Financial Conduct Authority

Feedback Statement FS16/1

FS16/1: Feedback Statement on DP15/4 – General insurance value measures

March 2016

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In this Feedback Statement we report on the main issues arising from Discussion Paper 15/4 Developing General Insurance Add-ons Market Study – Remedies: Value Measures.

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Abbreviations used in this paper

DP	Discussion Paper
IDD	Insurance Distribution Directive
GI	General insurance
PBA	Packaged bank accounts
PCW	Price Comparison Website

1. Overview

Introduction

1.1 In July 2014 we published the findings from our general insurance (GI) add-ons market study. We found that competition was not working well for consumers in add-on markets. There was little competitive pressure on firms because add-on buyers were less likely to shop around and were less price-aware than they would be when choosing a stand-alone product.

1.2 We identified poor value in both add-on and some stand-alone products sold by firms, which we measured by claims ratios[1]. For example, for personal accident and GAP add-ons, only around 10% of retail premiums were paid out in claims. Stand-alone personal accident products had an average claims ratio of 15%. In some cases these low claims ratios persisted over a number of years, indicating that firms were not under pressure to improve value. We also highlighted that the lack of a commonly available measure of value to assist market participants with value judgements heightened these issues.

1.3 To address these concerns our market study final report proposed the publication of claims ratios as a market transparency measure. In June 2015 DP15/4[2] explored a number of options for introducing and publishing value measures in GI markets, including the claims ratio. We expect that the publication of value measures data will incentivise firms to improve product value.

1.4 In this Feedback Statement we summarise the responses we have received to the options set out in the Discussion Paper and outline next steps.

Discussion Paper 15/4

1.5 In June 2015 we published DP15/4. The Discussion Paper explored the rationale for looking at value in GI markets and what we hoped to achieve by using transparency as a regulatory tool. We explored how a transparency remedy could work in practice and we set out a number of common features and principles that should apply.

1.6 The DP set out a number of potential options for presenting measures of value:

- the claims ratio as a stand-alone value measure
- a package of measures: claims frequencies, claims acceptance rates and average claims pay-outs ('scorecard option')
- the claims ratio plus claims acceptance rates

1 A claims ratio is broadly the percentage of the retail premium paid by consumers that is paid out in claims by insurers e.g. if a consumer pays £100 for a product and the insurer, on average pays out £50 in claims, the product will have a claims ratio of 50%.

2 DP15/4 Developing General Insurance Add-ons Market Study – Remedies: Value Measures (June 2015) www.fca.org.uk/your-fca/documents/discussion-papers/dp15-04

Summary of feedback

1.7 We received 47 responses to the Discussion Paper from firms, trade bodies, consumer organisations, professional bodies and consumers. The feedback received was very mixed; respondents generally agreed with the need to tackle poor value, but there was no clear consensus about which of the options in the paper was most likely to meet our objectives. Respondents also recognised the difficulty in measuring value in GI markets. Consumer groups tended to favour claims ratios as a stand-alone measure or a combined package of claims ratios and claims acceptance rates, while firms marginally favoured the scorecard option.

1.8 There was strong opposition to the claims ratio measure from firms; they considered it too complex for consumers to understand and ineffective for delivering a rounded assessment of value. There were mixed views about the benefits of the scorecard option, although some respondents recognised the potential benefits of a measure that covers a range of product metrics.

1.9 A number of industry respondents remained concerned about the risk of unintended consequences from the publication or disclosure of any value measure data, such as confusion created by the publication, particularly in terms of point of sale disclosure. There was a concern that consumers would not be able to adequately assess the value measures information, in addition to the consideration of both price and product features. Respondents did however recognise that publication of value measures could improve transparency in GI markets and assist us with more targeted supervision.

What we will do next

1.10 Having considered the feedback to the DP we intend to take forward the scorecard as our preferred option. The scorecard will include claims frequencies, claims acceptance rates and average claims pay-outs, potentially with the inclusion of an average premium metric. We still prefer publication as a market transparency remedy, rather than point of sale disclosure to consumers. We consider the scorecard could give users a wider breadth of information about GI products sold to consumers, while reducing some of the challenges and costs associated with the claims ratio.

