Financial Conduct Authority

Increasing transparency and engagement at renewal in general insurance markets

December 2015

Consultation Paper

CP15/41**

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We are asking for comments on this Consultation Paper by 4 March 2016.

You can send them to us using the form on our website at:
www.fca.org.uk/consultation-papers/cp15-41-response-form

Or in writing to:

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We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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Abbreviations used in this paper

ABI	Association of British Insurers
BIBA	British Insurance Brokers Association
CIDRA	Consumer Insurance (Disclosure and Representations) Act 2012
FCA	Financial Conduct Authority
ICOBS	Insurance Conduct of Business Sourcebook
RPPD	The Responsibilities of Providers and Distributors for the Fair Treatment of Customers
RCT	Randomised Controlled Trial. See Occasional paper: Encouraging Consumers to Act at Renewal

1. Overview

Introduction

1.1 This paper sets out proposals to introduce new rules and guidance for firms on steps they should take when renewing general insurance policies. These proposals address concerns about levels of consumer engagement and their treatment by firms at renewal, and the lack of competition that results from this. This can result in consumers defaulting to renew products that are not good value or have become unsuitable for their changing needs.

1.2 We are proposing:

- Rules that require firms to disclose last year's premium on renewal notices
- Rules that require additional disclosure when customers have renewed the same product four times or more
- Guidance on how firms can improve their processes around renewals
- Guidance about records that firms maintain to demonstrate compliance, including a record of premiums.

1.3 We also remind firms of their obligations to Treat Customers Fairly when developing their overall approach to renewal pricing and in their treatment of long-standing customers.

1.4 We expect firms to present the new disclosure clearly and to take active account of our discussion paper, *Smarter consumer communications.*[1]

1.5 Our proposed measures aim to increase engagement and promote competition through enhanced disclosure. We will assess the outcomes from these proposals before deciding whether we need to intervene further to address remaining inertia or other barriers to competition. The Department for Business, Innovation & Skills' call for evidence on switching principles will be useful for informing any future action.[2] Firms maintaining records of past premiums will help us consider whether further interventions are required.

1.6 Overall, our package of measures, and the increased stakeholder attention, will mean that firms should increase their focus on renewal pricing, and as a result improve consumer outcomes.

1 FCA, Discussion paper, Smarter consumer communications, http://www.fca.org.uk/static/channel-page/dp-smarter-comms/dp-smarter-comms-index.html

2 Department for Business, Innovation & Skills, Call for evidence: switching principles, October 2015. https://www.gov.uk/government/consultations/switching-suppliers-making-it-easy-for-consumers

Who does this consultation affect?

1.7 We are consulting on measures applying to insurers and intermediaries selling retail general insurance products.

Is this of interest to consumers?

1.8 The intention of these proposals is to benefit consumers when renewing their general insurance policies. We encourage consumers to consider their options at renewal to ensure their insurance cover is good value and remains suitable for their needs.

What have we done?

1.9 In 2014 we launched a large scale randomised controlled research project with over 300,000 customers from one home insurance and two motor insurance providers to assess whether improved disclosure can help consumers become more engaged at renewal. We also used information about approaches to renewal pricing from a sample of three firms. Full details of the research project are in Occasional Paper, *Encouraging Consumers to Act at Renewal*, published alongside this paper.[3] We tested four types of disclosure. Of these, we found that putting last year's premium on renewal notices had the biggest impact in increasing consumer engagement.[4] However, this was less effective for consumers who did not have large year-on-year price increases. Our research indicates that these consumers are more likely to have been with the same provider for over five consecutive years on average.

1.10 We also reviewed findings from our 2013 thematic review of auto-renewal terms in home and motor insurance markets, stakeholder views and complaints data. We found that the renewals practice of some firms could be improved to help consumers engage and make better informed decisions.

1.11 Our work suggests that disclosure and improving firms' practices can increase engagement, but are unlikely to fully address consumer inertia when renewing general insurance policies. There may be other reasons that explain why consumers do not act at renewal.

Summary of our proposals

1.12 We propose a new requirement for firms to disclose last year's premium on renewal notices for retail general insurance policies. The information must be clearly shown and allow comparison with the quoted renewal premium. Firms must also give information to encourage consumers to shop around and check their cover. Firms can provide other relevant information, including details of mid-term adjustments or the end of introductory discounts. However, this information must be in addition to the required disclosure and not obscure it.

3 FCA, Occasional Paper no. 11, Encouraging Consumers to Act at Renewal, http://fca.org.uk/news/occasional-paper-no-12

4 Disclosure tested: including last year's premium next to this year's premium in renewal notices; sending a leaflet with renewal notices i.e. a guide to shopping around or glossary of terms; simplifying renewal notices by using bullet points and simplifying language; and sending reminders two weeks after renewal notices are issued.

1.13 In order to work most effectively, we are proposing to allow firms to implement a format appropriate to their customer communications. We set out below one version of how firms might consider meeting the requirement to disclose last years' premium:

Your renewal quote for this year is:	£200.00
Last year's premium was:	£150.00
This is £50 more than last year.	
Remember:	
Check your cover	
Shop around for the best deal	

1.14 We are also proposing additional disclosure for consumers who have already renewed a product four times, i.e. consumers that have been with their provider for five consecutive years. These consumers must be provided with the following statement that encourages them to shop around: *"You have been with us for over five years. You may be able to save money if you shop around"*.

1.15 We also remind firms to consider how they are meeting their obligations under Principle 6[5] to treat customers fairly in respect of renewals. Specifically, firms need to be able to demonstrate how their renewal pricing in general, and their treatment of long-standing customers in particular, delivers fair outcomes to consumers. We specifically draw firms' attention to the needs of vulnerable consumers at renewal and highlight our recent occasional paper on Consumer Vulnerability.[6]

1.16 We have identified some additional ways that firms can improve their renewal processes in line with existing requirements. We are consulting on guidance to help firms understand what is required under the rules in respect of communications at and about renewal. This will support consumer decision-making and help address barriers to switching.

1.17 Finally, firms are already required to maintain appropriate records to demonstrate compliance with regulatory requirements. We propose guidance that makes clear to firms how our record keeping requirements apply to these changes and that they must keep records of past premiums to comply with these renewal requirements.

Equality and diversity considerations

1.18 We have assessed the likely equality and diversity impact, and have not identified any material issues. We welcome your comments on our assessment.

5 See PRIN 2.1 - Principle 6 Customers' interests: A firm must pay due regard to the interest of its customers and treat them fairly.

6 FCA, Occasional paper no.8, Consumer Vulnerability, February 2015. http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-8

Next steps

What do you need to do next?

1.19 We want to know what you think of our proposals. Please send us your comments by 4 March 2016. You can either use the online response form on our website or write to us at the address on page 2.

What will we do?

1.20 We will consider all responses and aim to provide finalised rules and guidance and a Policy Statement by mid-2016.

2. Increasing engagement and transparency with disclosure

2.1 This chapter sets out our proposal for firms to disclose last year's premium and additional information on renewal notices.

Consumer Engagement and Competition at Renewal

2.2 A range of stakeholders, including consumer groups and industry, have told us about poor outcomes for consumers from renewal pricing practices in general insurance. These concerns have mainly been about the high premiums consumers pay at renewal when cheaper options are available, and a lack of transparency about price changes. Complementing our research project, in the 2015 Summer Budget, the Government asked us to review what we can do to encourage people to shop around when they renew their insurance.

2.3 Consumers are engaged when they first purchase a product, which puts pressure on firms to keep prices down and increase value. However, once the policy is in place and firms offer to renew it, for a number of reasons consumers can be significantly less engaged and therefore may not make an informed decision about the new policy terms. This can mean that consumers repeatedly accept price increases rather than negotiate or switch provider.

2.4 Our research has considered how to better engage consumers who renew their policies. The findings set out in the Occasional Paper suggest that home insurance customers underestimated the benefits to shopping around and overestimated the time it takes to switch. It is reasonable that these customer views would apply more broadly to other general insurance products where switching is not high. Overall, the evidence suggests that some consumers do not shop around, switch or negotiate when they rationally should.

