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**August 2025 update:**
**This letter is historical. See our supervisory correspondence page for more information and current views.**

08 January 2020

Dear Board of Directors,

## Portfolio strategy letter to firms in the Personal & Commercial Lines Insurer (PL&CL) portfolio: identifying and remedying harms

We are writing to set out our view of the key risks of harm PL&CL firms could pose to their consumers and the markets in which they operate. It outlines the drivers of the harms and, outlines our supervisory strategy in relation to these. The key risks of harm identified in this letter form part of our wider supervision of your firm and you can expect there to be greater focus on these to the extent that they are relevant to you. Our strategy covers the period to January 2021.

### What we mean by Portfolios

A portfolio is how we group firms based on their business model. Each portfolio is made up of firms with broadly similar business models. We have allocated your firm to the Personal Lines and Commercial Lines insurers (PL&CL) portfolio.

We will write regularly to all firms within a portfolio to share our expectations, priorities and examples of good or poor practices for the group. Our intention is to next do this during 2021.

### What we expect

Our view of the General Insurance (GI) sector overall is that there are significant risks of harm that both the market and individual firms need to address. In doing so, we require PL&CL firms to deliver a step-change in their culture. This includes prioritising their focus on conduct and consumer outcomes throughout the customer journey.

Firms need to significantly improve their governance and operational controls. This includes how they proactively engage with, plan for and implement all relevant regulatory changes. We see firms' effective implementation of regulatory changes, such as those introduced by the UK implementation of the Insurance Distribution Directive (IDD), as fundamental to ensuring both the GI market treats consumers fairly and that consumers have products that meet their needs. As part of this, we expect all firms to have reviewed their customer journeys and made any necessary amendments to meet the regulatory requirements. We also expect Boards to hold firms and Senior Management to account on their engagement and timely delivery of regulatory change.

Firms should consider the degree to which they present risks of harm to consumers and markets and have implemented effective strategies to mitigate these risks. Where we identify firms that have not taken sufficient steps to do so, we will intervene and consider all our regulatory tools to take appropriate action.

### Our view of the key drivers of harm

We have analysed firms' strategies, business models, and drivers of culture, including governance arrangements and purpose. Our analysis has assessed when, how, and to what extent different types of harm may arise. Based on our analysis, we will prioritise our supervisory work in the following areas:

- poor oversight of, and poor remuneration practice in, distribution chains
- risk of consumers being provided with unsuitable or poor value products
- poor pricing practices
- ineffective management of some regulatory change and
- poor operational controls

### Firm business models and strategies

PL&CL insurers vary significantly in their size and type of business. Many focus primarily on personal lines business, others only offer commercial business, and some multi-line insurers provide both. Their use and means of distribution also varies considerably. Pressure from declining investment returns and some features of firms' business models have led to harm.

Below we outline some of these harms and their drivers, and what we expect firms to do to address them.

#### *Poor oversight of, and poor remuneration practice in, distribution chains*

Our GI distribution chain report identified significant potential harm from the product oversight and distribution approaches of some sectors of the GI market and by some GI firms. For example, consumers paying increased prices due to remuneration paid to firms in the distribution chain, where those firms incur little cost or deliver little benefit to consumers.

Alongside the report we consulted on, and have subsequently finalised, guidance making clear that we expect firms to consider the value the product offers to the end consumer and the impact that the distribution strategy/chain has on that products value. We expect firms to have reviewed the report, the associated Dear CEO letter and the final guidance and to have identified and addressed any gaps in their approach.

We will consider this when undertaking our firm facing work. We will take appropriate supervisory action where we identify firms that are not meeting expectations.

#### *Risk of consumers being provided with unsuitable or poor value products*

We have seen firms selling products which are unsuitable or of poor value to consumers. This is unacceptable. We expect firms to take appropriate action where they identify products are delivering poor value, and to ensure products are being sold that meet consumer needs.

