional Measures on Technical Provisions (TMTPs), and the opportunity for life insurers to reinsure longevity risk in the UK. As most members of AFM have not benefited from these past provisions, the overall impact will be more muted. This is due to their scale rather than business model, and it is important that the government takes proper account of proportionality, and the consequences for competition, in its final response.

Question 2.5 How could the Government be assured that resource that becomes available following a reduction in the risk margin would not be distributed to shareholders or used to increase remuneration to parties within the insurance firm?

The consultation indicates that the changes to the Risk Margin could free up a very significant sum. Were that money to be simply released by insurers to their shareholders, the net outcome would be a massive outflow of funds from the UK economy- since the average UK listed company now has around two-thirds of its shares owned overseas[10]. It is likely though that any special dividend would be subject to PRA review as part of its normal scrutiny, and we cannot comment on the likelihood or impact of that, as we do not represent shareholder-owned companies.

By contrast, mutual insurers are in a different position. As their ownership is almost entirely by UK citizens, whether the capital released is invested in infrastructure

[10] https://www.theguardian.com/business/2021/jun/07/foreign-investors-own-66-of-uk-listed-shares-analysis-shows

projects; or retained in the business to increase the level of new business written; or used to enhance returns to policyholders, all those funds would be retained within the UK.

With regard to executive incentives or similar, these are ordinarily based on P&L activity. We are not aware of any long-term incentives that are directly correlated with the release of dividends, so it is not the case that the release of tied up capital will be released to remuneration arrangements. For AFM members in any event, most have limited or no executive incentives.

We are happy to contribute to discussion on how most of the 'Brexit dividend' from this reform is put to good use in the UK economy.

Question 3.1 Taking into account the fundamental spread methodology needing to be sufficiently responsive to changes in investment decisions and reflect long-term exposure to credit risks, do you agree with the above assessment that the current methodology does not:
• sufficiently address the risks associated with assets with the same credit rating but different market measures of retained risks; or
• take account of all the risks associated with holding internally rated or illiquid assets?

Question 3.2 What is the impact of the fundamental spread including a credit risk premium of 25, 35 or 45% of spreads on life insurers':

Question 3.3 What is the threshold for any increase in the fundamental spread above which adverse effects become significant, such as excessive balance sheet volatility or increased reinsurance of risks off-shore?

Question 3.4 What is the impact on policyholder protection of a credit risk premium of 25, 35 and 45% of spreads, when accompanied by a risk margin reduction for long-term life insurers of 60-70%?

Question 3.5 What is the impact of selecting an averaging period (n) of 0.5, 1, 2, 5, 10 and 30 years?

Question 3.6 Are there other ways to achieve the same impact that changes to the fundamental spread would have?

The Matching Adjustment currently has limited applicability for our members given the nature of their liabilities. In cases where it might be applicable, any benefits derived are unlikely to outweigh the additional monitoring and administration required to continue to apply the adjustment.

Question 4.1 What would be the impact of these reforms on insurers' use of the matching adjustment and investment:

- in economic infrastructure, such as clean energy, transport, digital, water and waste;
- to support the transition to net zero, either allocation of capital to support the development of new green technologies or to support adoption of green solutions; and
- in any other asset classes.

Question 4.2 What are the additional risks that these reforms may pose to policyholder protection?

Question 4.3 What safeguards are appropriate to protect policyholders from the risks posed by allowing a wider range of assets into matching adjustment portfolios?

Question 4.4 What impact will these reforms have on insurers providing a greater range and more affordable pricing of products?

Question 4.5 What changes to the matching adjustment approval process are necessary to ensure that applications to use the matching adjustment are approved more quickly?

We note that Chapter 4 of the consultation is largely given over to consideration of how different investment options can be included within matching adjustment portfolios. As per our response on Chapter 3, the changes proposed here are largely intended to benefit larger insurers, who currently make use of the Matching Adjustment; we have though offered some general observations.

We support actions that enable insurers to better sustain a range of infrastructure investments, and to otherwise support the economy, as well as the transition to net zero. Insurers have significant portfolios, and the capacity to direct more of this to social purposes, whilst retaining a return to shareholders, will be welcomed.

Most mutual life insurers manage long-term liabilities too, and we welcome the opportunity to better match the term of asset holdings to their liabilities, for example through investment in long-term infrastructure projects. However, friendly society legislation and other legal restrictions limit the capacity of the sector.

We wrote to Treasury in summer 2021 on necessary changes to the Friendly Societies' Act 1992, and unless the legislation catches up with the Companies Act, these constraints will persist, regardless of relaxations offered via this consultation. A recent Private Members Bill offers the opportunity to take forward these reforms and we urge Treasury to provide active support to Sir Mark Hendrick.