2.5 If consumers do not consider the renewal information or engage with it, then they cannot make an informed decision. Firms know that they can charge higher premiums for renewal policies if customers are unlikely to pay attention to the size of the increase. Consumers may also fail to reassess their insurance cover to check whether their policy still meets their needs. Where consumers engage and are given the information to help them make an informed decision and then choose to remain with the same provider, we are less concerned.

2.6 However, where consumers are not encouraged to engage they often do not have the opportunity to make an informed decision. Our objective is to prompt consumers to engage in the renewal decision, increase transparency and improve competition by encouraging consumers to shop around. When consumers engage, they are in a better position to make an informed decision. They are also more aware of their choices; to stay with the same provider, switch provider or negotiate a better deal. By increasing engagement, we expect our proposals to put pressure on prices at renewal.

Findings on effective disclosure

2.7 We trialled four different disclosure options with customers in our testing: including last year's premium next to this year's premium on renewal notices; sending a leaflet with renewal notices; simplifying renewal notices by using bullet points and simpler language; and sending reminders two weeks after renewal notices.

2.8 We found that disclosing last year's premium was the most effective way to prompt consumers to shop around, cancel or negotiate their insurance policy:

- Customers were offered an average renewal price increase of over 5% for home (property and contents) insurance and including last year's premium in renewal notices caused 11-18% more consumers to switch or negotiate their policy.

- Where the average renewal price increases for two motor insurance providers were 0% and 5%, we found no statistically significant impact in switching or negotiating when last year's premium was included. However, survey evidence from one motor insurer suggests that including last year's premium increases shopping around by 7.3 percentage points. This suggests that people were engaged by the disclosure, but decided not to act.

2.9 We found that some firms have already introduced disclosure of last year's premium or are currently considering this. Consumer body Which? and the Association of British Insurers among other stakeholders have publicly supported this proposal.

2.10 We found that disclosing last year's premium had less effect on promoting engagement when price increases were small. Consumers renewing with the same provider for many years may pay significantly higher prices than if they shopped around, even if their most recent price increases were incremental or small. So we are proposing additional disclosure for consumers who have held an insurance product for five years.

2.11 We did consider whether there are alternatives to disclosure of last year's premium which might further increase engagement but which we did not test in the trial. For example, we considered whether to require disclosure of new business equivalent premiums or the lowest premium over time. These options are likely to show the large price differentials that appeared to prompt switching as we found with disclosing last year's premium. However, we decided against these options because, in comparison with last year's premium, they could be confusing for consumers, introduce practical implementation difficulties and higher costs for firms and give rise to potential unintended consequences.

Disclosure of last year's premium

2.12 We propose that firms are required to disclose last year's premium in a prominent position in relation to the new premium. This will be the premium the customer paid at the start of the previous year. Including this information in renewal notices increases transparency and highlights price changes to encourage consumers to give more attention to the proposed renewal premium. Disclosing last year's premium involves firms providing a simple figure that consumers will find easy to compare.

2.13 We considered whether to include mid-term adjustments (or other changes in the consumers' risk profile) in the calculation of last year's premium.[7] These adjustments are common and arguably provide a more accurate basis for comparison as they reflect an updated understanding of the consumer's cover and needs.[8] Our preferred approach is to require last year's premium as set at the beginning of the previous term as it strikes the right balance between engagement, simplicity and costs for firms. We will not prevent firms from providing other information (such as mid-term adjustments) as well as last year's premium. However, our proposed rules are clear that providing extra information should not dilute the simple disclosure of last year's premium.

2.14 We propose that last year's premium should be set out in a way that is consistent with the presentation of the renewal premium so that the consumer can easily compare the two. For example, if the renewal premium is quoted as a single amount, the previous premium should also be set out as a single amount.

Q1: Do you agree with our proposal that firms should disclose last year's premium on renewal notices?

Q2: Do you agree with our proposal that the premium displayed should be the premium the consumer started the year with, but that firms can include other information, such as mid-term adjustments?

Additional disclosure – all consumers

2.15 We considered whether other information should be shown as well as last year's premium. We propose that firms remind consumers to check that the proposed policy still meets their needs and shop around. Encouraging consumers to check their cover helps them focus on the overall value of the policy; consumers will make better decisions if they consider coverage and value rather than price alone.

2.16 Some stakeholders suggested that firms should be required to provide additional information including an explanation of premium changes or how discounts are applied. We consider that firms wanting to retain customers already have an incentive to provide information to consumers justifying price changes, and that many firms will do this already (albeit often after a query from the consumer).

2.17 Further, firms must currently provide customers with appropriate information so they can make an informed decision about proposed arrangements. In our draft guidance (see chapter 3 and Appendix 2), we encourage firms to consider how they are communicating information about changes to policy terms and conditions, so that consumers can most effectively make an assessment about whether the policy remains suitable.

2.18 We are mindful of the impact of too much information on consumer engagement and do not propose to introduce new rules requiring this additional disclosure at this time. However firms can choose to provide this information if they believe their customers would benefit.

Q3: Do you agree with our proposal that firms must provide information to consumers to: check the proposed policy continues to meet their needs and to shop around?

7 Examples of mid-term adjustments include adding another driver or changing your address on a motor insurance policy.

8 Information from one trade body suggests that the number of mid-term adjustments could be significant: affecting between 20% to 55% of intermediated policies.

Additional disclosure – for consumers who have renewed repeatedly

2.19 Disclosing last year's premium has a stronger effect the bigger the relative price increase on the previous year. This is important as we also found that while consumers who renew with the same provider for over five years may not receive sharp price increases each year, they can ultimately pay significantly more than new customers. This indicates that disclosing last year's premium may not have as great an impact on these consumers and they may need an additional prompt to engage.

2.20 We therefore propose that firms should give additional information to any retail customer who has renewed at least four times, i.e. kept the same product for five or more years. This information would prompt consumers further by reminding them about how long they have stayed with the same provider and the benefits of shopping around. We propose that this rule would apply to existing customers who meet the criteria (i.e. if a firm has a customer who has renewed five times when the rules come into force, the firm would provide this additional information to that customer as well).

2.21 From year five onwards, we propose that the renewal notice should include the following message in the same section as the last year's disclosure information: *"You have been with us for over five years. You may be able to save money if you shop around"*

Q4: Do you have any comments about this additional disclosure? Do you have any suggestions for the proposed message to consumers?

Presentation, scope and timing

Presentation of the information

2.22 We propose that the prescribed information is included on renewal notices in a position that makes it easy to compare with the renewal quote. The information must be shown clearly, accurately and prominently. We expect firms to take account of our discussion paper, DP15/5: Smarter Consumer Communications, when they implement the final proposal. Our findings from the trial suggest that including the disclosure on the front page is a prominent position that would be effective at engaging the consumer.[9] We would suggest that including the information towards the top of an online communication would have a similar impact.

2.23 We set out on page 7 one version of how firms might consider meeting the requirement to disclose last year's premium.

Q5: Do you have any comments on how the disclosure should be presented to the customer?

9 Firms testing disclosure of last year's premium all included the information on the front page of their renewal notices. Additionally, in the consumer survey for the trial, we asked consumers from two firms who renewed whether they read their renewal letter. At Firm A, 28% read the letter in detail and 44% skim read or read the first page. At Firm B, 23% read the letter in detail and 39% skim read / read the first page.

Scope of the requirement

2.24 This disclosure is intended to increase engagement and transparency and improve consumer decision-making at renewal. These objectives do not just apply to the home and motor insurance markets which our research focussed on. We therefore propose to apply the disclosure requirement to all general insurance products and whenever the firm provides an existing customer with the same, or similar, policy for a further term. The measure will apply to both automatic and manual renewals. If the insurance product was, or becomes, free, the disclosure requirement will apply.

2.25 The measure should only apply to sales to retail customers (consumers).

2.26 Customers can receive renewal information from either the insurer or an intermediary. To ensure consistency for all consumers, we propose that the requirement apply to the firm (insurer or intermediary) who provides the renewal communications to the customer. Our proposals apply to all distribution channels, whether direct or intermediated, and any medium (ie online or paper-based).

