

## Increasing transparency and engagement at renewal in general insurance

In December 2015, the FCA consulted on new rules and guidance for general insurance renewals. These proposals were intended to address concerns about levels of consumer engagement and the treatment of consumers by firms at renewal, and the lack of competition that results from this. The FCA proposed new rules across all personal lines general insurance markets requiring firms to:-

- disclose last year's premium at each renewal;
- include text to encourage consumers to check their cover and shop around for the best deal at each renewal; and
- identify consumers who have renewed with them four consecutive times, and give these consumers an additional prescribed message encouraging them to shop around.

In addition the FCA proposed guidance on how firms can maintain records to demonstrate compliance, including keeping a record of premiums and non-Handbook guidance to help firms meet their obligations towards consumers at renewal including:-

- providing appropriate information and issuing clear communications to consumers at renewal and
- how firms should treat consumers who want to switch or cancel, and the appropriateness of fees or charges for cancelling or renewing policies.

The FCA published their policy statement outlining the new rules and guidance in August 2016.

### **1. Rule Changes**

The FCA have decided on the following changes to their rules which will come into effect from 1 April 2017.

#### Last Year's Premium

- Firms must disclose last year's premium on all renewals. The total premium payable over the year should be displayed; however firms should also show the monthly premium where the customer pays monthly. If there has been a change part way through a policy year (mid-term adjustment) then the premium shown must be an annualised premium taking into account the change.
- Firms can include wording to explain the annualised premium (where a mid term adjustment has occurred) and can also include wording to explain any price increases.

#### Shopping Around Messages

The FCA have changed the renewals rules so that on each renewal of a policy of 10 months + duration the customer should be prompted at renewal to consider their cover needs and to

also be encouraged to shop around. The wording is not be prescriptive but must still be provided in writing. The FCA has suggested posing this as a question such as:-

**“Have you checked that your insurance cover still meets your needs? Have you considered shopping round to find the best deal for the cover you want?”**

From year 4 onwards as well as including a prompt to customers to consider their cover and whether they should shop around the FCA requires Firms to include the following prescribed wording in a prominent place on the renewal notice:-

**“You have been with us for a number of years. You may be able to get the insurance cover you want at a better price if you shop around.”**

The FCA require that this disclosure be presented **clearly, accurately and prominently** in renewal notices, in a place that makes it easy to compare with the renewal quote. They also expect firms to take into account results of their consumer trials, which showed that disclosure is most effective when on the front page of a renewal notice.

### **Record Keeping**

Firms must ensure that they keep appropriate and adequate records to ensure that they are able to comply with the new rule requirements. In addition these records must be sufficient to allow the FCA to monitor their compliance.

## **2. Non-Handbook Guidance – Improving General Insurance Renewal Practices**

The FCA has published finalised guidance in relation to renewals. A summary of that guidance is as follows:-

- firms need to consider the language in their renewal letters, and consider 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.
- Each time that a contract is renewed, a new contract is created which means that firms need to follow existing rules and guidance at each renewal point. For instance, the appropriate information rule at ICOBS 6.1.5(R), states that:

“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.”

Firms should take particular consideration into the following:-

- an auto-renewal term is considered 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, then the firm should communicate with the customer about how they intend to proceed. A communication could be by way of providing a renewal notice.

- The appropriate information rule also requires that the information is provided in good time. Firms should consider whether their customers have enough time to review their renewal documentation, make an informed decision about it and take appropriate steps, which may include shopping around.
- Firms should 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.
- Firms should take into account Consumer Insurance (Disclosure and Representations) Act 2012 and 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.
- Firms should consider whether and how they are providing consumers with information about their options for 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, firms should focus on the practical steps the consumer would take.
- Firms should consider what options they provide to consumers so that they can express their intention to switch or cancel.
- Firms may also wish to consider whether it would be useful to the consumer to be able to opt out of auto-renewal when entering a contract.
- 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.
- The FCA 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. The FCA specifically call attention to the rule set out at ICOBS 4.3.1 and 4.3.2.

**FCA – Complaint Handling Rules**

The new rules came in to effect from 1 July 2016. The main changes were:-

- Extension of informal complaints from close of next business day to close of third business day;
- All complaints to become reportable including those closed within 3 business days;
- Summary resolution template to be sent with all complaints closed within 3 business days informing clients of the right to refer their complaint to the FOS.

The FCA has also implemented new complaint reporting. For firms with less than 500 complaints a year the changes include:-

**General**

|   |         |
|---|---------|
| Does the return cover more than one entity                      | Yes/No  |
| If Yes list the FRN numbers                                     |         |
| We wish to declare a nil return                                 | Yes/ No |
| Total complaints outstanding at the reporting period start date |         |
| Total number of complaints opened during the reporting period   |         |

This has not changed.

**Table 1 – complaints opened**

|                               |          | Total | Advising, selling and arranging | Information. Sum/charges or product performance | General admin/ customer service | Arrears related | Other |
|-------------------------------|----------|-------|---------------------------------|---|---------------------------------|-----------------|-------|
| Insurance and Pure Protection | Property |       |                                 |   |                                 |                 |       |

The main change above is that the product is now specified and the second complaint category has changed to include product performance.

**Table 2- Complaints closed, upheld and redress**

|  | Within<br>3<br>days | 3<br>days<br>to 8<br>weeks | Over<br>8<br>weeks | Total<br>closed | Total<br>upheld | Total<br>redress<br>paid for<br>upheld<br>complaints | Total<br>redress<br>paid for<br>not upheld<br>complaints | Total<br>redress<br>paid |
|--|---------------------|----------------------------|--------------------|-----------------|-----------------|--|--|--------------------------|
| Total<br>insurance<br>and pure<br>protection |                     |                            |                    |                 |                 |  |  |                          |

The main changes are:-

- within 3 days has been included;
- 4 week timescale has been removed; and
- Redress is now split between upheld and not upheld complaints.

