General Insurance Pricing Practices Market Study Final Report

Annex 1: Detailed feedback on our Interim Report and our response

September 2020

1 Introduction

1.1 In our Interim Report, we set out our interim findings and the potential remedies that we proposed to focus on and invited feedback to five questions:

1. Do you have views on the interim findings set out in this report?
2. Do you have views on the potential remedies we propose to focus on? What are the potential benefits, challenges and unintended consequences that may arise from these?
3. Do you have views on the potential remedies that we propose not to focus on? What are the potential benefits, challenges and unintended consequences that may arise from these?
4. Do you think there are other remedies that we should be considering? If so, what remedies and how do you think they would address the harm we have identified?
5. Are you aware of potential changes or innovations in the home and motor insurance markets that may address the harm we have identified? If so, what are these and how will they address the harm and are there any potential unintended consequences?

1.2 We received over 60 responses from across the industry including firms and trade bodies as well as consumer groups and individual consumers. We have carefully considered this feedback and set out further details together with our responses below.

2 Views on our findings

Do you have views on the interim findings set out in this report?

2.1 Most respondents provided positive feedback on our findings, welcoming the work being undertaken and recognising the benefits of FCA intervention. A few respondents disagreed with our proposition that the market is not working well. They emphasised the highly competitive nature of the new business market and the progress that has already been made following recent regulatory changes. Furthermore, some respondents emphasised the differing business models in the market and warned against the potential for over emphasising price in consumers' choice when purchasing a policy.

2.2 In our Interim Report, we recognised that a significant number of consumers benefit from the lower prices available but there are also many consumers who are paying high or very high margins. We found that the market is not working well for those paying these very high margins. We recognise the comments made regarding the differences between firms and so our proposed remedies will apply to the relevant firms regardless of their business model.

3 Views on potential remedies

Do you have views on the potential remedies we propose to focus on? What are the potential benefits, challenges and unintended consequences that may arise from these?

3.1 We proposed to focus on:

1. Remedies to tackle high prices for consumers who do not switch or negotiate better deals;
2. Remedies to tackle practices that discourage switching; and
3. Remedies to make firms be clearer and more transparent in their dealings with consumers.

A large number of respondents expressed overarching views on the remedy package that we were proposing.

Feedback	Response
We need to recognise that consumers' choice of insurance product can be based on factors other than price. Respondents mentioned the importance of consumers assessing the value of insurance using a range of criteria. These include quality of service and the level and suitability of cover, in addition to price. Respondents felt that our proposed remedies may lead to a further increased focus on price with potentially negative consequences, such as the hollowing out of product features or consumers selecting cover that does not suit their needs.	We believe it is important that customers take out fair value products. By 'fair value' we mean that there is a reasonable relationship between the overall cost paid by the customer and the quality of the product and services. This includes factors such as the level of cover under the policy, the quality of service provided and the handling of claims. Our remedy package is designed with this in mind. Our pricing remedy allows firms to retain flexibility to offer a range of products with different features, such as the level of quality and the services provided, to meet the needs of different consumers. In addition, the proposed product governance remedies will require firms to consider whether their products offer fair value to the end customer throughout the lifetime of the policy. This will include ensuring that the product meets the consumer's demands and needs both in terms of product features and level of cover. We are publishing the <u>Policy Statement</u> alongside the <u>Final Report</u>. This sets out new rules requiring firms to provide information about the performance of their products which we consider will support improvement in the quality of products and the provision of fair value products to consumers.

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<td> Our proposed pricing remedies may lead to:

