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Dear CEO

Our expectations of life insurers in relation to the cost of living

Consumers across the country continue to be significantly affected by the rising cost of living, which is disproportionately hitting the poorest households. These rises combined with volatility in the markets are having a very negative affect on customers. We also know that businesses are facing challenges, including higher costs (such as energy) and staff resourcing issues.

The government have announced further support for consumers and businesses on energy costs and through other measures. However, there will still be challenges for many of your customers and life insurers have a critical role to play in helping them. It is important that life insurers meet the standards we expect to support customers, including those in financial difficulty. Consistent with the Consumer Duty, which comes into force next year, we also expect that life insurers consider how they act to deliver good outcomes via their customer propositions in the changing economic environment.

We are now setting out our expectations of life insurers, following the Dear CEO letters we published for lenders on 16 June 2022 and general insurers on 29 September 2022, and several conversations held directly with CEOs. Life insurers active in the lifetime mortgages market should also consider the messages on the rising cost of living set out in our portfolio letter to CEOs on 29 June 2022. In summary, our expectations of life insurers include:

- Protection products: We expect life insurers to ensure customers are provided with appropriate product information during all stages of communication and to make customers aware of the options available to them if they have difficulty paying premiums.
- Pensions, long-term savings and retirement income: We expect firms to take reasonable steps to make customers aware of their options and the consequences of accessing and stopping or reducing contributions to pensions and long-term savings, as well as highlighting to customers the potential risks associated with their chosen investment or drawdown strategies.
- Customer value: Firms have told us that they expect heightened demand for annuity products due to the significant increase in rates over this year and potentially for equity release / lifetime mortgage products among older consumers. We expect firms to ensure that these propositions offer fair value to customers. This is particularly important when lending on a long-term fixed rate in a higher interest rate environment.

- Customer support: Firms should be supporting customers showing signs of financial difficulty or struggling with debt. This should involve consideration of our Covid insurance and premium finance guidance. Supporting customers includes considering the needs of those with characteristics of vulnerability – our Vulnerable Customer Guidance sets out our views of what firms should do to comply with their obligations under our principles and ensure they treat customers in vulnerable circumstances fairly.
- Scams: We also believe an increasing number of consumers are vulnerable to scams. Life insurers should ensure anti-scam communications are used to protect customers where possible.
- Operational resilience: Life insurers should also consider what affect the rising cost of living will have on their operational resilience, including supporting their staff and effectively managing third party providers to reduce the risk of operational disruption.

This is not an exhaustive list of our expectations. In the year ahead we may undertake multi-firm reviews and will act on firm-specific intelligence to check that firms are meeting our rules and guidance.

Protection products

Insurers may see an increase in the number of protection products lapsing or being cancelled. Insurers should make sure they monitor policy arrears or cancellations and understand the underlying drivers for any trends. Insurers should then consider how to ensure customers are given the assistance they need.

Where it is recognised that customers are in financial difficulty, we expect insurers to take a flexible approach to deliver a fair outcome for them. This may include offering flexible payment strategies or increasing premium holidays. Insurers should include consideration of our Covid insurance and premium finance guidance.

It is essential that insurers act to ensure customers are provided with information which allows them to make informed decisions about their protection insurance products. Insurers must make customers aware that any immediate decisions, such as to reduce cover or cancel a policy, could have longer-term implications (eg the inability to subsequently reinstate the protection or that new underwriting terms may be required for a new policy).

Where there are products that have regular reviews which could result in premium increases, insurers should be aware of how this can affect customers who are likely to be financially stretched in other areas. We have seen examples of reviewable Whole of Life products where premiums have increased significantly with little notice to customers. Communication to customers should be timely and must clearly outline the reasons for increases and the options a customer has.

While not a direct consequence of the current increases to the cost of living or the changes to market conditions, these nonetheless make it even more important for insurers to ensure that their life protection products offer fair value to customers and that these products and the levels of cover are appropriate for their needs. For pure protection products (life cover such as term assurance, whole of life, or Over 50s plans, critical illness, or income protection without an investment element), the FCA's rules set out in PROD 4 introduced product governance and fair value assessment requirements which, if fully complied with, will satisfy the products and value elements of our new consumer duty rules. We expect that insurers are already fully complying with these requirements.

Pensions, long-term savings and retirement income

We expect to see customers' saving and investment patterns alter because of the rising cost of living, with firms already indicating that customers are considering reducing or stopping pension contributions. While this may be appropriate for some customers who face immediate financial pressures, we look to insurers to make customers aware of their available options and the short and long term risks of doing this, such as losing out on employer contributions and the increased risk of insufficient funds at retirement. Where insurers are seeing customers reducing their contributions, we expect insurers to keep appropriate data and consider how to continue to engage with customers, making it as easy as possible for them to restart their contributions.

There is potential for customers to increase the level of investment risk they are taking to boost expected income in retirement, or to make hasty decisions in the face of market volatility. However, some customers with lower-risk strategies may find their investments not keeping up with inflation. Regardless of circumstances, insurers must ensure that customers are provided with adequate information to make them aware of their saving and retirement options, including the risks involved in their current investment strategy and any tax implications of taking money from their pensions.

We think it is likely that more customers will access pensions and long-term savings for the first time or at an increased rate because of the rising cost of living. Again, while this may be appropriate for some customers facing immediate financial pressures, we expect insurers to make customers aware of their options and the related consequences (including providing retirement risk warnings (COBS 19.7) where relevant). Insurers should be proactive in contacting customers where potential future harm is predicted. This may include using trend analysis to identify customers facing potential harm and providing much earlier information to customers who could be at risk of drawdown exhaustion.