We note the plan to extend the matching adjustment to income protection products. AFM members manage around half of all individual income protection claims, but as previously explained, the size of our members and the high cost associated with implementing and maintaining the matching adjustment, make this unviable for most mutual providers.

We note that the PRA statement, issued at the same time as this consultation, and which reaffirmed the case for reform, also indicated that there was a need to ensure that a reduction in the risk margin and strengthening of the Fundamental Spread are properly aligned, to ensure the market continues to work effectively and provide the right level of policyholder protection[11].

However, we consider that the Fundamental Spread regime has a significant degree of prudence built in, and we do not consider therefore that further strengthening is necessary, or that a change in the risk margin should automatically be offset. As we mention in response to Question 2.1 and in our introductory comments, it is important changes positive changes in the Solvency 2 regime are not unduly diluted by other regulatory actions.

[11] See: www.bankofengland.co.uk/prudential-regulation/publication/2022/april/pras-statement-on-the-review-of-solvency-ii-consultation-published-by-hm-treasury

Question 5.1 What is the impact of these reforms on regulatory costs incurred by insurers?

The changes to reporting requirements taken forward by PRA in 2021 have already had a favourable effect on the cost of reporting, and streamlined efforts on it. In our response to PRA consultation CP11/21, we highlighted that the changes proposed would have only a limited impact on smaller insurers. We have previously put forward to PRA proposals for how to streamline asset requirements for smaller mutuals, having written in detail in 2019 and again in 2021, but have not had a response. We will explore how this is addressed in any future PRA consultation.

With regards to internal model changes, as these do not apply to smaller businesses and no AFM member runs an internal model, we cannot comment on the value of the proposals. The position is similar for the proposals on transitional measures, which were not applied by smaller businesses due to cost.

We had anticipated the review of Solvency 2 would have provided an ideal opportunity to consider greater proportionality of the regime, and in particular to explore those elements of Solvency 2 which have a greater potential impact on smaller insurers than the ones covered in Chapters 2 to 4.

In particular, where Chapter 5 explores reform to the Internal Model regime, we were disappointed there was no comparable consideration of the Standard Formula, which is used by the majority of insurers. We think this might distort the market, in providing a relative disadvantage to smaller firms. Possible reforms to the Standard Formula that would be helpful include making the mass lapse stress more realistic, and providing greater powers for the PRA to review the parameters within the Standard Formula.

We are mindful that PRA has indicated that at the end of the Solvency 2 review it will "consider the case for a simpler regime for smaller insurers and friendly societies". We are grateful for that, but disappointed it did not form part of the government review. Equally, where there is no apparent timeline for the implementation of changes in this consultation, or for the completion of the government's review, we are concerned that this pushes attempts to explore proportionality into the long grass. The concerns raised by some AFM members indicate that this may come too late to benefit them, particular when combined with the reluctance to review the threshold for existing Solvency 2 firms (as covered below). We strongly contend that greater proportionality should be a feature of this review, and not taken up at some uncertain date in the future.

Question 5.2 What would be the impact of removing capital requirements for branches of foreign insurers operating in the UK, both on existing branches and on the decision to establish new branches?

These proposals would be likely to increase the attractiveness of the UK to overseas insurers. As AFM only represents UK insurers, we are unable to quantify this.

We would be concerned however if the proposals resulted in a lower cost regime for the branches of foreign insurers, when compared to UK insurers. This is both in terms of the competitive disadvantage UK businesses would suffer, but also the consequences for consumers. Whilst greater choice will be positive, the past record of failures of overseas insurers has increased costs to UK insurers and policyholders, and has caused reputational damage.

Easing access is reasonable, so long as it maintains a level playing field for competition. It is unclear from the consultation how this will be maintained.

Question 5.3 What would be the impact of a new mobilisation regime for insurers and changes to thresholds at which Solvency II applies on:

- businesses currently considering whether to become an authorised insurer; and
- small insurers' ability to expand before Solvency II applies?

Whilst an increase in the threshold for Solvency 2 is welcomed, we believe the proposal needs more careful consideration in order to achieve the positive impact on competition envisaged. As worded in the question above, the policy approach is likely to have a detrimental effect on competition.

The UK has fallen some way behind the EU in looking at the need to raise the threshold at which Solvency 2 applies, as EIOPA and the European Council have been exploring increases to the threshold, as part of a range of measures for greater proportionality, for some time. EIOPA has recommended a threshold in the EU much greater than the proposals in the Treasury consultation: typically a threshold for premium income of 25 million euros, though with discretion for national supervisors to vary the level according to the maturity of their industry and local market conditions[12].