2.27 We propose to exclude policies with a term less than a year, e.g. a monthly policy. As these kinds of policies are renewed more regularly, the consumer is more likely to be aware of the previous premium without the need for additional disclosure. Any policy of a year or longer would be covered, and the 'last year's premium' would be the previous term's premium. We welcome views on this point, and specifically whether there are policies shorter than a year (but not monthly) that should be within scope.

2.28 Where a renewal notice covers a bundle of products, the requirement to disclose last year's premium applies to the total package. For example, for a motor insurance policy with breakdown and legal expenses cover as add-ons, we expect the firm to provide last year's premium on the total package rather than each insurance policy in the bundle. The firm will still need to tell the customer the prices for individual add-on policies, as required under the Insurance Conduct of Business Sourcebook (ICOBS).

Q6: Do you agree with the proposal to apply the measure to all situations where a general insurance policy is renewed with a retail consumer with the exception of policies with a term of less than a year?

Demonstrating compliance

2.29 We expect firms to be able to demonstrate they are complying with our disclosure requirements, including by maintaining appropriate records as required under the Systems and Controls Sourcebook (SYSC). This would include maintaining a record of premiums. We propose guidance to make this clear to firms. Maintaining such records would also support any future intervention we may consider.

Implementation timing

2.30 We propose an implementation date of 1 January 2017 for these proposals. This is just over 12 months from the consultation start date and is informed by firms' views about how long it would take to implement.

2.31 We have taken account of the disclosure requirements in Insurance Distribution Directive (IDD) to the extent that we can at this stage. We will continue to assess how our proposals interact with the IDD as we consider feedback and finalise rules and guidance.

Q7: Do you have any comments about our proposed implementation of 1 January 2017 for the disclosure measures?

3. Improving renewal practices

3.1 Disclosing last year's premium will encourage consumers to think about their renewal options. We expect consumers to make more informed decisions, and to see increased shopping around, switching and negotiating as a result. We also expect that these changes will lead firms to focus on their pricing strategies and consequently for consumers to achieve better value.

3.2 We also believe firms can improve their renewal processes more broadly to deliver better consumer outcomes. We propose non-Handbook guidance, which is set out in full in Appendix 2.

Background

3.3 Existing consumer protection legislation and the common law apply to the renewal of insurance policies, including the Consumer Insurance (Disclosure and Representations) Act 2012 (CIDRA) and unfair contracts requirements.[10] Additionally, we have regulatory requirements that apply to firms' practices at renewal, including the provision of appropriate information and clarity of communications.

3.4 Our proposed guidance reinforces our existing requirements and is intended to remind firms about our expectations. The draft guidance covers three main issues: appropriate information and communication, opting-out and lapses, and charges. It is informed by our 2013 thematic review of automatic renewal of home and motor insurance policies, issues highlighted in complaints, as well as information from stakeholders.

3.5 We propose that the guidance will apply to both insurers and intermediaries, and cover situations where the same provider intends to offer a new contract to an existing customer. We intend to apply the guidance to all general insurance policies for retail customers.

Appropriate information and communications

3.6 Communications play a fundamental role in helping consumers make informed decisions. Effective and engaging information is a key tool to promote effective competition and supports greater transparency. This improves outcomes for consumers, but should also mean greater efficiency for industry as less time is spent handling complaints.

3.7 Consumers receive a number of documents about their insurance policy over time, such as initial policy documents, renewal notices and follow-up documents if the renewal offer is

10 Firms should ensure that their contractual terms comply with the requirements of the Consumer Rights Act 2015 (for contracts entered into from 1 October 2015) and the Unfair Terms in Consumer Contracts Regulations 1999 (for contracts entered into from 1 July 1995 to 30 September 2015).

accepted. At each point, it is important that the message is clear as this can influence whether or not the consumer engages and can make an informed decision.

3.8 Firms should consider whether initial policy documents make it sufficiently clear to the customer what happens once the policy term has ended, e.g. if there is an automatic renewal mechanism and how this works. We have seen examples which are ambiguous about whether and how the firm intends to renew the policy. This can mean that consumers are not clear that they have agreed to an auto-renewal policy.

3.9 It is also important that renewal communications are clear about what actions the firm is proposing and the consumer's options. For instance, if firms intend to automatically renew the policy, they should tell the consumer this and explain the consumer's options. Renewal creates a new contract so there are existing information requirements the firm must meet, such as the requirement to provide appropriate information about the proposed arrangements.

3.10 Firms should also provide the consumer with information about the new insurance policy being entered into. Some consumers may not understand there has been a change to the terms and conditions of a renewed policy and lose out if they need to claim but are no longer covered. In meeting existing information requirements, firms should consider how they communicate changes to policy terms and conditions so that consumers are able to assess whether the policy continues to meet their needs.[11]

3.11 More broadly, we encourage firms to consider their language and the timing of communications. Ambiguous language risks misleading the consumer. For instance, consumers may be told that they do not need to act (e.g. in response to an automatic renewal notice) while simultaneously being told to check their cover. We also want to ensure that consumers have the renewal communication in good time for them to give it their consideration.

Switching and cancelling

3.12 Consumers have options when renewing their insurance – they can stay with the same provider on the same terms or agree new cover or terms, switch or cancel their policy. Consumers need to be clear about their options and about how to tell the firm about their eventual decision. This supports effective competition and addresses consumer protection concerns about consumers either being unclear about their choices (such as an ability to stop a policy from auto-renewing) or feeling that firms are not responding to consumer decisions (such as complaints that firms have continued to renew even after being told by the customer that they do not want to continue with the policy). This is particularly important if a consumer states their intention of switching to another policy after receiving an automatic-renewal notice.

3.13 We encourage firms to focus on communicating the practical steps consumers can take. Instructions should be simple and easy to follow so that consumers have no doubt about what they need to do. There are different ways firms can communicate; for instance, a flow diagram or step-by-step instructions.

3.14 We also encourage firms to consider whether renewal options are appropriate or if they put barriers in the way of consumers who want to cancel or switch. For example, it could be restrictive to insist consumers can only opt-out online. Firms should at least look at the

11 Information requirements include Principles 6 and 7, ICOBS 2.2.2R and ICOBS 6.1.5R.

communication options given to new consumers and consider whether the same range of options should be available at renewal.

Fees and charges

3.15 Consumers may have to pay charges or fees for services to both the insurer and the intermediary. It is important that the consumer is clear about any fees and charges they may need to pay ahead of time, for instance if a firm is charging for intermediation activity in renewing the insurance policy. A lack of clarity could lead to confusion and complaint, and could be a breach of our rules.

3.16 Firms should continue to review the appropriateness of any fee or charge. For instance, a consumer on an auto-renewal contract may have intended to cancel it but did not do so in time. We would encourage firms to carefully consider the nature and level of any charges in light of our general principle to treat customers fairly.

Q8: Do you have any comments on the proposed non-Handbook guidance?

4. Treating customers fairly, vulnerability, and future work

4.1 In earlier chapters we have set out our disclosure proposals and intention to introduce guidance for firms on renewal practices. These measures are designed to help consumers engage, make more informed decisions and shop around, switch or negotiate. This chapter sets out our considerations about whether further action may be necessary to improve consumer outcomes.

Renewal pricing findings

4.2 The research project, including the supplementary supervisory work with individual firms, provided further insights into renewal pricing more generally:

- Aggregated data from three home insurance providers suggests that average premiums increase materially over five years until they plateau. This average includes customers who kept lower premiums by negotiating and those who have not. Only a small proportion of customers renew many times at these firms.
- Consumers who negotiated their renewal price with one home insurer reduced their premium by an average of a quarter.
- Data from another home insurer showed that the firm did not expect the cost of claims to increase over time, so this was not the reason for increasing prices.
- We also have similar aggregated data from three motor insurers. Two of these firms showed little evidence of average premium increases at renewal. However, it is still possible for consumers to secure a lower premium - at one of these firms, consumers who negotiate prices at renewal reduce their premiums on average by a fifth.
- High prices do not just apply to the time when introductory discounts or offers run out; they persist beyond this point. While the trial did not focus on individual risk pricing, evidence suggests that the length of time a customer has had a policy may be the key factor in persistent high prices, rather than the underlying risk.
- Some consumers may face additional barriers to shopping around or switching.