Fewer customers shopping around and switching if the differential between new and renewal prices is reduced.
A rise in new business prices as firms try to recover increases in costs and expenses.
An increase in the sale and price of ancillary products where firms try to recoup any revenue that would otherwise have been earned from premium increases.
A reduction in access to insurance for some customers whom firms may consider having a higher cost to serve.
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<td> We acknowledge that any pricing remedy could lead to potentially unintended consequences and so we have sought to design a balanced pricing remedy that tackles the harm from price walking without:
a) causing significant increases to new business prices; and/or
b) damaging competition by removing the incentive for consumers to compare products or discouraging switching where it may be beneficial.
The pricing remedy that we are proposing will apply to both the core price of the policy and the ancillary products that may be sold alongside. Our proposed rules will also require firms to have appropriate policies and procedures to ensure that their pricing practices are consistent with the overall intended outcome and objectives of the pricing remedy.
In line with our mission framework, we plan to evaluate the impact of our intervention. We will consider the impact of the intervention on each of the relevant general insurance markets separately and in aggregate. Alongside this, we will evaluate the impact of the intervention on consumers of different tenures. </td>
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<td> Many of the proposed remedies will require significant time and investment to implement. This could impact different players in the market disproportionately.
While some respondents argued the need for action to be taken quickly, many respondents drew attention to the likely impact on the industry, particularly following the implementation of the Senior Management and Certification Regime (SM&CR) and the Insurance Distribution Directive (IDD). </td>
<td> In addition to our stakeholder engagement since the Interim Report, we have conducted a cost survey, described in Annex 2 to the Consultation Paper, which informed our estimate of the financial and practical costs of implementing these proposed remedies. We have taken this evidence into account when deciding which remedies to consult on.
We have seen the changes that have already been made in the industry following recent regulation and some of our proposed remedies build on these.
We recognise that the time needed to consider and implement changes will vary across firms and so, given the current impact of Covid-19, our consultation period will be open until 25 January 2021. Following this, we intend to publish a Policy Statement in Q2 2021 with any new rules coming into effect 4 months after publication. We believe that this strikes the right balance between taking prompt action to reduce the harm identified whilst giving firms sufficient time to prepare. </td>
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Remedies to tackle high prices for consumers who do not switch or negotiate better deals

Restrictions on pricing practices

3.2 We said that we would consider limiting or banning pricing practices that take advantage of consumers who do not switch or negotiate. This could include:

- Restriction on price increases to renewing customers.
- Restrictions on the use of particular factors in setting prices and determining margins.
- Restrictions on the price level relative to a benchmark such as the new business price for the policy.

<table>
<tr><th>Feedback</th><th>Response</th></tr>
<tr><td>Remedies to restrict price increases to existing customers could help but may be difficult to determine and to consistently apply across the market.

Respondents broadly agreed on the need to tackle price walking, particularly for customers who are paying very high margins. However, they expressed differing views on the desirability of prohibiting price discrimination by tenure. Many argued that the ability to offer new business discounts encourages competition and results in low prices for many consumers.

In particular:
Consumer groups expressed the need to curb those practices that exploit customers who do not switch.
Many industry respondents saw benefits to allowing firms some discretion to discount new business prices, provided there were restrictions to price walking, such as a benchmark to the equivalent new business price.
Some insurers and intermediaries that already use such benchmarks cautioned against setting an industry- level benchmark due to the difference in policies and levels of cover across these markets. Other insurers and intermediaries argued against benchmarking to an equivalent new business price, citing the lack of equivalent price for products that aren't available to new customers, or cases where they set the renewal price using data they hold on their existing customers that is not available to set new business prices.
Some insurers and intermediaries were concerned that a remedy restricting</td><td>We consider that our current proposed pricing remedy provides the best way of tackling the harm from pricing practices.

It prevents firms from charging higher prices to renewing customers than they would be charged if they were a new business customer, whilst allowing firms to retain flexibility for offering different prices and products to different consumers. We think this will help retain the benefits and incentives for firms to continue offering competitive deals to consumers.

We also seek to require firms to ensure that they do not systematically discriminate against customers based on their tenure which will help to apply consistency across all customers.

We considered other potential pricing restrictions including a cap on the level of margin and a ban on price optimisation. As set out in Chapter 5 of the Final Report, we considered alternative pricing remedies and decided not to proceed with these given the possible negative impacts on competition and are likely to be less effective in addressing price walking. We also noted the risk that some of the other proposed remedies could reduce access to insurance products. For example, a firm may be less likely to insure a customer if they are considered more costly.</td></tr>
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margins on renewal business would be unworkable. They argued that the cost and revenue bases of insurers and intermediaries are very different, and such a remedy could easily be circumvented. • Insurers' margins are also only known with certainty once all claims have been settled, unlike those of intermediaries.	
There were differing views on remedies to restrict margin optimisation or use of pricing factors linked to likelihood of switching or negotiating Industry respondents generally felt that such remedies could limit competition and innovation of benefit to consumers. Other respondents, including consumer bodies, argued that these practices are inherently unfair, and which could discriminate against customers vulnerable or protected characteristics. Other points raised included: • Some firms argued that optimisation and lifetime value models can help them provide complex or niche products. • It would be costly and disproportionate for firms to justify their rating factors. • Firms could get around the restrictions by using pricing factors that correlate with protected characteristics. • Restrictions on optimisation could also make it harder for firms to apply a consistent margin across all policies.	As set out in Chapter 5 of the Final Report, we have undertaken analysis that indicates there can be competitive advantages to price optimisation. As such, we are not proposing a ban on this. We have set out the Draft Handbook changes in Appendix 1 of the Consultation Paper. This includes indicators of a product not providing fair value such as where a firm increases the price of the insurance product based on whether a policy is subject to auto-renewal or where the customer has purchased the policy using retail premium finance.