1.11 However, rather than consult immediately on introducing a scorecard approach for a broad scope of GI products, we have decided to run a pilot replicating our current preferred scope. This will allow us to refine the remedy design and obtain further evidence of the remedy effectiveness and costs ahead of any potential consultation. We intend to launch a pilot of the scorecard in the summer, on a limited number of products. We envisage that the pilot will cover two one year periods (with two data collection points one year apart) and data will be published on the FCA website.

1.12 We will continue to engage with stakeholders on the pilot design ahead of its launch.

2.
Value in general insurance markets

2.1 This chapter summarises the feedback we received and our response concerning our views on value, and how users may use value measure data.

Value

2.2 In DP15/4 we set out our view that, broadly, value relates to the quality or benefits offered by a product, relative to the price paid for it. We asked:

> ***Q1: Do you have any comments on the aspects of value discussed?***

2.3 Respondents generally agreed that measuring value, and increasing transparency in this area, is a positive step. However, concerns were raised by industry respondents about the absence of 'peace of mind' and customer service from the description, the risk of unintended consequences, the relevance of including premium data, and the need for testing before implementing the full remedy. Respondents cited potential unintended consequences such as: firms not investing in fraud and claims handling, customer service and speed of handling as well as scope of consumer confusion and wider misinterpretation of the value measures data.

Our response

We still believe that measures such as peace of mind and customer service, while important, are too subjective to measure and compare. However, firms are free to publish factual data on their claims themselves.

We recognise the concern raised by some respondents around the potential unintended consequences of introducing and publishing new measures to the market. We believe the pilot of the collection and publication of the scorecard metrics on a small number of products will provide further evidence of the impact of the remedy. Furthermore, we believe that multiple metrics will provide stakeholders with a broader sense of the value offered by a product. Piloting the remedy in this way will also help us mitigate against possible unintended consequences before any potential consultation on the remedy.

In addition to the metrics discussed in the DP for the scorecard, we are also considering including average retail premium data. This could allow for more meaningful comparisons and conclusions about the value on offer.

The introduction of a value measure and how it might work

2.4 In the Discussion Paper we set out that the publication of value measures data would help highlight value in GI markets and improve competition around value. The published information would be used by market participants to exert pressure on firms to improve value. We asked:

> ***Q2:*** ***Do you have any comments on our rationale for introducing a value measure and how we see such a measure working?***

2.5 Firms were concerned that the information would be difficult to incorporate into a consumer friendly measure, with the possibility that many consumers would misinterpret or not use the data at all. Some respondents agreed that publishing the data would incentivise firms to improve product value and would provide the FCA with a tool to further investigate areas of poor value. One trade body also felt that the data could highlight competition issues, disproportionate distribution costs and poor design of products. However, there was a concern raised by firms that publication could encourage competition on the measures at the expense of other product features.

2.6 Six consumer groups responded to this question – all confirmed that they would be interested in the information and that they would use it in their day-to-day work.

2.7 The majority of firms expressed that they did not object to providing value measure data to the FCA, but were more concerned about the publication of the information. Some firms were concerned that consumer groups and the financial press could use the information in an unbalanced and sensationalist way.

Our response

By publishing the value measures data on our website we want to incentivise firms to improve product value. We will publish any data and context in a user-friendly, understandable format and we expect the data will be used primarily by consumer groups, the financial media, firms and us, the FCA. We expect that the combined pressure generated by publicity, changes in consumer behaviour, regulatory intervention and peer review will incentivise firms to improve value. While consumers may access and use the information, the remedy is not primarily designed to be consumer facing at this stage. We intend to pilot the publication of the value measures data.

3.
Introducing a measure of value

3.1 In DP15/4 we explored how value measures data could be introduced to GI markets, covering product scope, measure calculations, granularity of data, data collection, publication and remedy costs.