Treating customers fairly and vulnerability

4.3 Our work so far shows the benefits that additional disclosure can bring. However, we know that disclosure will not address all consumer engagement issues in these markets.

4.4 We considered whether, as well as stronger disclosure and improved practices, we should limit or minimise price increases for consumers at renewal. For example, we considered whether we should:

- Introduce caps or collars, limiting the price increases firms can impose on renewing consumers
- Ban introductory discounts
- Place limits on the number of renewals or place other conditions on auto-renewals

4.5 At this stage we do not propose to intervene in pricing or by placing limitations on the renewal process itself.

4.6 However, we do expect that firms consider how they are meeting their obligations to treat customers fairly, under principle 6 of our Principles for Businesses. Specifically, we expect firms to consider how their approach to renewal pricing in general, and their treatment of long-standing customers in particular, delivers fair outcomes to consumers.

4.7 We recognise that firms have different approaches to managing their businesses. While introductory discounts appear common, some firms have policies in place to identify long-standing customers and actively manage their price increases and others do not.

4.8 We also expect firms to think about the needs of vulnerable consumers. Our recent Consumer Vulnerability occasional paper highlighted that vulnerable consumers may be significantly less able to represent their own interests and more likely to suffer harm.[12] Data that we hold on some insurers show that a large proportion of long-standing customers are older. Age can be an indicator of vulnerability and this potentially raises questions about treating these consumers fairly. This is consistent with our recent consumer research, which found that people over 55 are overall less likely to shop around and more likely to renew policies with the same provider.[13]

Future work

4.9 The immediate next step for this work is to consider the feedback received by this consultation and produce final rules and guidance. We encourage your feedback. We aim to publish a summary of feedback and final rules and guidance in a Policy Statement in mid-2016. Once any new measures are implemented and embedded, we can assess what, if any, further action is necessary to address renewal issues in future.

4.10 We welcome industry efforts to address concerns about renewal pricing and practice, including steps to support vulnerable consumers at renewal.

12 FCA, Occasional paper no.8, Consumer Vulnerability, February 2015. http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-8

13 Unpublished FCA Consumer Insight Survey. Conducted by GfK. On-line survey of insurance holders 2015. Question: "Which statement best describes what you did when you arranged your insurance most recently" Base: 2000 respondents (838 aged 55+) holding 6,255 policies. Question: "When you got this […] insurance, did you shop around?" Base: 2,000 (838 aged 55+)

Annex 1
List of questions

Q1: Do you agree with our proposal that firms should disclose last year's premium on renewal notices?

Q2: Do you agree with our proposal that the premium displayed should be the premium the consumer started the year with, but that firms can include other information, such as mid-term adjustments?

Q3: Do you agree with our proposal that firms should also provide information to consumers to check the proposed policy continues to meet their needs and to shop around?

Q4: Do you have any comments about this additional disclosure? Do you have any suggestions for the proposed message to consumers?

Q5: Do you have any comments on how the disclosure should be presented to the customer?

Q6: Do you agree with the proposal to apply the measure to all situations where a general insurance policy is renewed with a retail consumer with the exception of policies with a term of less than a year?

Q7: Do you have any comments about our proposed implementation of 1 January 2017 for the disclosure measures?

Q8: Do you have any comments on the proposed non-Handbook guidance?

Q9: Do you have any comments on our cost benefit analysis (CBA)? (Note: see Annex 2)

Annex 2
Cost benefit analysis

1. The Financial Services and Markets Act 2000, as amended by the Financial Services Act 2012, requires us to publish a cost benefit analysis (CBA) of our proposed rules. Specifically, section 138I requires us to publish 'an analysis of the costs, together with an analysis of the benefits that will arise if the proposed rules are made'. It also requires us to include estimates of those costs and benefits, unless they cannot reasonably be estimated or it is not reasonably practicable to produce an estimate.

2. The proposed interventions we are consulting on are set out in chapters 2 and 3. This chapter presents the CBA that we have completed to inform our proposed policy approach. It begins by setting out an overview of the market failure that gives rise to the need for a change in our proposed rules and then presents our assessment of the benefits and costs associated with this intervention.

Disclosure of last year's premium

Market failure analysis

3. General insurance markets are typically characterised by many suppliers and relatively free entry. The concerns addressed here are not classical market failures regarding market power.

4. However, there is more scope for market failures relating to consumer behaviour, and these in turn can be exacerbated by how firms respond to known consumer behaviour. When consumers need to purchase a new insurance policy, they are usually sensitive to price and shop around, putting pressure on firms to keep prices low and provide quality cover and service.

5. When they have signed up to a policy and firms offer to renew it at the end of the current term, consumers can be significantly less price sensitive. Where consumers do not respond by either negotiating or switching this gives firms incentives to increase renewal prices above the competitive level, potentially allowing them to earn excess profits on these consumers. The fact that policies can automatically renew without further consumer engagement can exacerbate consumer inertia. Also, where consumers do not engage in the renewal information, their ability to make an informed decision is compromised.

6. This illustrates the evident market failure related to consumer behaviour at the point of renewal of general insurance. While higher prices at renewal are not necessarily evidence of a lack of overall competition, they indicate that intense competition for new customers does not protect those who do not shop around at renewal. This situation is comparable with the model developed by Gabaix and Laibson (2006)[14] that describes how firms lack incentives to draw attention to, or compete on add-ons prices in markets with many consumers who do

14 Gabaix, X., & Laibson, D. (2006). Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets. Quarterly Journal of Economics, 121 (2), 505-540.

not anticipate the costs of these add-ons. The prices of these add-ons are 'shrouded'. Some consumers pay high prices for add-ons while other consumers shop around and avoid high prices.

7. The evidence we have for the home insurance market is consistent with this 'shrouded equilibrium', in that purchasing the add-on is analogous to purchasing the home insurance product at renewal. Our findings for home insurance suggest that consumers often do not switch or negotiate at renewal because they do not anticipate how much they could save from doing so or believe the difficulties of switching are prohibitive.

8. Motor insurance is typically quoted by stakeholders as an example of a competitive market. Our own recent consumer research found that 77% of respondents with motor insurance stated that they shopped around, and 37% stated that they switched.[15] Recently, the Competition and Markets Authority (CMA) found that switching levels for private motor insurance were substantial.[16]

9. This indicates that, for the motor insurance market, there is a reasonable level of engagement. But even in this market there is a group of consumers who do not shop around. Our randomised controlled trial (RCT) explored this issue and indicated that it is possible to drive greater consumer engagement by disclosing last year's premium on the renewal notice. Our results indicated that the presentation of this information on the renewal notice increased shopping around by 7.3 percentage points at a firm where the base level of shopping around was already relatively high (67% shopped around).

10. More broadly within general insurance markets, there is evidence of consumers who are not engaging in their renewal decisions. When we measure engagement using the numbers of consumers shopping around, we found that nearly half (45%) of consumers of GI products shop around for their insurance policy. However, there are certain GI product markets where consumers are less likely to shop around such as gadget insurance (43%), extended warranties (16%), and mobile phone insurance (29%).[17]

11. In addition, there were examples from the General Insurance Add-ons market study research in which renewal prices were significantly higher than new business prices. For instance, some home emergency products' renewal prices increased by over 100%. For legal expenses insurance there was an example of a price increase at renewal above 30%. At one firm selling travel insurance, prices offered to existing consumers were approximately 50% higher than those given to new consumers.

12. There appear to be issues across general insurance markets. However, consumer inertia levels will vary between products and over time, and firms will adapt their pricing strategy in response to consumer behaviour at renewal stage.

13. The scale of price increases for existing customers concerns us, and indicates how widespread consumer inertia is for some firms or products and that even fairly intense competition for new customers does not protect existing customers who do not switch or negotiate at renewal.