Helping consumers find and switch to better deals

3.3 We said that we would consider requiring firms to move consumers on to cheaper equivalent deals.

Feedback	Response
There are practical challenges with remedies requiring moving customers to cheaper deals (auto-switching) either with the same firm or another firm. These included: • Difficulties in identifying "like for like products" • Auto-switching could lead to customers being moved to products with features that do not meet their demands or needs, purely on the basis of price. • Firms would need to assess customer	We have decided not to pursue any remedy that would require firms to switch customers to alternative similar products automatically. We are considering the potential benefits and risks of Open Finance which could include auto-switching. Through the development of common interfaces, Open Insurance could make switching cheaper and easier for consumers, particularly those who are disengaged. However, there are also many potential challenges given the complexity of insurance products.

needs, when they may not have the additional customer information to do so. One firm argued that they may also need additional regulatory permission to do so. • Auto-switching could move customers away from a product they have chosen and with which they are satisfied. • Auto-switching could "result in a culture of continuous switching," producing little benefit or product innovation in the interests of consumers. It could also hurt longstanding customer relationships • Shifting the onus onto insurers would lead to further disengagement of consumers, discouraging them from searching and switching to better cover.	We will be continuing our work on open finance through the Call for Input process.

Strengthening product governance rules

3.4 We said that we would consider strengthening existing rules on product governance and introducing greater accountability for pricing from senior managers.

Feedback	Response
Most respondents supported our proposals on product governance and greater accountability for pricing from senior managers. Some industry respondents also argued that further governance remedies should take into account industry initiatives, while others called for more policing of existing rules. The following additional points were raised in responses: • The need for further remedies should be assessed once the IDD and SM&CR are fully embedded by firms. • Many firms supported the proposal to extend rules to cover all products that had been launched before 1 October 2018 although caution was raised around the potential for retrospective regulation. • There was also an argument that we should either incorporate parts of the Association of British Insurers and British Insurance Brokers' Association "Guiding Principles and Action Points for General Insurance Pricing" (GPAPs) into our rules or supervise against them. • Many firms also supported the proposal to require consideration of the value of the contract which included the proposal for a formal review and approval process for renewal pricing practices. This would also include senior management responsibility	Our rules already set out firms' responsibilities for their general insurance and pure protection products and the systems and controls that govern these products throughout their life cycle. Our rules implementing the IDD and the extension of the SM&CR to insurers have been in place since 2018 and should be fully embedded by firms. We propose to extend and build on these responsibilities as set out in Chapter 4 of the Consultation Paper. This includes: • Extending our product governance rules to cover all products that are currently live in the market regardless of when these were first launched. These will include all general insurance product classes and pure protection, to ensure consistency across the sector. This is not solely in response to the findings of the Market Study. • Amending our rules to require manufacturers and distributors to consider whether their products represent fair value for customers. • Introducing a requirement for a senior manager to provide an annual attestation that the firm's pricing approach is compliant with the new pricing remedy. We welcome the actions that have already been taking place in the industry, including the

for the value of products to the target market. • Some respondents suggested further responsibilities for a senior manager to take, including the formal approval of any renewal pricing practices.	development of the GPAPs to address concerns about pricing practices for their customers. We recognise the work that BIBA and the ABI are doing and expect this to continue alongside any intervention that we make. Our ongoing work in this area has included evaluating measures that firms have put in place to address pricing differentials following the Thematic Review – Pricing practices in the retail general insurance sector: Household insurance, publication of our GI value measures data and our Finalised Guidance on the GI distribution chain.