Scope

3.2 We proposed a list of 26 GI products or risk covers for which value measures data would be reported, as well as naming four products that we felt should be excluded (namely packaged bank accounts (PBAs), no claims bonus protection products, bespoke policies for high net worth consumers and commercial products). We also proposed that the remedy should apply to incoming EEA passporting firms. We asked:

> ***Q3: Do you have any comments on the proposed scope for a value measure?***

3.3 Some respondents commented that we had taken the correct approach by having a broad scope, rather than simply restricting ourselves to 'poor value' products. However, other respondents disagreed and felt that the case had not been made for a broad scope.

3.4 There was general agreement to our proposed exclusions, but a number of respondents felt that PBAs should be included to create a level playing field. Some respondents suggested that additional products should be exempt including private medical, home, motor, legal expenses, breakdown and emergency assistance. Reasons included a claims ratio measure not being appropriate for legal expenses products, because of the service element and complications with measuring claims costs. For other products, respondents felt that they already offered good value or that complications with claims pay-outs could make inclusion too complex.

3.5 Most respondents, including some consumer groups, agreed that data should be collected at product level, e.g. personal accident insurance, rather than sub-product level e.g. personal accident bronze cover. They recognised that sub-product reporting would be more costly and could potentially produce less reliable data. A few respondents commented that our proposal to include EEA firms was beneficial.

Our response

We intend to proceed on the basis of the proposed broad scope set out in the DP, but will continute to engage with stakeholders. We propose to collect and publish the data at product level. The pilot will provide further insight on the merits of a broad scope. Following the pilot and ahead of any potential consultation we will consider whether any additional products should be included or exempt from the proposed remedy.

Granularity

3.6 The DP discussed how granular the value measures data should be, and proposed that the data should be split between add-on and stand-alone sales. We asked:

> *Q4: Do you agree with the proposed product granularity and split by add-on and stand-alone sales? Do you think we should further split data by distribution channel?*

3.7 The majority of respondents agreed on the proposed data split between add-on and stand-alone sales. However, a concern was raised that add-on products could be driven into the standard core products, reducing consumer choice.

3.8 Some respondents questioned the benefit of splitting the data by distribution channel, and raised concerns about data reliability, increased complexity and scale of reporting. However, one firm identified that requiring data split between sales channels would highlight where value is lower.

3.9 Several respondents suggested alternative or additional ways of splitting the data, including splitting between price comparison websites (PCWs) and other brokers or by customer segmentation.

Our response

We agree with the majority of respondents about the appropriate level of granularity and the proposed split of data between add-on and stand-alone sales. This remains our preferred scope. The benefits of collecting and publishing the data at this level, as well as splitting the data by distribution channel, will be tested through the pilot.

We consider that splitting data by customer segmentation will be overly complicated and will produce less reliable data. We will explore the potential for separately reporting PCW sales.

Calculation

3.10 We explored different calculation approaches for the three options proposed in the Discussion Paper. We asked:

> *Q5: Do you have any comments on the proposed calculations? What challenges do the calculations raise, and how might these be overcome?*

3.11 Most firms focused on the claims ratio calculation. Some firms had concerns about specific aspects; for example, the scope for firms to reclassify costs to influence the calculation. A number of respondents emphasised the need for clear calculation definitions and the associated high cost to industry. Concerns were also raised that inefficient firms with higher claims costs could result in misleading claims ratios and reduce efficiency incentives, as higher claims pay-outs would result in a higher ratio. While respondents recognised the rationale for excluding certain service costs (e.g. helplines) they considered that an important aspect of product value would not be captured by the claims ratio.

3.12 For claims acceptance rates respondents highlighted a need for consistency of treatment, for example currently some firms treat consumer enquiries over cover as a claim and others do not. One firm noted that claims declinature data should be available by product, although not necessarily by distribution channel. Respondents questioned whether partially declined claims should be treated as 'a decline.'

Our response

We recognise that creating an appropriate calculation framework for producing comparable data for claims ratio is challenging, because of the range of existing practices by firms. We believe that the calculation for the 'scorecard' option is less complex than the claims ratio. The calculation design will build on the calculation proposals set out in Annex 1 of the DP. For example, claims frequencies could be calculated as the number of claims notified as a percentage of the average number of policies in force. We will continue to engage with firms to test and refine the calculations, with a view to ensuring standardisation of approach for the products in the pilot. The pilot in turn will help us refine calculations before any potential consultation.

