Association of British Insurers 51 Gresham Street, London EC2V 7HQ Tel: 020 7600 3333 Fax: 020 7696 8999

ABI response to the Review of the Balance of Competences – Single Market: Financial Services and the Free Movement of Capital – call for evidence

The UK insurance industry:

The UK insurance industry is the third largest in the world and the largest in Europe. It is a vital part of the UK economy, managing investments amounting to 26% of the UK's total net worth and contributing £10.4 billion in taxes to the Government. Employing over 290,000 people in the UK alone, the insurance industry is also one of this country's major exporters, with 28% of its net premium income coming from overseas business.

Insurance helps individuals and businesses protect themselves against the everyday risks they face, enabling people to own homes, travel overseas, provide for a financially secure future and run businesses. Insurance underpins a healthy and prosperous society, enabling businesses and individuals to thrive, safe in the knowledge that problems can be handled and risks carefully managed. Every day, our members pay out £147 million in benefits to pensioners and long-term savers as well as £60 million in general insurance claims.

The Association of British Insurers:

The Association of British Insurers (ABI) is the voice of insurance, representing the general insurance, protection, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 300 members, accounting for some 90% of premiums in the UK.

The ABI's role is to:

- Be the voice of the UK insurance industry, leading debate and speaking up for insurers.
- Represent the UK insurance industry to government, regulators and policy makers in the UK, EU and internationally, driving effective public policy and regulation.
- Advocate high standards of customer service within the industry and provide useful information to the public about insurance.
- Promote the benefits of insurance to the government, regulators, policy makers and the public.

ABI submission:

Over the last year we have discussed the balance of competence exercise with ABI members of varying sizes (operating solely in the UK, pan-European, and third country headquartered). While we are not in a position to respond in detail to the call for evidence, and responses are mixed, there are a number of common threads that can be drawn. We

hope you will find these high level points a helpful contribution, and we are at your disposal should you wish to discuss this further.

When asked the general question about the balance of competence between the UK and EU in the regulation of financial services, the response from ABI member companies will primarily depend on whether they operate in or are familiar with markets outside the UK. This in turn often identifies the degree of familiarity with the EU institutions.

There is certainly comfort in knowing your national regulator, and a national regulator is more likely to understand the local markets, the needs, ways and means of doing business in the UK. However, that said most ABI members will also say when it comes to conducting business it is less about the location of the regulator than the quality of the regulation and the judgement of the individual supervisors. What is important is that the regulation is sound and fit for purpose.

Solvency II is referenced in the call for evidence, and is clearly core EU legislation for the insurance industry. The collaborative working relationship and good dialogue by HM Treasury with other member states resulted in a workable outcome on the framework legislation for Solvency II (Omnibus II). It shows what can be achieved if the time, effort and proper resources and expertise is put into dialogue and delivery.

However, we are not fully there yet. The detailed secondary legislation is still to be finalised, so it remains a little too early to draw any definitive conclusions on Solvency II until the process is complete and implementation has happened. We are very conscious of the tight timeline for implementation. While we want legislation to be coherent and well considered, delays due to extended negotiations will often eat into firms' time to prepare for implementation. Further consideration of timing, and perhaps securing a minimum implementation time for substantive legislation, would be of benefit to both national supervisors and firms.

The difficulties in finalising the Solvency II negotiations highlight both the attractions of EU level regulation and its drawbacks. For many years there has been consensus that there would be great advantage for regulators, industry and policyholders in an updated EU level framework for prudential regulation. However, pension and pension-like products, such as annuities, differ widely across the EU, and additional time was needed to find regulatory solutions that were sound, and encouraged regulatory convergence across Europe, but did not undermine the pension/life insurance system in individual member states. It was essential for the credibility of the EU as an insurance legislator that this balance was struck, and this outcome is an indicator that the balance of competences lies in roughly the right place.

Another important factor in assessing the balance of competences is how EU legislation is implemented on the ground, not least in the UK. There is often much consideration given to "gold-plating" (ie. that the UK Government will layer additional requirements on top of EU legislation) but nothing on "over-implementation" (ie. use national discretions to apply additional layers of capital). While we are concerned about both, in our experience there is far less attention given to the UK supervisory authorities' potential to "over-implement" against the spirit of the original EU legislation. We are therefore looking at how the

Prudential Regulatory Authority (PRA) will use its' discretionary capital add-on powers, and development of early warning indicators, with considerable interest.