15 Unpublished FCA Consumer Insight Survey. Conducted by GfK. On-line survey of insurance holders 2015. Question: "When you got this […] insurance, did you shop around?" Base: 211 respondents with motor insurance. Question: "Which statement best describes what you did when you arranged your insurance most recently?" Base 1258 respondents with motor insurance.

16 CMA, Private motor insurance market investigation: final report, para 5.33.

17 Unpublished FCA Consumer Insight Survey. Conducted by GfK. On-line survey of insurance holders 2015. Question: "When you got this […] insurance, did you shop around?" Base: 70 respondents with gadget insurance, 95 respondents with an extended warranty, and 107 with mobile phone insurance.

14. If consumers do not make informed choices they may lose out by not buying the best value products available– i.e. the products that give them the desired level of quality at the best price. This does not imply that consumers should necessarily buy the cheapest products. Consumers may deliberately choose to buy a relatively expensive product on the basis of other valued characteristics. Our concern is that consumers who are not fully aware of the prices and other characteristics of other available products buy expensive products by default and lose out as a result.

Proposed intervention

15. In 2014 we launched a large scale randomised controlled trial examining auto-renewal pricing and consumer behaviour in the home and motor insurance markets, involving over 300,000 customers. The full details of this trial are in the accompanying occasional paper.[18] In the trial, we tested how consumers at three firms reacted to four different disclosure treatments on their renewal notices. We looked at the effect that these treatments had on shopping around, switching or successfully negotiating the price downwards and found that the most effective disclosure treatment was to include last year's premium on renewal letters. Informed by the trial findings, we propose to require firms to include the previous year's premium on renewal notices.

16. We considered whether there is a more effective disclosure alternative to the inclusion of last year's premium, such as disclosing the new business equivalent premium or the disclosure of the lowest premium over a period of years. We assessed these options against principles including simplicity, ease of understanding for the consumer, and the likelihood of it increasing engagement. The inclusion of last year's premium on the renewal letter remains our preferred metric, due to the simplicity of the concept which allows consumers to easily engage with the information.

17. The aim of including last year's premium in renewal letters is to increase consumers' engagement at renewal, so that they can make a more informed decision. It should increase shopping around by consumers, as it makes it easier for them to find out the past cost of their policy and see more clearly if this has changed. In our trial, we looked specifically at the impact that inclusion of last year's premium in the renewal letter had on switching rates in home and motor insurance. We found that including last year's premium at renewal increased switching and negotiating by 3.2% for combined home insurance at one firm. We also found that, while it did not increase switching or negotiating for motor insurance, it did have a positive impact on the proportion of consumers shopping around, increasing this from 67% to 73%.

18. Disclosure of last year's premium has a stronger effect the bigger the increase relative to the previous year's price. We recognise that including last year's premium is less effective where price changes year-on-year remains similar, or where the prices go down. If prices significantly increase, consumers may interpret the difference between this year's price and last year's price as a "loss", which can encourage them to act. On the other hand, if prices do not increase it may "anchor" consumers' expectations, making them less likely to take action.

19. We found evidence that some consumers who have been with the same provider for more than five years pay significantly more than new customers, even though the prices that they pay may not increase as steeply year-on-year as for new customers. Disclosing last year's premium may not be an effective remedy for these consumers, who may need additional support. We

18 FCA, Occasional Paper no. 11, Encouraging Consumers to Act at Renewal, http://fca.org.uk/news/ocassional-paper-no-12

propose additional disclosure to address this, in the form of a statement on renewal notices drawing attention to the fact that the consumer has been at the provider for a number of years and suggesting that they shop around. This would be required once consumers have renewed with the same provider four times.

Analysis of costs and benefits

Baseline

20. The relevant baseline against which we assess the costs and benefits of the policy is what would happen in the absence of our proposed intervention. In this situation, firms would not be required to disclose last year's premium on their renewal notices. In the absence of any expected material change to market conditions following the introduction of the remedy, the relevant baseline in this case is the status quo.

Benefits

21. We anticipate that our proposals will promote greater consumer engagement in the renewal decision. We expect consumers will engage and generally make more informed decisions about the renewal of their general insurance policies. Even if the consumer takes no further action, the fact that they consider the renewal quote more closely and make an informed decision to stay with the same provider is a positive outcome. ABI research from May 2014 shows that 89% of respondents who received an insurance renewal said that it would be helpful to have last year's price printed on their insurance renewal.[19]

22. We expect that our proposals will "nudge" more consumers to shop around as a result of having additional information at renewal. However the proposals' benefits will differ between different consumer groups, depending on their behaviour:

- Consumers who are already active and likely to continue shopping around and switching in the absence of the proposed remedies.
- Consumers who are inactive but who are likely to shop around as a result of the proposed remedies.
- Consumers who are inactive and who are likely to remain inactive regardless of the proposed remedies.

23. We estimate that the second group of consumers will benefit most from our proposed remedies. These consumers will shop around, and switch or negotiate as a result, potentially achieving lower premiums while likely retaining similar coverage. However, we also expect that consumers in the first group will benefit from reduced search costs. Consumers in the third group could benefit if the policy constrained firms' incentives to increase prices at renewal. However, as we set out below, we think that any impact on prices is likely to be limited.

24. We have not provided a quantification of the benefits of more informed decision making or reduced search costs for consumers that already shop around, as this would require particularly complex but unreliable quantification exercises. This would involve a disproportionate cost and use of the FCA's resources, and so it is not reasonably practicable to do so, particularly as the results would be of limited accuracy.

19 ABI, Renewal pricing – customer questions and answers. https://www.abi.org.uk/~/media/Files/Documents/Publications/Public/2014/GI/Renewal%20pricing%20customer%20questions%20and%20answers.pdf

25. Our discussions with firms and with trade bodies indicated that these measures will increase transparency and may generate greater consumer trust. Again, we have not produced a quantification of this benefit on the same grounds as above.

Quantification of benefits

26. We estimate the benefits of lower insurance premiums for consumers that change behaviour and switch or negotiate as a result of including last year's premium in the renewal notice. We use data from the RCT to assess the likely increase in the proportion of consumers switching or renegotiating their insurance premium and combine this with evidence on the gains from negotiating or switching. For all products we assumed that all of the increase in cancellation rates observed in the trial, due to displaying last year's premium, consisted wholly of consumers that switched to another provider. This is because knowing last year's premium does not give consumers any information that would be relevant to a decision to cease to buy insurance, whereas it does give information that is relevant to a decision to seek an alternative provider.

- For motor products this implies no change, as we did not find a statistically significant effect on consumer behaviour.
- For home insurance, this amounts to a 3.2% increase in consumers switching or renegotiating.
- For medical, travel and pet insurance we assumed that the proportion of consumers that change their behaviour is the same as home insurance consumers. Although we did not have information on consumer behaviour for these products we consider that home insurance is more likely to provide an appropriate comparator than motor insurance, which is compulsory and subject to particularly intense forms of competition.

27. Firms may have an incentive to change their overall pricing structure as a result of the proposed measures. However, as the expected increase in switching or negotiation is relatively small across products (3.2%), we do not expect that changes related to this will be substantial and have therefore not sought to estimate the positive scale of such changes.

28. We recognise that the size of benefits that accrue to consumers will be influenced by whether they choose to switch provider or renegotiate the premium with their existing provider. Typically where customers switch provider, they are likely to attain a more favourable premium, as a new customer, than if they renegotiate as an existing customer. We had access to data from the trial and evidence from our Supervision work that allowed us to estimate these two different scenarios for home content insurance: a "low scenario" where we assume that the gains from cancellation and switching are the same as from negotiating and a "high scenario" where we assume that all consumers who cancel or switch will receive the price new consumers pay.

29. For all other GI products, we assume that the gains from cancellation and switching are the same as those to negotiating (as in the low scenario described above). This is because we do not have sufficient information on prices for new customers for these products. As the returns for switching are likely to be higher than those for negotiating and staying with the same provider (as seen for home products), our estimate is likely to underestimate the true impact of our proposals.