Reporting

3.13 The DP proposed that insurers would be responsible for calculating the value measure data and reporting this to the FCA on an annual basis (with a £1m reporting threshold). We asked:

Q6: Do you have any comments on our proposals for reporting?

3.14 Some firms supported a one year reporting period. Others acknowledged that while this was appropriate for some products, a multi-year rolling average would be more appropriate for products with higher expected claims volatility. Other firms expressed a preference for a rolling three-year average across all products in scope, although concern was raised that a multi-year average could obscure product changes.

3.15 Most respondents agreed that insurers and Lloyd's managing agents were the appropriate firms to report the value measures data. However, several firms suggested the Society of Lloyd's should aggregate and report data for Lloyd's managing agents.

3.16 A number of respondents supported the £1m threshold limit proposed in the DP. This set out that where the gross earned premiums for a product are below £1 million, firms would not need to report. One firm suggested there should be a threshold for new products. Several respondents considered that the £1m threshold was too low, especially for large markets (such as motor). However, others were concerned that the threshold will exempt a number of perceived low value products, such as key cover, which should be included. Several respondents suggested that policyholder count would be a more appropriate threshold measure than premium.

Our response

We recognise that for certain products (such as home insurance) a multi-year rolling average may be more appropriate than a single annual reporting period. Nevertheless, we consider that publishing a multi-year rolling average alongside a single annual reporting period for the same product and firm could give a more complete picture.

We do not consider that publication of Lloyd's market data at an aggregated level is sufficient to generate incentives on individual firms.

We will continue to refine the reporting thresholds. This will include any lessons learnt from the pilot, recognising that data from low volume niche products may be challenging from a data comparability point of view.

Publication and contextualisation

3.17 We proposed in the DP that we would publish firm data annually to enable comparisons between products and firms. We explored the option of publishing in percentage bands (for example claims acceptance rates between 80 and 85%) and with market averages, to provide additional context. We also discussed naming brands, to assist users in trying to find particular firms. We asked:

> *Q7: **Do you have any comments on our proposals for publishing and contextualising the data?***

3.18 Most respondents supported publication by us, the FCA, as an independent and authoritative source. However, we were asked to be mindful of keeping the publication as simple as possible. A few respondents expressed concern at the idea of publishing any data, citing potential information overload or confusion for consumers.

3.19 Alternative suggestions were put forward, including creating an industry-only portal on the FCA website to publish the data, and testing publication with real data before implementing the remedy more widely.

3.20 We received mixed views on the use of percentage bands, although the majority of respondents saw the benefits in publishing additional market average information. Some respondents suggested that, instead of publishing data at individual firm level, we should publish at a market-aggregated level to minimise the risk of unintended consequences.

3.21 The vast majority of respondents commented that appropriate contextualisation would be essential, highlighting that it must be given sufficient prominence. There were mixed views on whether firms should be allowed to provide their own context.

Our response

We intend to publish the value measures data on our website at individual firm level. Publishing the data at firm level is important to create the market pressures to incentivise firms to make value improvements. Where appropriate, we believe publication of data in bands is preferable to help overcome confidentiality issues, for example where exact figures could provide insight to a firm's business model. This approach will be tested through the pilot.

Potential costs

3.22 We asked respondents:

> **Q8:** ***What costs – both type and scale – would be incurred in delivering the different value measures discussed? Are there any ways to reduce these?***

3.23 Responses to this question were limited. Most firms considered that the compliance costs would be substantial, and the more granular the reporting requirements the higher the costs. Some firms reported that they were unable to estimate the costs without more detail. Several respondents urged us to utilise existing data to minimise costs, such as PRA returns or Solvency II data. However, one firm and one trade body reported that the costs would not be significant.

Our response

We do not consider that the data provided by the PRA insurer returns or Solvency II reported data provide sufficiently granular information to incentivise firms to improve product value, because of the broader reporting categories. The pilot will provide further insight into the scale and types of costs ahead of any potential consultation.