Customer value

Over the course of this year, market conditions have changed significantly, with higher interest rates and increased volatility. Customers and firms were accustomed to a lower interest environment and the changes this year have the potential to change the customer value of insurers' propositions, as well as customers' attitude to risk. We expect firms to consider what these changes might mean for their customers, what value their propositions provide to their customers and whether the product design will support good customer outcomes in line with our expectations under the Consumer Duty once this comes into force.

We have heard from firms that they are expecting increased demand for annuity products from retail customers due to the significant increase in rates already observed this year. Given the significance of this retirement decision for consumers, and that they will be locking into an annuity rate for life, we expect firms to ensure that the prices offered are fair value to consumers and that, in accordance with our rules on pension annuity comparison information (COBS 19.9), firms make clear to them that they may be able to achieve a higher rate by shopping around on the open market, including for impaired / enhanced annuities. This should be shown prominently, clearly and in an engaging way in the documentation a customer receives.

While the market for retail annuities might be price-competitive, we understand that pricing may be used as a way to manage a firm's capital budget (eg reducing annuity rates to be less attractive to avoid selling too much relative to the available capital budget or operational capacity). Insurers should ensure that relative to market conditions / yields on assets being used to back annuities, they are still providing fair value for those customers buying their annuities. Firms have also told us that they expect there to be increased demand for equity release / lifetime mortgage products from consumers seeking additional funds in later life. Given both the increased interest rate environment and potentially greater uncertainty about residential property market values, we expect firms to be actively considering whether these propositions are priced and structured to offer fair value overall. We have already heard from some firms that higher interest rates start posing a question about whether these products offer fair value to all customers.

Customer support and scams

We are aware that financial advice will not be affordable or available for many customers. Insurers should ensure that they signpost customers effectively to sources of guidance to help them navigate their options and find out what help is available. This includes signposting via the Stronger Nudge to PensionWise and more generally to organisations providing money help or free debt advice.

We believe increased numbers of savers could be vulnerable to scams. Insurers should detect, report and disrupt scams and ensure anti-scam communications are used to protect customers where possible. We expect firms to have a clear process in identifying customers that may be vulnerable to scams at an early stage and have suitably trained staff to deal with these situations.

As frontline services are likely to experience increasing contact from customers who are affected by the rising cost of living and presenting with a complex range of vulnerabilities, we expect firms to provide customers with an appropriate level of care and support and frontline staff to be suitably prepared.

We expect staff to be well-trained, knowledgeable and capable of having complex conversations with vulnerable customers and those in financial difficulty. Staff should also be able to respond flexibly to customers' needs and circumstances (eg empowered to offer tailored forbearance if appropriate and signpost to other sources of assistance like debt management).

Operational resilience (including outsourcing)

Ensuring the UK financial sector is operationally resilient is important for consumers, firms and financial markets. Operational disruptions can cause wide-reaching harm to consumers and pose a risk to market integrity, threaten the viability of firms and cause instability in the financial system. As set out in PS21/3 - Building Operational Resilience, it remains critically important for insurers to understand the services they provide, including those undertaken by outsourced service providers, and invest in their resilience.

The ongoing reliability of critical business services remains essential for millions of customers who are dependent on UK insurers making regular income payments (eg retirement annuities and drawdown; income protection payments). For many, these payments will be their only source of income.

Increased demand from customers who are experiencing financial difficulties could affect firms' ability to maintain adequate levels of customer servicing and completion of key business activities within agreed service level agreements (SLAs). This could lead to increased errors and rule breaches occurring with delays contributing to the development of operational backlogs.

You should ensure you have robust governance arrangements and effective tools in place to identify, manage, monitor and report the risks you may be exposed to. We expect monitoring to include customer behaviours and the actions they are taking (eg drawing down retirement proceeds quicker; increased lapses) so you can adapt and respond more quickly to changing circumstances. You should consider different scenarios that may test your operations, to ensure that your internal processes and control mechanisms are adequate.

For firms which use outsourced service providers as part of their business model, we expect these providers to be effectively managed to reduce the risk of operational disruption and harm to their consumers as set out in our Outsourcing and Operational Resilience and Outsourcing in the Life Insurance Sector publications.

We also expect firms to oversee the distribution of their products, including oversight of intermediary distribution, to ensure harm does not occur. The FCA's Conduct of Business Sourcebook (ICOBS) and product governance and oversight rules (PROD 4) place obligations on the insurer to oversee the distribution of their products.

In addition, we expect firms to respond and support their workforce, recognising that staff may be directly affected by the increasing cost of living and experiencing financial hardship, vulnerability, or stress themselves; particularly those on the frontline working in operationally challenged areas. Where this is not well managed, this may lead to increased absenteeism and attrition which may harm the effective operational resilience of key business processes.

Next steps

Please consider the content of this letter and act to ensure your firm is well placed to support your customers now. We will continue to monitor and scrutinise firms using our supervisory and enforcement powers where necessary. We are also considering options for consultation on adapting our insurance Covid guidance for customers in financial difficulty.

In PS22/9, setting out our final rules for the Consumer Duty, we set an expectation that firms' boards should have agreed their implementation plans and how they will maintain oversight of delivery by the end of October 2022. We do not expect all firms to have fully scoped all work required, but we do expect firms to have a plan for this. Firms should be mindful of work that needs to be undertaken with other parties (including any outsourced service providers they work with) to prepare for the Duty.

We look forward to working together to promote good outcomes for consumers. If you have any questions, please contact your usual firm supervisor or the FCA Supervision Hub.

Yours sincerely

Sheldon Mills
Executive Director