Monitoring firms' actions to tackle concerns about pricing practices

3.5 We said that we would consider ways in which firms are taking actions to improve their pricing practices. One option could be looking at how to consistently monitor price differentials

Feedback	Response
Many respondents expressed qualified support for collecting data to monitor pricing practices and pricing differentials. Some respondents argued that the measures should apply across all parts of the distribution chain but questions were raised as to whether insurers or intermediaries would be accountable and responsible for providing the information. Some industry respondents highlighted the difficulties with making comparisons between firms' data given the wide range of differences between firms. To address this, some suggested that we publish a set of principles and desired outcomes, against which firms could monitor their own performance. In addition, one respondent made a proposition for us to mandate that firms set out a pricing framework to be overseen by senior management. Some respondents also noted the significant operational costs that might be incurred if we were to set out a standard format for data. Opinions on the scope of reporting varied. One respondent said that data gathered on pricing differentials for customers of different tenure needs to cover large groups of customers to be meaningful, whereas another suggested focusing specifically on vulnerable customers. On the other hand, another respondent thought	Alongside the publication of our Thematic Review in October 2018, we published a letter to the CEOs of insurance firms involved in pricing activities. This set out our expectation that firms should be implementing an appropriate pricing strategy with effective governance and controls. As such, firms should already be collecting some data to monitor their pricing practices and the impact of these on their customers. We are proposing to require firms to submit pricing information reports. Chapter 6 of the Consultation Paper sets out the scope and granularity which includes splitting data by factors such as sales channel, tenure and books of business. The data will include average gross written premiums, average expected claims ratio and cost and proportion of customers paying high and very high premiums. This will help us to monitor firms' compliance with and impact of our pricing remedy. The responsibility for reporting data relating to the pricing of core policies will fall on insurers and price-setting intermediaries. However, the additional data we are proposing regarding premium finance, add-ons and other ancillary products, fees and charges will be required from all relevant firms, including non price-setting intermediaries.

that reporting should be more targeted, e.g. focused on specific firms and in-depth, rather than a blanket, aggregated approach. There was another respondent who suggested monitoring product/brand proliferation.	

Remedies to tackle practices that discourage switching

3.6 We said that we would consider actions to address practices that could discourage or make it more difficult for consumers to make informed decisions and act to get better deals.

Feedback	Response
Respondents, from industry, consumer groups and individuals, strongly argued against banning or restricting auto-renewal. These responses included that: • There could be serious consequences for consumers, particularly those who are vulnerable or could be left without insurance if they forgot to renew. • Banning auto-renewal would require a change in consumer behaviour as it would remove the convenience and reassurance of knowing that a policy is in place. • A ban would be disproportionate, removing the choice from customers who want this feature and want to stay with their current provider. • Many consumers want an auto-renewal option, which they find convenient, and which provides security in the event of forgetting or being unavailable to renew, for instance as a result of an unexpected hospital stay.	We have decided not to pursue a remedy that bans auto-renewal as we recognise that many customers may want their policies to auto-renew and that there are material risks for consumers associated with banning it. We understand that auto-renewal is a valuable service for some customers, giving them comfort that they will have the cover they need in the event of unforeseen or challenging circumstances which could otherwise result in significant loss and consumer harm. We do however still recognise that some action is needed to address the ways in which firms could discourage consumers from switching.
Respondents agreed that auto-renewal should be clear and optional for consumers, but many felt that requiring auto-renewal to be opt-in would require a significant change in consumer behaviour. Supportive respondents argued that making auto-renewal opt-in would increase engagement, lead to more active choices and result in consumers better understanding of the terms of their cover. Some also expressed support for rules to make it easy for customers to decline auto-renewal both at the point of sale of the policy and at subsequent renewals. Many respondents also felt that consumers should be provided with a clearer explanation of auto-renewal to enable them to make an informed choice. However, some raised concerns that a change could lead to a rise in numbers of consumers forgetting to renew and being left uninsured.	We want all firms to offer a simple and effective process by which consumers are provided with information, at initial purchase and at subsequent renewals, to allow them to understand whether their policy is set to auto-renew and the implications of it doing so. As set out in Chapter 5 of the Consultation Paper, we are proposing to require firms to inform customers whether the policy will automatically renew and what the effect of automatic renewal is for them. Firms will also be required to provide information on the customer's right to cancel the automatic renewal. These will have to be provided both before the conclusion of the contract and at all subsequent renewals. This builds on our earlier measures set out in our Policy Statement PS16/21 – Increasing transparency and engagement at renewal, by prompting consumers to engage and shop around.