4.
Assessing value measure options against our objectives

4.1 In DP15/4 we set out three main options for how we might introduce value measures, as well as some alternatives that we did not consider to meet our objectives.

Options for a value measure

4.2 The Discussion Paper proposed three options:

- claims ratio
- claims ratio with claims acceptance rates
- claims frequencies, claims acceptance rates and average claim pay-outs (scorecard option)

4.3 We asked:

> ***Q9: Do you believe the measures discussed can meet our objectives and why? Do you have a preferred option?***

4.4 Respondents focused their comments on the claims ratio. Most firms considered that the claims ratio would not help us meet our objectives for this work, suggesting a number of potential unintended consequences. Risks included: firms reducing their service, limiting their cover, and focusing on claims ratio rather than delivering a good customer experience. Firms were concerned that the claims ratio would not capture service (or quality) and would favour inefficient firms (penalising firms who have strong fraud controls, accurate risk pricing and selective underwriting). Issues with data comparability, consumer confusion and the risk that consumers would not consider cover and benefits were also voiced. However, there was a small minority of firms that recognised some benefit in having a claims ratio value measure, albeit with potential issues.

4.5 A number of consumer groups thought that the claims ratio (with or without claims acceptance rates) would meet our objectives and so this was their preferred option. Additionally, a small number of respondents highlighted that claims ratios and claims acceptance rates have the best chance of showing value while also capturing the experience of consumers who make a claim.

4.6 Some firms considered that the only measure to create a positive impact was the claims acceptance rate metric on its own, and expressed the view that it provides a more accurate reflection of the level of cover relative to expectations.

4.7 Opinions were divided on the scorecard option. Some respondents thought that it could provide users with a fuller picture of value, while others referred to the risk that consumers would be confused or overwhelmed with information. Several firms commented that claims frequency is driven by the demographic of the customer base and therefore not comparable. However, one trade body noted that claims frequency could be useful in helping consumers make informed decisions. Some respondents considered that the average claims pay-out could be misleading because it fails to represent the wide range of claim payments.

4.8 Other concerns across the options included:

- sharing of commercially sensitive data to competitors through publication
- lack of focus on the quality of products and customer experience
- the backwards looking nature of the measures.

Our response

We recognise that inclusion of the claims ratio in a value measure poses challenges. We also recognise the potential of the scorecard option to give users a better overall picture of product value, providing information about how often consumers are likely to claim, the likelihood of the claim being successful and the average claim pay-out. For this reason we intend to take forward the scorecard option. We believe this package of measures provides users with the opportunity to see what is driving the overall value and contains measures that may be more easily understood. We intend to pilot the publication of these measures. We will continue to develop the scorecard and in addition explore whether to include average retail premium alongside the other metrics, to assist with assessments of value and quality.

Other measures we considered

4.9 We set out a number of alternative measures including:

- customer satisfaction rates
- customer retention rates
- time to settle claims
- the percentage of claims settled in full

4.10 We asked:

> ***Q10:*** ***Do you have any comments on the alternative measures discussed? Or do you have any suggestions for how another measure might meet our objectives?***

4.11 The majority of respondents acknowledged the concerns we highlighted about these alternative measures. They recognised that some of the options could be easier than others for consumers to understand – such as settlement times – but that, taken alone, the measures would not give the necessary assessment of value.

4.12 Respondents suggested a number of other alternative measures, including:

- asking firms to give reasons for rejecting a claim
- combinations of manufacture, distribution and servicing costs
- commission and profit
- combined operating ratios
- pie charts showing where the premium is spent
- consumer education
- Defaqto[3] style ratings
- expansion of our already published complaints data.

Our response

We have considered the alternative suggestions put forward but believe they are too subjective to be effective, do not sufficiently show value and/or could undermine the comparability of the data. We think the scorecard option (potentially with average premium information) will provide a fuller assessment of value.