30. The results of this analysis are displayed in the table below. In total we expect that benefits to consumers who switch or negotiate to be in the region of £85.3 – 137.9 million.

31. However, we acknowledge the possibility that some of the higher prices that consumers would have paid may not represent pure profit, and instead may be competed away in an attempt to

gain additional consumers. Moreover, consumer learning may cause sharp increase in prices for customers to eventually disappear. For example, once consumers experience a sharp increase in insurance premiums, they may start to shop around every year to ensure that they secure a good deal for themselves. Disclosing last year's premium may speed up this learning process.

32. This "waterbed effect" could potentially reduce the total benefits to consumers. There are reasons to believe that this "waterbed effect" may not be complete, as consumers may value other aspects of their policy over price, such as brand loyalty. For this reason, we consider a scenario where the waterbed effect is 25 per cent[20], which would reduce the benefits for consumers to a range of £64.0 to £103.4 million per year.

33. Table 1: Estimated benefits to consumers from switching or negotiating

Product	Estimated increase in customers negotiating & cancelling (000)	Estimated returns to negotiation & cancellation (£)	Estimated benefits to consumers (£ million)
Motor*	0	0	0[22]
Home combined*	544	117 – 214	63.8 – 166.4
Home contents*	15	34	0.3
Medical	28	424	11.7
Travel	445	7	3.1
Pet	97	65	6.3
Total	1,129	-	85.3 – 137.9
Total including 25% waterbed effect			64.0 – 103.4

34. This estimate does not include additional benefits from other general insurance products as we do not have sufficient data to provide a precise estimate for these products. This includes a large number of smaller products and would require a significant data collection exercise. In addition, in view of the range of uncertainty in the above estimate, and since it provides a quantification for the most widely sold products, it is unlikely that providing additional quantification would add significantly to our understanding of the scale of benefits. Providing an estimate of these additional benefits is therefore not a reasonably practicable exercise.

35. These benefits to consumers are a transfer from firms, meaning that there is a corresponding reduction in firms' revenues equal to the amount that consumers save. This represents the net transfer. Some firms, those to which consumers switch to gain more competitive prices, will also benefit. In addition, firms such as price comparison websites or brokers could see increased interest from consumers.

Costs

36. We quantified the expected costs of our proposal using information from a mix of firms, including those in the trial and others with experience of disclosure.

37. Based on our discussions with firms, our assessment is that firms may incur the following costs:

- One-off implementation costs, particularly systems changes and exchanges with partner firms (e.g. discussions between distributor and insurer and with software providers).

20 This is in line with our approach in other cost benefit analyses, such as the one used in CP15/24: Cash Savings remedies.

21 In the trial, we found that disclosing last year premium had no statistically significant treatment effects on switching or negotiating, however we note that it did have a significant effect on the proportion of people shopping around.

- On-going costs incurred because of increasing numbers of consumers contacting firms to negotiate their premiums.

- Reductions in revenues as a result of changes in consumer behaviour – either because consumers switch away from them or negotiate a lower premium. These represent a transfer from firms to consumers.

38. We also expect consumers would incur costs from spending additional time cancelling and negotiating their GI renewal as a consequence of the policy.

Implementation costs

39. We expect that the main implementation costs will be from changing IT systems to include the new disclosure on renewal notices. The firms that will incur these costs will be those that provide consumers with renewal notices. In some cases this will be insurers providing notices to consumers directly. In others, intermediaries will provide these notices.

40. Firms may make the IT changes themselves or may outsource. We were also told that systems change costs will be heavily influenced by timing – the shorter the timetable to implement the proposal, the more expensive it will be for firms. This process also involves management time, the involvement of product experts, business analysts and testing. Costs would also depend on the number of systems (or platforms) and the age of these systems.

41. Our discussions with firms generally indicated that there was little reason to expect costs to be significantly different between insurers and intermediaries. One sample of firms broadly indicated a range of £500,000 to £1 million per firm for implementing the changes for motor and property insurance, though one firm within the sample gave an estimate of £100,000. Other firms estimating costs on a product line basis suggested figures of £30,000, £100,000 and £100,000 to £150,000 per product line requiring changes.

42. Overall this evidence is consistent with costs of approximately £100,000 for each system that requires amending. We examined data from insurers on the number of different product groups (motor, household, etc.) they sell. Assuming that firms have two different systems covering each product group, this suggests an average firm would incur costs of around £350,000. We expect that these changes would affect approximately 350-400 firms will make these system changes, comprising of a mix of insurers and intermediaries. This suggests total costs to firms of systems changes in the region of £133 million.

Additional customer queries and shopping around

43. As a result of disclosure prompting the consumer to engage with their provider, either to negotiate or cancel their policy. As noted, we believe there are benefits to this, but also recognise that there will be a cost to firms potentially from more staff time needed to cover the increased volume. One firm that we spoke to stated that they expect about a 20% increase in the number of queries. However in our trial we did not observe a significant increase in the volume of consumer contact.

44. Information from our survey on the amount of time consumers spend cancelling their policies suggested that 77% of respondents took 15 minutes or less to cancel their insurance policies, with 32% taking less than five minutes. Based on the total number of consumers that we expect to cancel or negotiate in response to this policy assuming that each call takes an average of 15 minutes at a cost of approximately £14 per hour, this suggests total costs to firms of

dealing with additional enquiries of £3.9 million per year.[22]

45. We expect that costs for consumers could arise from time spent researching, negotiating or switching. We looked at information from the trial on time spent shopping around. At one firm, 50% of consumers who did not shop around believed it would take more than 1 hour to do so, whereas only 31% of consumers who did shop around actually spent more than 1 hour. At another firm, 56% believed it would take more than 1 hour and 57% actually spent this time.

46. On the basis of average UK wages of approximately £12 per hour and the total number of additional consumers that we expect to switch or negotiate, assuming it takes one hour to do so, we estimate shopping around costs of £13.1 million per year.[23]

Reductions in profit

47. In addition, as set out above, we estimate that the increase in consumers negotiating and switching to cheaper products would reduce firms' revenues by £64.0 to £103.4 million per year. As this represents revenue above the amount necessary to cover costs, and we do not expect any further change in firm or consumer behaviour, we expect that this reduction in revenue amounts to a reduction in profit of the same amount. This is a transfer from firms to consumers and incorporates the "waterbed effect" that we discussed above.

Analysis of costs and benefits

48. We expect the remedy to give rise to costs and benefits as detailed below. This consists of benefits to consumers of £64 – 103 million per year, which is a transfer from firms' profits. In addition, we expect firms to incur increase call handling costs of £3.9 million per year, and we estimate the costs to consumers of time spent shopping around to be £13.1 million per year. In addition, we expect firms to incur one-off implementation costs of £133 million.

49. Table 2: Summary of costs and benefits

	Benefits	
	One-off	On-going
Reductions in consumers' premiums	-	£64 - 103 million per year
More engaged consumers	-	Not quantified
Reduced search cost	-	Not quantified
Increased transparency	-	Not quantified
	Costs	
	One-off	On-going
Systems and IT changes	£133 million	-
Reduction in firms' profits	-	£64 - 103 million per year
Increased call handling costs	-	£3.9 million per year
Consumer time shopping around	-	£13.1 million per year

22 Hourly cost based on average cost of employing a call centre worker of £25,000 per year, working 7.5 hours per day with 240 working days in a year. Assumptions taken from Competition and Markets Authority, Private Motor Insurance Market Investigation.

23 ONS Annual Survey of Hours and Earnings 2014 indicated median hourly pay of £11.61.

Renewal practice guidance

50. While section 139A of FSMA does not require us to carry out a cost benefit analysis, we have considered the cost implications of the proposed guidance. We believe the guidance is likely to result in minimal incremental costs to firms (incremental with respect to existing requirements). This is because this guidance is a reinforcement of existing principles, rules and guidance and therefore does not put any new burden on firms.

Q10: Do you have any comments on our cost benefit analysis (CBA)?