Most respondents agreed that it should be as easy as possible for customers to exit or not renew their policy, if they wish to do so. Furthermore, some firms mentioned practical steps that have already been taken. These include removing administrative fees or charges for cancellation and extending the 14-day cooling-off period.	We agree that the process for consumers to cancel the auto-renewal of their policy, or switch to other providers, should be as clear and simple as possible. To make it easier for consumers to cancel contracts or auto-renewal agreements, we are proposing that firms must provide customers with a range of different easy and accessible methods for cancelling any automatic renewal feature in their contract. This is also set out in Chapter 5 of the Consultation Paper.

Remedies to make firms be clearer and more transparent in their dealings with consumers

3.7 We said that we would consider how to help consumers make informed decisions.

Feedback	Response
The renewal transparency rules have made a difference in the market in providing consumers with increased information. Some respondents argued that the implementation of the renewal transparency rules, have made a difference in providing information to consumers and helping them choose whether or not to search for a cheaper price. Some argued that the benefit of showing this additional information might have been reduced through inconsistent implementation by firms. This variation across the market needs to be taken into account when introducing any further rules or guidance.	We published Evaluation Paper – EP 19/1: An evaluation of our general insurance renewal transparency intervention which found that the rules appear to have made an impact on the difference between the premium offered at renewal and the premium paid for the previous year. This is estimated at an average of £185m a year. We recognise that firms have taken steps to comply with our existing renewal transparency rules and do not propose to make changes to these at this stage.

Improving the way firms communicate with customers

3.8 We said that we would consider requiring firms to make clear to consumers that renewal prices have increased because they have not switched for a number of years. We also said that we do not see this as the only solution to the concerns we identified but improvements could reinforce and support our overall package of remedies.

Feedback	Response
While industry and consumer respondents want clearer information on pricing, they recognised that additional information requirements could make it harder for consumers to make decisions. Many industry respondents supported the principle of providing more information on pricing. Suggestions included showing whether increases were the result of switching or whether a new business discount had been applied. Other respondents, from both industry and consumer groups, argued that customers could be confused and deterred from engaging with their renewal choices if we added to the volume of information in renewal documents. Unless the information helps consumers understand how the final price of their policy is calculated, it may not be of value, or help vulnerable customers, and those currently least engaged.	As we set out in Chapter 5 of the Final Report, we are not planning to introduce any further changes to the way prices are shown in customer documents at this stage. However, our proposal to prevent firms discriminating on the basis of tenure when they communicate with customers at renewal should improve communications with customers of longer tenure. Our Portfolio strategy letter to Personal & Commercial Lines Insurers in January 2020 reiterated our expectation that communications should be clear, fair and not misleading. We further set out that firms should review their current pricing practices and consider whether they are in their consumers' interests. Our Supervision Strategy for Personal and Commercial Lines Insurance Intermediaries published earlier in September 2020 set out that we believe insufficient or unclear information at the point of sale is one of the

	biggest contributors to customers buying unsuitable or poor value products.

Increasing public scrutiny of firms' pricing practices

3.9 We said that we would consider requiring firms to publish information about their pricing practices or differences in prices between customers of equivalent risk.

Feedback	Response
Any remedies for firms to publish additional pricing information must ensure that the information would be useful to the intended consumer audience. Many firms also saw challenges in publishing information about their pricing practices. These included doubts that this would help customers who are currently less engaged to understand how firms calculate the price of their policy. Some also saw challenges in making comparisons between customers of "equivalent risk," given the individuality of consumers as well as the availability and comparability of data. They felt that specific guidance would be needed as to what constituted "equivalent risk". Some respondents also considered that it would be difficult to separate responsibilities between insurers and intermediaries, and so the resulting information may not provide an accurate reflection of firms' differing distribution chains.	We are proposing to collect data on an annual basis to support our supervision of firms and their pricing practices. The information to be gathered is set out in Chapter 6 of the Consultation Paper. However, we are not proposing to publish any data at this stage. We may consider publishing some of this information in the future where we think this may benefit competition and the functioning of the market.
Publication of information on firms' pricing practices may increase costs for firms and harm competition. Most respondents argued that the publication of data would bring additional costs to firms and could damage competition in the market given the commercially sensitive nature of the intellectual property. Further, aggregated data may also provide a skewed view of the market and would not take into account firms' different structures or customer bases. This may be of limited value to consumers.	We recognise the comments that have been made and are not proposing to require any publication of information about firms' pricing practices at this stage. However, we may choose to do so in future if we consider there would be value in doing so.