We had anticipated the UK government would have recognised the scale of the UK insurance sector, and the potential to increase competitiveness of UK industry, by providing a high threshold. An increase to just £10 million will mean that small insurers in the UK are disadvantaged compared to counterparts in the EU.

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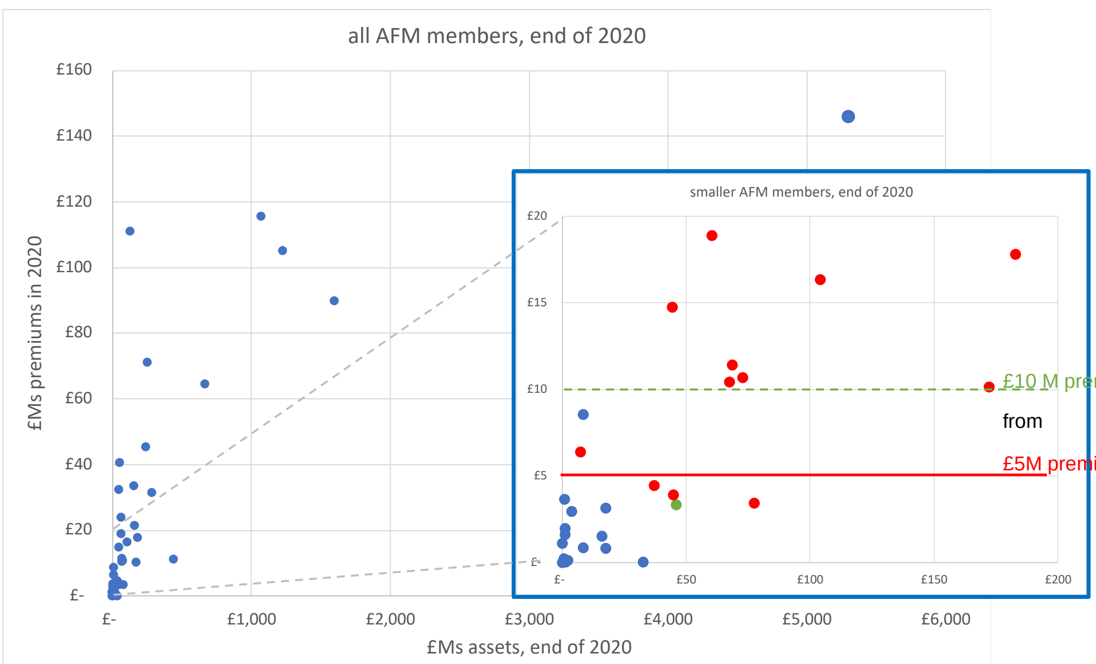
[12] The EIOPA opinion published in December 2020, proposes: "allowing an option for the Member States to set the threshold referring to direct gross written premium income between the current 5 million Euros and a maximum 25 million Euros".

Worse, as stated in Question 5.3, Treasury proposes the higher threshold does not apply to firms currently in the scope of Solvency 2, with premium income of under £10 million. This will mean those firms would be at a significant competitive disadvantage compared to new businesses. This is not just because of the punitive capital and regulatory regime: these firms also fall within the definition of Public Interest Entity (PIE), which extends to all UK insurance companies within the scope of Solvency 2. Being classified as a PIE impacts audit requirements, and means that effective audit is becoming unaffordable and very difficult to place for smaller mutuals.

Recently, BEIS stated that it would consider excluding 'some smaller entities from the PIE definition altogether'[13]. Should that include smaller mutual insurers, it would make a significant difference to the cost base of those businesses, without distorting accountability to members, or policyholder protection. (As we stated in our response to the BEIS consultation, and as echoed in BEIS's paper, the oversight of PRA and FCA provide a significant overlap of responsibility[14].)

By our analysis, there is only one member of AFM that is close to approaching the current Solvency 2 threshold, who might therefore benefit from the proposals in the consultation paper. This is illustrated in the chart below (source: AFM).



The larger chart plots premiums and assets for all AFM members, with the inset chart showing all those with less than £20 million premium income. Organisations

[13] Restoring trust in audit and corporate governance, May 2022, p31
[14] https://financialmutuals.org/wp-content/uploads/2021/01/AFM-response-to-BEIS-on-audit-reform-0721.pdf

represented by red dots are required to comply with Solvency 2 now; those in blue are either too small, or offer a form of discretionary cover which is exempted from Solvency 2. The one green dot represents an organisation with premiums below the current Solvency 2 threshold, who might have expected to be included in scope in the next five years or more, but who may no longer need to under a revised threshold of £10 million premium income.

