Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Policy Holder Protection responses
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Dear Orla

CP21/14 – Policyholder Protection

This is the Financial Services Consumer Panel's response to the Prudential Regulation Authority's consultation paper setting out its proposals to amend the rules for insurance policyholder protection.

The Panel welcomes the aim to create an effective policyholder protection compensation scheme that provides greater protection for policyholders through enhanced compensation scheme rules.

Proposals on compensation limits

The Panel agrees that there should be a link between compensation limits and the risk of significant adverse consequences for policyholders of cover being disrupted or obligations not being paid. We support the recognition that there is a difference between long and short term policies and the effects on the policyholders who hold them.

The Panel has long argued that the limit of 90% compensation for long term insurances such as annuities, pensions and investment life savings was not appropriate because it did not reflect the real value of the product. With the current arrangements there is potential for real detriment to consumers. In many cases these policyholders are locked into a product for many years, and may face penalties for surrendering their policy, and could be vulnerable to a sudden loss of income. Therefore, we strongly support the proposals to increase this limit to 100%.

However, there is a further issue that relates specifically to enhanced annuities that we would like clarification on.

Our understanding of the position, should an insurance company fail, is that the first course of action by the Financial Services Compensation Scheme is to try to place the business with another insurer who will take over the book at market value. With standard annuities this is likely to be possible.

However, enhanced annuities are individually underwritten and therefore the 'market value' of the book will not reflect the actual income being paid to annuitants.

Our understanding is that, if no insurer can be found who is willing to take on the existing book, that 100% (currently 90%) of the market value of the annuity would be paid which is likely to reflect the income paid under a standard annuity and not an enhanced annuity. This could result in a severe drop in income for annuitants in receipt of enhanced annuities and their spouses.

Given the recent pension reforms and the drop in annuity sales, we feel that one or two of the enhanced annuity providers with large legacy books may be particularly vulnerable and we are concerned about the safety of their customers' income in the event of them failing or being taken over.

Yours faithfully

Sue Lewis
Chair
Financial Services Consumer Panel