

Our general insurance add-on market study

We are calling for evidence from firms and consumers

Why are we calling for evidence?

In December 2012, [the FSA announced](#) that it was going to carry out a study into sales of general insurance add-on products (GI add-ons).

We are now continuing this study as part of our competition objective. We expect to publish our findings by early 2014.

To carry out this work we need firms and consumers to send us their evidence and representations **by 10 September 2013**.

Below we discuss our work so far, consider our theories of harm¹ and set out our next steps.

What do we mean by 'evidence'?

We want to receive information that will help us to consider whether consumers are paying too much for these products, whether the products being sold to them are appropriate for their needs, and whether they shop around.

We are particularly keen to receive information from consumer organisations and we will seek to engage closely with them going forward.

We also want to see information on any barriers to entry, or any other constraints firms face as well as information on features of sales processes and interactions that may lead to poor outcomes for consumers.

See below for more information on the kind of evidence we are looking for.

Background

A wide range of general insurance products are sold alongside or on the back of 'primary products'.

These primary products may be financial services – e.g. home insurance – or they may be non-financial products, such as motor vehicles, mobile phones or other services such as passenger flights.

¹ Our theories of why or how consumers may be harmed in these markets.

The insurance products sold alongside primary products are known as 'add-ons'.

An 'add-on' product has a separate price from the primary product, whether or not it is part of the same contract, and it is not necessarily sold at the same time.

The FSA aimed to complete a study into the sales of general insurance products as add-ons to other goods and services in the third quarter of 2013 and publish a report shortly after that. We are extending this original publishing deadline to give us more time to gather evidence, reflect it in our analysis, and bring the study in line with our approach to competition.

The FSA became increasingly concerned that consumers were experiencing poor outcomes when purchasing insurance as an add-on, specifically around the extent of risk transfer, value for money and their understanding of what risks products do and do not cover.

We have continued to look into this, and we recently published reports of thematic work on [motor legal expenses insurance](#) and on [mobile phone insurance](#).

Our competition objective and the study of GI add-ons

One of the FCA's objectives is to promote effective competition in the interests of consumers. We expect to use market studies as our main tool for examining competition issues in the markets we regulate. Where necessary, we may use our powers to require authorised persons to provide information.

We recognise that a wide range of problems in markets can prevent competition being effective. These can include barriers to entry and other potential supply-side constraints on competition that make it harder for alternative providers to enter the market and/or to expand, as well as demand-side information problems, consumer behaviour and the way firms respond to consumer behavioural patterns.

Our GI add-on market study will enable us to analyse the effectiveness of competition in markets for these products and the reasons why competition may be ineffective.

Why study GI add-ons?

We want to decide on an appropriate regulatory response to any evidence of recurring poor outcomes for consumers that we find across sales of GI add-ons, so we are assessing whether or not competition is effective regarding these products. And where competition is ineffective, we want to know why.²

² This approach is different from thematic reviews.

Publishing our study in early 2014 means we can better capture the variety and complexity of distribution models. It also gives us the opportunity to carry out further consumer research.

In early 2014, at the same time as publishing our draft conclusions on the effectiveness of competition, we will ask for comments on our analysis and proposals.

If appropriate we will include our proposed solutions for addressing any concerns identified. We may, for example, say we intend to make rules to change how the relevant markets work. Any proposals for changes in our rules will be subject to our statutory consultation processes, including a cost benefit analysis.

Or, depending on our findings, we may decide that no further action needs to be taken.

Our progress so far

Theories of harm

We have developed some theories of harm that might explain why consumers are experiencing poor outcomes in these markets. We are testing these by analysing the evidence we gather from firms and consumer organisations and undertaking targeted consumer research. We set out our theories of harm below.

Chosen products

We have chosen five insurance products for our initial data collection from firms and from consumers: guaranteed asset protection insurance (GAP insurance), home emergency, gadget, travel and personal accident. We included products where we think most consumers will be aware of standalone alternatives (travel) and products where they may not.