The IDD implementation strengthened conduct requirements and in places introduced a range of requirements in new areas. There are requirements for firms to ensure consumers are better informed about products, and to propose only those products which are consistent with the consumer's insurance demands and needs. We are planning a broad programme of work to include industry engagement, further multi-firm work to assess levels of compliance with the regulatory changes brought about by the IDD implementation - including how customer journeys have changed - and engage with individual firms where we identify non-compliance and poor consumer outcomes. As part of our focus to improve the delivery of better value products we consulted on requirements for firms to use GI value measures, as part of their monitoring and governance of insurance products. Firms need to keep up to date with these proposals as they develop.

***Poor pricing practices***

Our thematic report on household insurance pricing practices found that many firms' pricing decisions appeared to focus primarily on achieving business plan and financial objectives without appropriate consideration of consumer outcomes. The report also identified the potential for harm from differential pricing where some identifiable groups of consumers are paying significantly higher prices than others with similar risk and cost-to-serve characteristics.

In response to these concerns, we started a Market Study into general insurance pricing practices. We published our interim report in October 2019. This stated that pricing practices in the home and motor insurance market are not working well for all consumers.

Industry has acknowledged the need to address concerns about pricing practices and has been taking some steps to do so. However, we are also considering potential options for regulatory intervention and will issue our final report in early 2020.

This remains an area that requires significant improvement and we expect firms to have already delivered changes to improve their governance and practices in line with relevant FCA policy and supervisory work.

We have also, for example, found that some firms' practices might deter consumers from switching at renewal, for instance with consumer communications which might discourage consumers from making active decisions. We remind firms that communications should be clear, fair and not misleading. We also found that some firms require consumers to contact them by phone to cancel auto-renewal, even if they originally took policies out online. Outcome 6 of the consumer outcomes that firms should strive to achieve to ensure fair treatment of customers says firms should ensure 'consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.' Firms should review their current practices and consider whether they are in their consumers' interests.

***Firms failing to properly establish a consumer's ability to enter into - or increase borrowing under - a regulated credit agreement***

Consumers may be harmed where firms extend credit to them and they are not able to repay without suffering harm.

We have found that some firms are not considering sufficiently the potential costs and risks to consumers of borrowing to fund their insurance cover. In November 2018, we established new rules and guidance on assessing creditworthiness, including affordability, in consumer credit. Some firms are not complying with our creditworthiness rules, for example their assessments focus solely on credit risk rather than establishing affordability. Through our ongoing multi-firm work, we are requiring firms to make necessary changes to correct this.

### Governance arrangements and firms' culture

As set out in our 2019/2020 Business Plan, firms' culture and governance is one of our key cross-sector priorities. Firms' culture, alongside their business model and strategy, shapes the outcomes for consumers and markets. Our aim is for each firm to assess and address its drivers of culture; leadership, purpose, governance and also its approach to managing and rewarding employees.

The speech we delivered at the British Insurance Brokers' Association (BIBA) Conference 2019 underlined our view that the insurance sector needs to make a step-change in its approach to conduct and culture. Poor culture in financial services is now widely recognised as a key root cause of the major conduct failings of the financial services industry, causing harm to both consumers and markets. We expect firms' culture and governance to drive good behaviours and produce fair outcomes that are likely to benefit consumers and markets, and for individuals to be accountable for their actions. Although the market has undertaken work to tackle the problem, it still appears to be a significant issue. Clearly, much more needs to be done to tackle poor behaviours and their underlying causes.

We want Boards and senior management in firms to prioritise embedding a healthy culture, with consumers at the heart of their business. We have seen failings that can often be traced back to weaknesses in governance, senior manager accountability and employee incentives.

The failings include:

#### *Poor governance around firms' decision-making on pricing strategies:*

Our thematic report on household insurance pricing practices identified that some firms did not have effective governance over their pricing practices. This meant they could not reliably assess and evidence how their pricing decisions affect consumers and ensure fair outcomes.