Under Treasury's proposals, the firms represented by red dots would remain within the scope of Solvency 2 if, as stated in the question, the higher threshold only applies to new insurers or those below the current limit. Whilst it is true that a firm that drops below the current threshold and consistently remains below it for a number of years might seek to exit Solvency 2, there is no regulatory exit route in place or viable alternative regulation. Even if there were, such a route would not offer a short-term solution.

With regard to the potential for the creation of new insurers, the regulatory regime has had a mixed record. There has been no new friendly society created since 1995, as a result both of ill-fitting legislation, and high regulatory obstacles. The PRA and FCA established a new insurer start up unit in 2018, to follow on from the new bank start up unit established in 2013. Whilst the latter has an active webpage and claims that 30 new UK banks have been set up since 2013, the new insurer start up unit does not publish data on its webpage.

Reassuringly, the 2021/22 PRA annual report indicated seven new insurers were established in the year[15]. However, previous annual report indicated new UK insurers are being created at the rate of only one or two a year. In correspondence with AFM, PRA confirmed since legal cut-off in 2013, it had overseen the establishment of 24 new insurers, 11 Lloyds Managing agents, 3 overseas branches and 7 ISPVs (Insurance Special Purpose Vehicle).

However, the net number of insurers regulated by PRA has fallen to 462 today, according to their latest fees consultation, from 610 in 2013, a fall of around one-third. Meanwhile, regulatory fees for insurers have doubled, to £99.1m, meaning that the average cost of PRA oversight per regulated insurer is 260% of the 2013 level[16].

Meanwhile, the relative ease by which overseas firms have been allowed to passport into the UK, means that where we have seen very few failures amongst insurers in the last 20 years, most of the claims the Financial Services Compensation Scheme have dealt with have been for branches of overseas insurers.

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[15] https://www.bankofengland.co.uk/-/media/boe/files/annual-report/2022/pra-2022.pdf?la=en&hash=134FE889D5ACE0768E3B573EBA840447E3782AA5#page=49, page 82

[16] https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/consultation-paper/2022/april/regulated-fees-and-levies-rates-proposals-2022-23.pdf?la=en&hash=6926E36A60D6DFC54EE97775897C32210FC32DCF

We would like to see a more imaginative and active approach from the new insurer start-up unit. In our own assessment the high regulatory hurdles detract from the UK as an attractive place to establish a new insurer. From our own experience, there is no shortage of interest in establishing new mutuals, particularly in sectors of the economy where the price of insurance is high and the prospects of claims being handled fairly is limited.

Whilst it is true that no new friendly society has been created since 1995, we have seen continued interest in establishing discretionary mutuals. Discretionary mutuals are not new in themselves: some AFM members have traded in this way for over 100 years. However they have become more popular of late because their products fall outside the regulatory definition of insurance, and they are therefore able to provide extensive benefits to their members without punitive regulatory overheads. We have though seen severe competition and aggressive tactics by incumbents in areas that discretionary mutual seek to operate, and this has meant discretionary mutuals are not widespread in the UK[17].

We recognise that the consideration of thresholds has been under-developed in the review so far, warranting a mere paragraph in the consultation. But the principles are clear, and we are concerned that the absence of attention will, in short, hasten the demise of well-established insurers, reduce choice for consumers and increase the commoditisation of the UK market. All of this is contrary to the Treasury's stated expectation, which is that the proposed change in threshold will increase competition.

We consider that a threshold of at least £20 million, and potentially as high as £50 million would be realistic in comparison to the EU, and provide an opportunity to enhance competition, by reducing costs to small businesses, as well as offering an opportunity for start-ups to gain real momentum before entering full regulation. There is precedence for this in the two-speed regulation of credit unions, and in PRA's proposals for 'strong and simple' regulation in banking. We have put the case to Treasury and PRA in the past that a 'Solvency 2 lite' regime might be developed to transition smaller insurers out of Solvency 2 without their having to surrender all the investment they have made in developing tools, skills and processes to support Solvency 2.

If Treasury is serious about creating new competition in insurance- and in our assessment the consultation does not wholly evidence this- the solution is more complex than a token increase in the Solvency 2 threshold, which will have little or no impact on the market. We remain, as ever, happy to explore options for introducing new competition, and for enabling existing small insurers to thrive and to support UK consumers and the UK economy more effectively.

[17] Recent examples, which have enjoyed mixed success, include Nexus Mutual, The Miliary Mutual and Local Government Mutual.