BANK OF ENGLAND

News release

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Insurance, stability and the UK's new regulatory architecture - speech by Paul Tucker

Speaking in London today, Paul Tucker – the Bank's Deputy Governor for Financial Stability and member of both the Monetary Policy Committee (MPC) and the Financial Policy Committee (FPC) – speaks to insurance leaders about how the industry fits within the UK authorities' efforts to make the financial system more resilient. He underlines the importance of the insurance industry to the UK economy, discusses its role in financial stability and outlines a view of the issues with which the authorities are grappling in relation to insurance regulation.

Discussing the role of the insurance industry within the economy, Paul Tucker underlines the role it plays in enhancing efficiency and welfare and says "it is something to be proud of". Reflecting on whether insurance is integral to stability, he highlights the potential for insurance firms to build shadow banks within their group, for example through their securities lending business. He emphasises that "nothing must be done to jeopardise the essential functions of securities lending" which, he says, are key for any capital market to work efficiently. But he notes the challenge which the maturity transformation and leverage involved in collateral swaps, and the invisibility of the market, presents to the authorities as they seek to protect and enhance the resilience of the system. Highlighting the need to put some structure around the market, and the Bank's desire "in line with our traditions, to find market-led solutions where we can", he suggests one option might be to introduce a Trade Repository.

Paul Tucker underlines the importance of effective consolidated regulation and supervision of insurance groups. Reflecting on the EU's latest insurance directive, Solvency II, he talks of the Bank (and the FSA) being "dismayed by how much it is costing the industry and the regulator to adapt to Solvency 2" and voices concerns that "like the initial attempts at Basel 2 for banks, it risks being too complicated in its desire to introduce a 'risk sensitive' regime ... We need to be wary of regulators drowning in masses of data going beyond anything they can get their hands round. Unless we are careful, it risks distracting supervisors from the big risks."

Talking about the new supervisory approach, Paul Tucker points to "supervision that attends to the big risks that would undermine the safety and soundness of a firm" and says that objective is "a big improvement on

what has gone before". Noting the provision within the UK's regulatory reform Bill for the Prudential Regulation Authority (PRA) to take a view from the Financial Conduct Authority (FCA) on 'fairness' issues, he acknowledges concerns within the industry over having to engage with two microregulators. But, he says, "I hope you will accept that the previous architecture, based on 'one-stop regulatory shopping', didn't serve society or the City itself at all well".

Paul Tucker emphasises that the focus on safety and soundness "means that insurers must be able to fail quietly, in a controlled, orderly way", and cautions against the received wisdom that this is necessarily straightforward for insurers. He believes the importance of tackling the issue of resolution of insurers "will be underlined as [the global community] remove the safety net for banks, leaving holders of bank bonds exposed to risk. Insurers are significant investors in bank paper. In the future, whether in the UK or elsewhere, you will not be protected by an implicit guarantee from the state for those investments. Over time, that will be good for stability because it will increase market discipline. But it will be a new world for the insurance industry to adjust to."

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