Annex 3
Compatibility statement

Compatibility with the FCA's general duties

1. We are required by section 138I(2) of the Financial Services and Markets Act 2000 (FSMA) to also include in our consultation:

   - An explanation of the FCA's reasons for believing that making the proposed rules is compatible with its duties under section 1B(1) and (5)(a) and;

   - Any statement prepared under section 138K(2), which sets out whether the proposed rules will have a significantly different impact on mutual societies, as opposed to other authorised persons.

2. In fulfilment of section 1B(1) we explain how we are acting in accordance with our strategic objective, and advancing one or more of our operational objectives. In fulfilment of section 1B(5)(a), we also explain how we have had regard to regulatory principles in section 3B and the importance of taking action to minimise the extent to which business is carried out in connection with financial crime.

Compatibility with our strategic objective and operational objectives

3. The proposals we are consulting on, in chapters 2 and 3 of this document, are consistent with our strategic objective of ensuring that the relevant markets function well. The proposals take account of evidence from firms and consumers. We have found that encouraging engagement and shopping around when renewing general insurance products is beneficial, and reinforcing industry standards of renewal terms and practices can help address consumer protection concerns and mitigate barriers to shopping around and switching.

4. We intend our proposals to advance two operational objectives: promoting effective competition in the interests of consumers and securing an appropriate degree of protection for consumers.

5. Our proposal to require firms to disclose last year's premium information and additional information on renewal notices promotes effective competition in the interests of consumers by:

   - Encouraging consumers to engage in their renewal decision, and so make an informed decision about their policy.

   - Increasing engagement should also mean that more consumers will shop around and, if they consider it necessary, may switch or negotiate. This should result in savings on insurance for individual consumers.

6. Our proposals to reinforce standards about renewal practices by issuing guidance will:

   - Achieve an appropriate degree of consumer protection by reminding firms of how our principles, rules and guidance apply to the renewal of general insurance policies. This will remind firms about our expectations, for instance, in respect of the fair treatment of customers and that communications should be clear, fair and not misleading.

   - Encourage firms to consider whether their existing renewal terms, communications and practices may act as barriers to consumers making an informed decision at renewal and, as appropriate, shopping around and switching. These barriers could negatively affect competition, so reinforcing standards should also support our objective of promoting effective competition in the interest of consumers.

7. We also consider that more action is needed to address concerns about the treatment of long-standing and vulnerable consumers at renewal. Our view is that firms can take action without regulatory intervention at this time, and we will work to support this where appropriate.

8. Further action may be necessary in the future – as we review how proposed proposals are embedded and monitor changes in the market. We will consider this at a later point.

Compatibility with the FCA's regulatory principles

9. We set out below how our proposals demonstrate regard for each of the regulatory principles.

The need to use our resources in the most efficient and economical way

10. With the support of three firms, we have tested four different disclosure measures to inform our decision about an appropriate disclosure solution to the concern that consumers are paying too much on their renewal premiums. This large scale research trial identified that disclosing last year's premium is the most effective of the options we considered. Our findings also show that last year's premium may not be as effective where year-on-year price increases are not as large, therefore we propose additional disclosure to prompt these consumers. Overall, this means that we are confident that our proposal will have a positive impact and therefore be an efficient and economical use of resources.

11. We expect that the guidance about renewal practice will increase firms' focus on how they interact with consumers at renewal, and reinforce existing principles, rules, and guidance. We have decided not to be prescriptive by setting out rules, because we expect firms to know their customer base and to exercise judgment in how they comply with existing requirements.

12. We have also made an assessment that it would not be a good use of our resources at this time to introduce new requirements for the treatment of vulnerable customers at renewal. Instead, we will work with industry because we have seen examples where firms can manage this issue without regulatory intervention. However, should we find that sufficient change has not been made, we may need to reassess this.

13. Overall, the introduction of new rules will require supervision and potentially enforcement. This can be managed within our resourcing allocation.

The principle that a burden or restriction should be proportionate to the benefits

14. Our cost benefit analysis finds that the policy results in a transfer, with consumers' premiums reduced by £64-103 million per year and firms' profits reduced by the same amount. When

considering the other costs that the policy imposes, overall it generates significant on-going net benefits to consumers. We think these are proportionate to the costs that the measure imposes on firms.

15. We propose to introduce guidance, rather than rules, for renewal practice. The guidance does not require firms to take any action, but should reinforce existing expectations. Firms will retain the ability to apply existing requirements as appropriate to their circumstances.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

16. We believe that our proposals, if implemented, will increase competition in the general insurance sector and improve value for consumers, which will encourage sustainable growth. The disclosure requirements in particular should encourage consumers to shop around, where appropriate. This should support firms, including new entrants, to develop innovative and value propositions that are attractive to consumers and encourage them to take up insurance. It should also reduce the reputational issues that can limit growth caused by publication of examples where consumers may not have received good value at renewal.

The general principle that customers should take responsibility for their decisions

17. Our research suggests that consumer inertia is driven by low perceived benefits from shopping around relative to the actual benefits, and that consumers may not be paying attention to price increases at renewal. Our disclosure measures aim to resolve this issue by highlighting last year's premium and encouraging consumers to check their cover and shop around. We consider that this strikes the right balance by encouraging consumers to act, therefore taking responsibility, without us limiting their options.

18. The guidance reminds firms of their existing responsibilities, and therefore should not impact the consumer responsibility principle.

19. However, we recognise that not all consumers are the same. We have specific concerns about long-standing and vulnerable consumers, whom we believe may require additional support for their renewal decisions. We are reminding industry of their obligations to treat customers fairly, which could mean that firms introduce additional protections. It is up to firms' judgment to assess their customers' needs and, as necessary, introduce protections.

The responsibilities of senior management

20. Senior managers will need to ensure compliance with our disclosure rules, as well as our existing principles, rules and guidance as they apply to renewals. Senior management should pay particular attention to the needs of all of their customers, including long-standing and vulnerable consumers, at renewal and reassure themselves that they are acting fairly.

The desirability of exercising our functions in a way that recognises differences in the nature and objectives of business carried on by different persons

21. We recognise that firms have different business models, and we have shaped our proposals in a way that takes account of these different approaches.

22. The guidance allows for a flexible approach and so is consistent with the diversity in the market.

The desirability of publishing information relating to persons on whom requirements are imposed by or under FSMA

23. Our proposals meet this principle.

The principle that we should exercise our functions as transparently as possible

24. We consider that our approach is consistent with the principle of exercising our functions as transparently as possible. Together with our consultation we are publishing our findings from the behavioural trial on auto-renewal of motor and home insurance. This occasional paper provides stakeholders with additional evidence about our findings.

25. One limitation is the need to treat commercially sensitive information appropriately. This is a particularly difficult area as this consultation touches on issues of pricing, which is often particularly commercially sensitive. We have tried to strike a balance in providing sufficient information to be transparent about our rationale, without compromising firms' sensitive information.

Expected effect on mutual societies

26. We see no reason why our proposed rules and guidance would impact a firm differently based on the firm having a mutual society structure. We discussed our proposals with two mutual societies and there do not appear to be different implications for them in comparison with other firms.

Legislative and Regulatory Reform Act 2006

27. We are required under the Legislative and Regulatory Reform Act 2006 (LRRA) to have regard to the principles in the LRRA and to the Regulators' Compliance Code when determining general policies and principles and giving general guidance (but not when exercising other legislative functions). We consider that our proposal is:

- Transparent: We are following a consultation to make these rules
- Accountable: We are seeking feedback from this consultation paper on whether stakeholders agree with our proposed approach
- Proportionate: we have carefully deliberated on our approach and believe our proposals are proportionate as we have sought to minimise costs and we expect net overall benefits
- Consistent: Our proposed approach is meant to apply in a consistent manner to firms
- Targeted at situations in which we see detriment, or the potential for detriment: As explained in the paper, we consider there to be a strong case for the introduction of these measures.

28. We have also had regard to the Regulators' Compliance Code for the parts of the proposals that are general policies, principles or guidance. We consider that the proposals will be effective in helping firms understand and meet regulatory requirements more easily, in a manner that leads to improved outcomes for customers and addresses the issues identified in this market.