4 Views on potential remedies we proposed not to focus on

Do you have views on the potential remedies that we propose not to focus on? What are the potential benefits, challenges and unintended consequences that may arise from these?

4.1 Respondents agreed with our proposal not to focus on requiring firms to offer multi-year contracts. This was largely due to the difficulties associated with risk calculation over a longer period of time. Respondents also agreed with our proposal not to focus on requiring a single switching and renewal period for all consumers as it is unlikely to address the harm that we have identified.

5 Views on other potential remedies

Do you think there are other remedies that we should be considering? If so, what remedies and how do you think they would address the harm we have identified?

5.1 Many respondents observed that Price Comparison Websites (PCWs) have contributed to the current dynamics in the home and motor insurance markets, including:

- An excessive focus on price when providing quotes.
- Situations where customers receive an initial quote from a PCW, which later increases after providing further information to the insurance provider.
- High acquisition costs
- Use of Most Favoured Nation clauses which restrict the insurance provider from offering a cheaper price. This has seen increases in the market power of PCWs.

5.2 In the Interim Report, we acknowledged the ways in which PCWs can affect the market dynamics. We have previously assessed the product information provided by PCWs and published our findings in TR14/11 - Price comparison websites in the general insurance sector.

5.3 Other work was undertaken by the Competition and Markets Authority (CMA) with their market study on digital comparison tools which found that improvements could be made. We have previously noted the CMA's broadly positive conclusions on the role of PCWs in helping consumers shop around and compare products.

Other responses provided included:

5.4 A suggestion regarding restrictions on pricing practices was to require firms to conduct a review of their legacy products, i.e. products that they no longer sell as new business, and take any remedial action for consumers who are found to be paying very high prices. Our proposed reporting requirements, will set out information for firms to gather regarding each of their products including their closed books of business in order for us to understand their treatment of legacy customers. Our proposed PROD rule changes may also require firms to re-assess existing products to ensure that they are providing fair value.

5.5 A couple of respondents proposed the removal of any fees and charges when consumers are undertaking the cancelling or switching process – we are proposing to gather information on fees charged to consumers which are not part of the premium price in order to monitor any changes that may arise as a consequence to our proposed remedies. We are also proposing to require firms to not impose unnecessary barriers or charges on customers wanting to stop auto-renewal.

6 Views on changes to and innovations in the market

Are you aware of potential changes or innovations in the home and motor insurance markets that may address the harm we have identified? If so, what are these and how will they address the harm and are there any potential unintended consequences?

6.1 Most respondents recognised Open Finance and the benefits that this could bring to the insurance industry by providing easier access to insurance and supporting the innovation of products. Many respondents drew attention to new products in the market, for example AutoSergei, which aims to enhance customers' online journeys with automatic comparisons and AvivaPlus which sets out renewal price guarantees for their customers.

6.2 The potential for developing artificial intelligence and machine learning to support data collection and accuracy in the calculation of risks is welcomed by most respondents. However, some raised concerns that automation could reduce consumer engagement particularly with vulnerable consumers who may not understand newer technological processes. This could enable insurance providers to control which customers can access their products. Further, the development could also increase costs which may be passed on to the consumer and result in higher prices.

6.3 Many respondents view these developments as part of a longer-term project as the complexities of the insurance market will need to be carefully considered. Additionally, many felt that this should be a separate consideration rather than one that will address current pricing issues.

6.4 We note the potential for these developments to deliver significant benefits to consumers and competition in the market but also acknowledge the concerns raised.

6.5 Our work on Open Insurance will be taken forward as part of the advisory group and our Call for Input on Open Finance. The next steps that we propose to take have been set out in Chapter 5 of the Final Report.