Concurrently, we also published a Dear CEO Letter which reiterated that good governance of pricing outcomes for consumers should be central to firms' pricing practices. We have engaged with several firms on their response to the letter and found some are still not meeting our expectations. We are taking supervisory action to ensure firms address this.

#### *Incentive arrangements which do not support a positive conduct culture:*

We have seen examples of poor governance of incentive arrangements that drive behaviours that harm consumers.

We have found this is often caused by incentive structures which focus primarily on financial metrics – without taking broader factors into account. We have already assessed some firms' remuneration policies and the remuneration of individuals to ensure practices reinforce a healthy culture and do not drive the wrong behaviours. Where appropriate, we will continue to do this and meanwhile, expect firms to be taking this action themselves.

***Ineffective management of some regulatory change:***

A lack of clear accountability has led to firms managing some regulatory change poorly. This includes our rules on complaints handling, disclosure at renewal and the requirements introduced by the IDD.

The Senior Managers and Certification Regime (SM&CR) aims to reduce harm to consumers and strengthen market integrity by creating a new system that enables firms and regulators to hold people to account. It will also help us to be more interventionist in future, and presents a unique opportunity to set a new standard of personal conduct for everyone working across the industry.

While firms typically engage closely with the Senior Managers Regime, they should be aware that the Certification Regime and Conduct Rules are also fundamental parts of the SM&CR regime. We expect all SM&CR firms to ensure they are fully embedding the SM&CR requirements in their business. We will continue to engage with individual firms to assess how they have implemented the SM&CR.

We will hold senior managers accountable for the harms we identify.

## Poor operational controls

Firms must ensure they have effective systems and controls in place right across their business, including key areas such as the three lines of defence, third party oversight, and their overall operational resilience.

We have seen examples of firms failing to offer sufficient protection of consumer data, resulting in data breaches. There is still a risk of harm from more frequent and widespread cyber-attacks in this market. This is potentially exacerbated by complex and ageing IT systems, outsourcing of operations and the increasing frequency of data transfer between firms.

PL&CL firms must ensure that their technology and systems are resilient to outages and cyber-attacks. Our Operational Resilience discussion paper highlighted the risks from cyber-attacks and disruptive operational incidents. We subsequently published a co-ordinated consultation paper with the Bank of England and the PRA setting out proposals for firms to set impact tolerances for their important business services and take steps to remain within those tolerances. Firms should keep up to date with developments in this area and consider the use of these proposed principles to strengthen their resilience to prevent such incidents, and to minimise the resulting harm to consumers and markets – as well as to a firm's viability.

We will also continue to focus on the importance of firms strengthening their information security controls by using ethical-hacking (CBEST) to assess firms' ability to detect and respond to cyber-attacks.

## Brexit

The UK government has committed to the UK leaving the EU with a Withdrawal Agreement on 31 January 2020. If that happens, we will enter an implementation period during which the UK will negotiate its future relationship with the EU. The implementation period is due to operate until 31 December 2020. During this time EU law would continue to apply in the UK and passporting would continue. We expect you to consider how the end of the implementation period will affect you and your customers, and what action you may need to take to be ready for 1 January 2021. For information on Brexit, including what an implementation period will mean, visit our website. We will update our pages after 31 January 2020 to reflect the UK's new status.

## Next steps

We will continue to engage with PL&CL insurers in 2020 through our planned programme of work.

We will write to you again in early 2021 to provide our updated view of the key risks firms in this portfolio pose, the extent to which these risks are being mitigated, and our updated supervisory plans as a result.

We expect firms to keep up to date with regulatory development generally and with the areas covered in this letter.

If you have any questions please contact your normal supervisory contact or call us on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with the FCA. Further details of how we can be reached are available on our website at https://www.fca.org.uk/contact.

However, we recognise that there may be occasions in which your firm faces urgent issues of strategic importance. In such significant circumstance, if I am not available, please contact the Lead Associate responsible for the PL&CL Portfolio, Nikesh Vaghela at Nikesh.Vaghela@fca.org.uk.

Yours sincerely

Roma Pearson
Head of Department
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