Appendix 1
Draft Handbook text

INSURANCE (INFORMATION DISCLOSURE FOR RENEWALS) INSTRUMENT 2016

Powers exercised

A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (The FCA's general rules);
(2) section 137T (General supplementary powers); and
(3) section 139A (Power of the FCA to give guidance).

B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on [*date*].

Amendments to the Handbook

D. The Insurance: Conduct of Business sourcebook (ICOBS) is amended in accordance with the Annex to this instrument.

Citation

E. This instrument may be cited as the Insurance (Information Disclosure for Renewals) Instrument 2016.

By order of the Board
[*date*]

Annex

Amendments to the Insurance: Conduct of Business sourcebook (ICOBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

6.1 General

…

Group policies

6.1.12 R …

Renewals

6.1.12A R (1) This *rule* applies to a *firm* when a *renewal* of a *general insurance contract* for a period of more than 12 months is proposed in relation to a *consumer*.

(2) A *firm* must, provide to the *consumer* the following information in good time before the *renewal*:

(a) the *premium* to be paid by the *consumer* on *renewal* of the *policy*;

(b) in a position so it can be easily compared to (a), the *premium* last paid by the *consumer* for the *policy*;

(c) a statement indicating that the *consumer* should check that the level of cover offered by the *renewal* is appropriate for their needs; and

(d) a statement indicating that the *consumer* is able, if he so wishes, to compare the prices offered by alternative providers.

(3) Where a *consumer* has entered into four or more consecutive *renewals* in respect of the *policy* the subject of the proposed *renewal*, a *firm* must also include the following statement, to appear alongside the matters required by (1)(a) and (b): "You have been with us for over five years. You may be able to save money if you shop around."

(4) This information must be communicated in a clear and accurate manner and in writing or another *durable medium*, and made available and accessible to the *consumer*.

(5) This information must be drawn to the *consumer's* attention and must be clearly identifiable as key information that the *consumer* should read.

6.1.12B	G	A *firm* should have regard to the record-keeping obligations referred to in *ICOBS* 2.4.1G and ensure that it has appropriate systems and controls in place with respect to the adequacy of its records so it may fulfil its regulatory and statutory obligations, and sufficient records are kept to enable the *FCA* to monitor the *firm's* compliance with the requirements under the *regulatory system*.

Appendix 2
Draft guidance on renewal of general insurance products

Introduction

1. This guidance helps firms understand our expectations for the renewal of general insurance contracts, both in terms of what needs to be covered in the contract and what steps need to be taken if the firm intends to offer the consumer a subsequent contract.

2. Our objective is two-fold:

   - to remove barriers to consumers shopping around and switching, and
   - to ensure consumers are treated fairly and that communications are clear, fair and not misleading.

Background

3. In 2014, we launched a randomised controlled trial to test how consumers respond to different disclosure treatments at renewal and understand the root causes of consumer inertia. The trial gave us valuable insights into why consumers may not be engaging in their renewal decisions and the scale of the challenge of encouraging consumers to shop around. The full report on the trial methodology and findings has been published separately.[24]

4. Before this, in 2013 we undertook a thematic review of auto-renewed home and motor insurance contracts from an unfair contracts perspective. We identified examples of poor practice in the fairness and clarity of contract terms as well as firms' practices. We provided feedback to the individual firms who participated in the review at the time, but we have drawn on relevant findings and set out our views here so that the wider industry can benefit.

5. We have also identified common areas of complaints about general insurance renewals. These include pricing, communication issues, changes in policy details, poor administration, the role of the firm in highlighting alternative products and the auto-renewal mechanism.

Application of this guidance

6. This guidance applies to both insurers and intermediaries of general insurance products to retail

24 FCA, Occasional Paper no. 11, Encouraging Consumers to Act at Renewal, http://fca.org.uk/news/occasional-paper-no-12

consumers. Although commercial customers are not within scope, we would also encourage firms to consider whether any of the issues raised by us about retail consumers would equally apply to commercial customers and if there is benefit to making wider changes.

7. This guidance covers the following areas: appropriate information and communications; switching and cancelling; and fees and charges. We set out below our guidance on each of these areas in turn:

Appropriate information and communications

8. Firms must comply with our existing principles and rules about disclosure and communications, including Principle 7:

A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

9. We encourage firms to consider the language in their renewal letters and whether this could discourage the consumer from checking that the policy is appropriate or from shopping around. Firms should particularly look at this if the proposal is to automatically renew the policy, as the customer could read the notice as indicating that they do not need to take action.

10. Each time that a contract is renewed, a new contract is created. This means that we expect firms to follow existing rules and guidance at each renewal point. For instance, our appropriate information rule at ICOBS 6.1.5(R), states that:

11. *A firm must take reasonable steps to ensure a customer is given appropriate information about a policy in good time and in a comprehensible form so that the customer can make an informed decision about the arrangements proposed.*

12. Our guidance at ICOBS 6.1.6(G) explicitly states that this rule applies to renewals. So we would expect firms to be able to demonstrate that they are complying with this rule. We draw specific attention to the following aspects:

- We consider an auto-renewal term to be an important feature of a contract. Firms should consider whether and how they are providing consumers with appropriate information about the auto-renewal term, including what the consumer should expect and how it will operate.
- If an auto-renewal term is included in the preceding insurance contract, we expect the firm to communicate with the customer about how they intend to proceed. A communication could by way of providing a renewal notice.
- The appropriate information rule also requires that the information is provided in good time. We encourage firms to consider whether their customers have enough time to review their renewal documentation, make an informed decision about it and take steps, which may include shopping around. We encourage firms to consider how they are communicating information about changes to policy terms and conditions, so that consumers can make an assessment about whether the policy remains suitable.

13. In terms of changes to the consumer's risk profile since the last renewal, firms should be aware of existing legislation on consumer disclosure requirements such as the Consumer Insurance

(Disclosure and Representations) Act 2012. We also have a relevant Handbook, for instance our guidance at 5.1.1 and 5.1.4. Firms should consider the needs of their customers and whether it is realistic to expect the consumer to remember all of the information they previously provided and the questions they were asked.

Switching and cancelling

14. As we have stated above, firms should consider whether and how they are providing consumers with information about their options in respect of renewal. This is particularly important for auto-renewal contracts, where a consumer may have to take active steps to make clear their intention to switch to another policy. When considering what information to provide consumers, we encourage firms to focus on the practical steps the consumer would take.

15. We also encourage firms to consider what options they provide to consumers so that they can express their intention to switch or cancel. We have seen examples of onerous requirements, which in practice create barriers to the consumer exercising choice and switching to a policy that is more appropriate to their needs. Firms may find it helpful to consider how consumers communicate with them as potential new customers and whether these modes of communication can also be appropriate for opting-out or lapsing. We also specifically note our recent rules limiting the cost of calls consumers make to firms to a maximum 'basic rate', including post-contractual calls.

16. Firms may also wish to consider if it would be useful to the consumer to be able to opt-out of auto-renewal when entering a contract.

17. Once the policy has renewed, cancellation rights apply. A firm must provide a consumer with information on the right to cancel a general insurance policy, as set out in ICOBS 6.2.5(R). The information must be provided in good time before the conclusion of the contract. A consumer's right to cancel is within 14 days for a general insurance contract, unless one of the exceptions applies or it is a pure protection or payment protection contract. Within this period, there are limitations on what the firm can require a consumer to pay.

Charges

18. We expect firms to be able to evidence their compliance with our principles and any applicable rules about fees and charges, including our principle of treating customers fairly. We specifically call attention to the rule set out at ICOBS 4.3.1 and 4.3.2:

<u>ICOBS 4.3.1R</u>

(1) A firm must provide its customer with details of the amount of any fees other than premium monies for an insurance mediation activity.

(2) The details must be given before the customer incurs liability to pay the fee, or before conclusion of the contract, whichever is earlier.

(3) To the extent that an actual fee cannot be given, a firm must give the basis for calculation.

<u>ICOBS 4.3.2G</u>

The fee disclosure requirement extends to all such fees that may be charged during the life of a policy.

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