Point of sale disclosure

4.13 We also asked respondents to consider whether the FCA should look at the point of sale disclosure of any value measures, including commission disclosure:

> ***Q11:*** ***Are there any measures you think we should consider for point of sale disclosure to consumers in the future?***

4.14 We received mixed responses to this question. Industry respondents considered that the value measures information should not be disclosed to consumers because:

- the information would not relate to consumers' specific circumstances
- the technical nature of the data would make it unsuitable
- disclosure of this information to consumers would be out of line with our commitment to smarter communications

3 Defaqto publish product star ratings assessing the quality of products based on product features and benefits.

4.15 However, some respondents – including consumer organisations – said that disclosing value measure information to consumers could help with their decision-making. Some firms supported disclosure in the form of a pie chart, scorecard or picture format; making the information easier for consumers to digest and understand.

Our response

We believe that the value measures remedy works best as a market wide transparency remedy. We do not propose to introduce point of sale disclosure of value measure data at this stage but we may consider this again in the future. Instead of direct to consumer disclosures we believe that consumer organisations and other stakeholders are in a good position to assess and process the value measures information into a clear format for consumers. Consumers will benefit from the information in this way.

Commission disclosure

4.16 In the Discussion Paper we considered whether we should require commission to be disclosed to consumers. We asked:

> *Q12:* ***Should we consider commission disclosure – either as a transparency measure or as a point of sale disclosure remedy? How should any such measure be calculated and by whom? What are the benefits and costs of a measure highlighting distribution costs?***

4.17 While a few respondents, including consumer groups, were positive about commission disclosure, a high proportion of respondents did not consider it an appropriate remedy in GI. Industry respondents thought that commission disclosure would be costly, unhelpful to consumers' purchasing decisions and that it could result in information overload and/or confusion. Some industry respondents questioned why we were considering commission disclosures beyond the requirements of the Insurance Distribution Directive (IDD).

Our response

We do not propose to consult on new commission disclosure rules at this stage. We will closely monitor developments in this area.

5.
Next steps

5.1 We remain committed to tackling poor value in the GI market. Following the Discussion Paper feedback we intend to take forward the scorecard option (including claims frequencies, claims acceptance rates and average claim pay-outs) as a market transparency remedy. We intend to pilot the collection and publication of the scorecard data. The format of the pilot will reflect our current preferred approach, as discussed in the preceding chapters.

5.2 As part of the pilot we propose to collect the scorecard data from firms involved in the sale and underwriting of our chosen products. We intend to have two data points, each covering a period of one year. Where possible, we intend to include EEA firms to ensure a level playing field. The FCA will review any data and publish it on our website, alongside appropriate contextualisation, for interested parties to use.

5.3 We intend to collect data for a small number of retail GI products for the pilot. We intend to split this data between firms, by add-on and stand-alone sales and by distribution channel. We will test the impact of the publication as well as collect evidence of the associated costs. Further, we will use any insight gained from the pilot to help refine any proposals on which we may consult.

5.4 We plan to launch the pilot in the summer and will engage further with stakeholders beforehand on the design of the pilot.

Annex 1
List of non-confidential respondents

Admiral Group plc

Alps Ltd

Amlin plc

Andrew Yule Limited

ARAG plc

Arc Legal Assistance Ltd

Association of British Insurers

British Insurance Brokers' Association

British Gas Insurance Limited

BUPA

The Charity Commission for Northern Ireland

Citizens Advice Scotland

DAS Legal Expenses Insurance Company

David J Miller Insurance Brokers Ltd

Epoq Legal Ltd

Esure Services Limited

Financial and Legal Insurance Company Limited

Financial Services Consumer Panel

F J Wakefield

Finance & Leasing Association

Hastings Insurance Services Limited

Institute and Faculty of Actuaries

International Underwriting Association

Lloyds Banking Group plc

LIIBA

Lloyd's

Lloyd's Market Association

MAPFRE ABRAXAS

MoneySavingExpert.com Limited

National Franchised Dealers Association

Paginator Limited

Royal & Sun Alliance Insurance plc

Scope

Source Insurance Limited

Tesco Underwriting Limited

The Royal Bank of Scotland PLC

The Money Advice Service

Virgin Money

Which?

Financial Conduct Authority

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