Firm questionnaires

We have received responses to questionnaires from underwriters and distributors and we are assessing and analysing these, going back to firms where they are incomplete or unclear.

Consumer research

We have commissioned an initial round of consumer research, which is testing product awareness, shopping-around behaviour and the product limitations awareness between consumers who purchased through add-on and standalone channels, taking account of differences in consumer characteristics.

Behavioural research

We have also commissioned behavioural research to test the mechanisms that might come into play in add-on sales and whether these can reduce the extent and effectiveness of consumers shopping around for the best deal.

Call for evidence

The information you provide to us in response to this paper will help us test our theories and decide whether competition is effective in these markets.

Our theories of harm

Based on our work to date on this study, one focus of our study is whether poor outcomes in add-on sales could reflect particular consumer behaviours and firms' responses to them.

The specific context of add-on sales may limit how far consumers explore alternatives or base their decisions on relevant measures of price and quality.

This could happen in a number of ways:

- The nature of the add-on sale may inhibit a consumer's desire to shop around.
- The sale may be based on consumer concerns that have increased during the sale process – for example, if the consumer has just purchased a valuable item and as a consequence has a heightened perception of risk, which creates a desire to purchase insurance cover.
- Consumers may consider the price of an add-on product against the price of the primary product, rather than against the price of relevant alternatives.

These features may interact in complex ways with the fact that firms know more than consumers do about the nature of the cover provided by the insurance.

We will consider whether there are barriers to switching for consumers.

We may also need to assess any potential barriers to entry or other constraints on competition that make it harder for alternative providers to enter the market, expand in the market, or affect the price and quality of add-on sales.

Based on the evidence currently available, we believe that, if there are *common* causes of ineffective competition, they are more likely to lie on the demand-side of the market (i.e. consumers). However, we will also look at potential supply-side constraints on competition (i.e. firms).

What are we testing?

We are testing whether the **prices** are excessive for a given quality. Relevant evidence will include whether insurance products offering equivalent cover are available at significantly lower prices elsewhere, and whether margins and profits in the distribution chain significantly exceed normal commercial rates.

We are also testing whether quality is often not **what consumers reasonably expect**. Relevant evidence will include consumers not understanding and over-estimating the actual cover provided by their policies, and information on claims rates, payouts, claims rejections and complaints.

We believe that **standalone sales** may provide a useful benchmark, after allowing for relevant differences in costs. So we are collecting information from consumers and firms on both add-on and standalone sales.

For example, we can consider the profitability of add-on and standalone sales for underwriters and distributors, alongside evidence on whether consumers who purchased these products actively considered alternatives, and whether standalone alternatives affect the price of comparable add-on products.

In doing so, we need to reflect that some consumers may value the convenience of add-on sales, and they may benefit if firms can reduce their costs by selling add-on products alongside other products.

We are not directly testing for mis-selling or any other form of misconduct by firms – we are focusing on whether competition is ineffective and, if so, why.

Next steps and how to submit evidence

Please email any new or additional evidence to us by 10 September at: FCAGIadd-on@fca.org.uk.

In particular please consider the following questions.

Q1 *Is competition in the sale of GI add-on working well for consumers?*

Relevant evidence here would include:

- a. whether consumers purchasing GI add-ons generally pay more than they need to for given insurance cover
- b. how far consumers can and do shop around between alternative suppliers, and any restrictions on their ability to shop around and switch
- c. how far the products purchased match consumers' needs and reasonable expectations.

Q2 *Where you consider competition is not effective, why do you think that is?*

Relevant evidence here would include:

- a. any barriers to entry and expansion faced by different kinds of firms
- b. any information problems consumers or other market participants may face in these markets
- c. any factors shaping consumer and firm interaction that contribute to poor consumer outcomes
- d. relevant features of add-on sales and how these affect consumers.

We intend to publish these responses, so please send both confidential and non-confidential versions, clearly indicating any confidential information.