CP61- Consultation on Impact-Based Levies and Other Levy Related Matters

Response from the Irish Insurance Federation

Following consultation with our members and discussion within the Irish Insurance Federation Central Bank Levy Working Group the following is our response to CP61.

Increase in Levy Fees

Members who responded to a request for information as to the impact of the proposed levy regime have indicated increases in some cases of between 250% and 300% as between fees paid in 2012 and those likely to be payable in 2013 under the proposed new regime. In the light of this unexpected increase in regulatory costs we are concerned that the Central Bank should be committed to managing its own costs in a fashion that anchors them to a genuine need to manage empirically-determined risks within the insurance industry.

We believe that the CBI needs to consider and develop a strategy as to how it will reduce its costs in the future, including how it will manage and fund its personnel costs, benefits and pensions schemes, in a way that is not storing up trouble for an industry, that is no longer offering comparable benefits to its own newer employees, as we move eventually to 100% funding.

Further we are concerned that the new levy structure and proposed authorisation fees may discourage smaller enterprises from establishing in Ireland or, perhaps more seriously, may encourage larger incoming enterprises to establish on a branch-only basis or to distribute entirely via intermediaries. Has the CBI taken the possibility of such behavioural responses into account and has it considered the potential for emerging systemic risks to be masked by such behaviour?

The following are responses to the particular questions asked by the CBI.

General Questions:

1 Do you agree with the Central Bank's proposal to use firms' impact categorisation under PRISM as the basis for the setting of the levies it charges regulated entities on an annual basis? If you disagree, what would you propose instead?

In general yes. However, the use of impact rating alone does not appear to be entirely proportionate to the resources applied. It takes no account of the actual risk rating of companies or the issues which they face. Nor does it adequately take into account the regulatory costs incurred under Solvency II e.g. internal model companies vs. standard formula companies which have presumably consumed a large amount of resources. We would like to CBI to review this approach in the future.

2 Do you agree with the Central Bank's proposal to allocate the cost of financial regulation activity on a basis consistent with the allocation of supervisory resources to regulated entities? If not, what cost allocation methodology would you propose?

In general yes we agree.

We note the CBI's response to our concern about the difference in fees for different bands given at the IIF CBI Levy WG / CBI meeting on 22nd January that the bands reflect the actual resources allocated, and that 'high' resource are about four times 'medium-high' resources and that the bands represent business categories that are fundamentally different in impact level and that each requires significant different levels of CBI resources.

We understand that companies within the same category may have different resources allocated to them. Has the CBI considered the difference in cost of supervision between these firms when proposing levies?

We also note that the CBI has indicated that the occurrence of the process whereby companies move from one band to another is very infrequent, will usually involve significant developments in the business or fundamental changes to the business model itself and will take place in the context of lengthy engagement with the CBI whereby any changes to the bands will be built into the planning and discussion process with the CBI.

4 Do you agree that the credit union sector should be required to fund the relevant proportion (currently 50 per cent) of the cost of financial regulation that would apply under an impact based approach to the levy process? If not, what alternative approach would you propose and why?

We believe that all sectors must make the relevant contribution to costs and that there should be no cross-subsidisation between sectors. We understand from our meeting with the CBI on 22nd January that the exchequer will be making up any short-fall in regulatory costs incurred by the Credit Union Sector.

5 Do you agree that this change be phased in over a period of 5 years? If not, what alternative approach would you propose and why?

See answer to 4 above.

6 Do you agree with the Central Bank's proposal to impose an application fee in respect of each industry funding category proportionate to the average time taken to consider an application for authorisation? If not, what alternative would you propose?

We would agree in principle with the proposal to impose application fees but there should be some allowance for the size of the applicant. The proposed €50,000 fee seems very high in comparison with other jurisdictions. We understand that the CBI is proposing a policy of charging the 'full cost' of the application process. An application fee of this size could put off a 'seriously interested' medium-sized insurer from setting up in the Irish market. Whilst €50,000 may not seem material for a business whose premium turnover could be in the region of €10M – for example, it ignores the often large difference between gross premium and profitability where €50,000 could make the difference between profit and loss during the start-up phase. Thus the fee could prove more an unintentional prohibition to the cost-sensitive business with significant potential than a real deterrent to the unready and uncommitted.

The CBI should consider that it is likely to be prohibitive, in comparison with other jurisdictions and, therefore, whether this approach is a good idea for the long-term health of the Irish insurance industry and for employment.

See also our comments under *Increase in Levy Fees* above concerning disincentives to establish and the possibility of behavioural distortions and hidden systemic risks.

We suggest a compromise whereby some of this cost could be recoverable during the first year of operation (by, for example, discounting some of the application fee from the first year's regulatory levy).

We understand that the CBI is not proposing to charge for an application to change the classes of insurance underwritten.

We would also like clarification as to whether the CBI would charge an application fee where an entity seeks additional authorisation within the same industry funding category. For example where a life insurance undertaking seeks authorisation as a reinsurance undertaking. As the entity is already authorised within Category B, is it correct that there would be no application fee charged in this instance or would it be viewed as a fresh application, subject to the full Application Fee?

7 Do you agree that such a fee should be payable at the time an application for authorisation is submitted and that it should be non-refundable in the event that an application for authorisation is withdrawn or refused? If not, what alternative would you propose?

See our comments above. This proposal should be benchmarked against market practice in other countries competing with Ireland.

8 Do you agree with the Central Bank's proposal to maintain the policy of imposing pro-rata levies in respect of the period in relation to which a regulated entity holds an authorisation from the Bank? If not, what alternative do you propose?

Yes, we agree.

9 Do you agree with the Central Bank's proposal to impose a penalty on any and all firms who do not pay their levy within the time allowed? If not, what alternative course(s) of action would you propose to ensure that all regulated entities pay their Industry Funding Levy?

In general yes although we would suggest that the CBI should have and use discretion to deal with exceptional circumstances.

10 Do you agree with the Central Bank's proposal to seek the power to unilaterally revoke the authorisation of those firms which continue to fail to pay their Industry Funding Levy? If not, what alternative would you propose?

Yes although we would question whether yet another specific power is necessary given the existing wide powers of the CBI.

11 Do you agree with the Central Bank's proposal to remit 100 per cent of the value of monetary penalties to the Exchequer? If not, how would you propose to treat monetary penalties?

We believe that for the CBI to rely on penalties to alleviate its funding costs would be a mistake. However we would suggest that the Central Bank look at how monetary penalties are used in other EU states given that the funding model for the regulatory aspects of the Central Bank in Ireland is currently split 50/50 between the financial services industry and central government.

We suggest that penalties could be paid into a fund and released over time, say five years, to smooth unforeseen additional costs of the CBI.