Looking to the future development of the balance of competences, we believe that the operation and functioning of the European Supervisory Authorities (ESAs) will be a key factor. At present we believe it is too early to determine their impact, as they have only functioned in their current form for three years. The European Insurance and Occupational Pensions Authority (EIOPA) is the ESA we are in most regular contact with, and there is indeed some nervousness about how it will develop and function in practice in the long term.

We believe the role of EIOPA will become clearer now it has a 'foundation' text to work with (Solvency II), and we will follow and engage with much anticipation. There is a risk that national supervisors' reaction to national developments may pull the Single Market apart. However, this role will also require a high degree of sensitivity to national needs, and we are interested in seeing how ESA 'guidelines' are agreed and used in practice. There is some concern (admittedly not so far evidenced) that binding guidelines may become a means of circumventing the politically overseen regulatory process, and in practice become a supervisory tool for layering additional requirements. This must be guarded against, both at EU and UK level.

As the ESA's legal founding is not concrete in a number of areas – such as the status of guidelines and its consumer role – there is some concern at how the ESAs may act outside the spirit of the remit intended by their founding Regulations.

The lack of clarity on the consumer role under Article 9 has seen some ESAs adopting a broad interpretation. There has been considerable use of the consumer protection provisions in Article 9 with a lot of resource being devoted to producing additional and potentially unnecessary guidelines. We have closely followed the work undertaken by both ESMA and EIOPA in respect to their consumer protection mandate. However, we do question the value of these ad hoc consumer driven initiatives and wonder if this detracts the ESAs from much needed work elsewhere within their agencies.

Indeed, in policy areas where there are close links with national social security arrangements, such as pensions and annuities, there should be much less (if any) focus on trying to assimilate different national regimes, especially where differences, such as taxation, are insurmountable. What would be far more beneficial would be to identify a way of how these differing regimes can best sit side by side each other.

Looking further ahead in the development of the balance of competences, the future development of relations between the eurozone and the UK are a source of concern for ABI members. There will be a temptation for eurozone countries to gather financial services regulation into the eurozone. If this happens, the Single Market will be an empty shell. If the UK is to reap the benefits of EU membership, it is essential that the British Government remains fully engaged with its EU partners, participating constructively in the debate. This warning applies to the approach of the UK regulators also. Supervision cannot be treated as a national preserve.

There has always been much interest in the European Commission about how to support or encourage the distribution of insurance products cross border. While the ABI recognises the

underlying theoretical principles and the attractiveness of being able to provide retail products across the EU borders, not least because an asymmetry of regulation makes it easier (and less expensive), the reality is that there is limited consumer demand. In our experience customers simply prefer to shop close to home, in a language they understand, protected by their national legal system. The increase of internet shopping may change this over time, but it would be wrong to load cost on to consumers to force the development of cross-border trade for which there is little demand.

Furthermore, national regulators and supervisors are closer to the consumer, and are best placed to identify the needs and expectations of those in their jurisdiction. We therefore hope that there is a pause in retail regulation at European level for the foreseeable future, and any changes in customer demand that warrant the modernisation/new rules are done so at a calm and reasoned pace. The consequences of ill-though through regulation in the retail area are likely to be much more severe, and take longer to rectify than in other areas. As a minimum, it is therefore essential that the UK Government prioritises retail issues when negotiating in Brussels, and certainty treats them on a par with as much vigour as it does with wholesale financial services – for example, MIFID2, PRIPS, IMD2 negotiations.

In addition, there needs to be more careful consideration about how the various strands of legislation interplay, especially where they are drafted by different Commission teams – eg. Packaged Retail Investment Products (PRIPs) sales rules, potentially being introduced in Insurance Mediation Directive, and the review of Markets in Financial Instruments Directive (MiFID). There is much scope for improvement when it comes to cross-departmental interaction, and for all policymakers (EU and UK) to consider the consequences of, and work against, any overlap of different legislative proposals.

ABI 16th January 2014