**Table 3 – Contextualization metrics – new information**

Number of policies in force at reporting period end date (insurers).

Number of policies sold within the reporting period.

## **FCA Appointed Representative Thematic Review**

Following identified concerns highlighted in the FCA Business Plan, the FCA has undertaken a detailed thematic review into firms using appointed representatives in the general insurance market.

### **1 Methodology**

The FCA split their review into three phases:-

- Initial online survey of 190 Principals operating a network of appointed representatives primarily in the general insurance market. This was to gain insight into their business models, size, AR activities, governance structures, customer numbers, product types, sales methods and revenues;
- Desk based analysis of 15 Principals from its sample using a risk based approach to ensure representation of a diverse range of business models, products distributed, sales methods and sizes of AR networks. The FCA requested and reviewed further information to gain a greater insight into their businesses and activities of their appointed representatives.
- Finally the FCA visited 14 of the 15 Principals selected and 25 of their appointed representatives. This involved interviewing senior management and staff, reviewing policies and procedures, contractual documentation, customer files and listening to sales calls.

### **2 Findings**

The FCA have stated that the issues identified were serious and widespread and showed that over half of the principal firms did not fully understand the risks arising from their AR activities or were able to demonstrate that they were complying with their obligations to control and oversee their activities.

In five of the 14 firms visited the FCA identified material risks to customers arising from poor practices. This resulted in the regulator taking early supervisory intervention actions in the public interest.

The findings fall under three main headings:

- Business Models and Risk management;
- Governance and Oversight;
  - Due diligence and appointment;
  - Set-up and contracting;
  - Ongoing oversight and termination; and
- Customer Outcomes.

#### **2.1 Business Models and Risk Management**

In this part of the review the FCA assessed whether Principals had considered the impact of appointing ARs on their business and core activities and whether they had put in appropriate

risk management frameworks to enable them to manage the risks associated with appointing ARS.

In particular they considered whether these principals could demonstrate that they:-

- understood the nature, scale and complexity of the risks arising from the activities of their ARs and, in particular, the risks these activities presented to customers;
- had appropriately assessed these risks when deciding to appoint ARs; and
- had taken reasonable steps to put in place an appropriate risk management framework to identify, assess and manage the risks their ARs presented to their business and to customers.

The FCA found the following:-

- Half of the Principals could not demonstrate that they had considered how their potential ARs activities aligned to their existing activities and whether they had adequate resources in place to oversee these ARs and enforce compliance with the AR contract and regulatory requirements;
- The majority of the 15 Principals could not demonstrate consistently that they had taken reasonable steps to assess how the appointment of the ARs would impact their current business model and core activities. This included assessing whether they had adequate resources to oversee their ARs. This generated a significant risk to both the Principal and their customers and in many cases the Principal had not recognised this risk;
- Five firms in the sample acted primarily as wholesale insurance intermediaries distributing their products to customers via other authorised firms. However they had taken on ARs to distribute their product directly to customers and did not appear to have recognised the additional risks and their responsibilities in the sales process. Furthermore three of these did not recognise that the ARs activities were part of their own regulated activities or were capable of ensuring that the sales made were compliant;
- The majority of firms in the sample did not appear to have considered the full costs of operating a compliant AR network and as a result did not have adequate or sufficient resources in place both financial and non-financial;
- Many of the Principals had grown their network rapidly and could not demonstrate that they had sufficient people with the appropriate skills, knowledge and expertise to manage the risks that this growth presented. Furthermore some had altered or broadened their model as they grew but had not made any changes to manage the additional risks that this posed; and
- Three of the Principals operated an “umbrella” network where the primary purpose of the business was to operate a network of ARs and provide a compliance service to these ARs. These principals did not always have full knowledge or control of the

ARs' activities and could not consistently demonstrate that they were meeting their oversight obligations including mitigation of risks to customers.

## **2.2 Governance and Oversight**

The FCA review considered whether the Principal had put in place appropriate governance and systems and control frameworks. This was split into three main areas:-

- the initial appointment of the AR,
- the set-up and contracting of the relationship and
- on-going oversight of their activities.

### **2.2.1 Due Diligence and Appointment**

There are three core elements that a Principal should assess when considering appointing an AR:-

- Impact on the Principal;
- Solvency and suitability of the AR; and
- Adequacy of controls and resources.

#### **Impact of the Principal**

The FCA found:-

- The majority of Principals had not considered the impact of taking on ARs on their own business;
- They had not taken a risk-based approach for the appointment and ongoing monitoring of ARs and generally applied a “one-size-fits-all” approach without taking into account the specific activities being performed by the AR and resulting risks;
- The level of due diligence was generally limited. Examples of areas not addressed were as follows:-
  - The fit of AR's with the Principals business model;
  - Type of products being sold, sales process and method of sale and the needs and risks to customers;
  - Remuneration of sales agents;
  - Additional costs of appointing an AR;
  - The experience and capabilities of the AR and its management;
  - Conflicts of Interest in appointing the AR;
  - Availability of staff with the right skills to monitor and oversee the AR;
  - Any relationship with parties in the value chain which could prevent the Principal from overseeing the AR properly; and
  - Their own experience, knowledge and capabilities.

### Solvency and Suitability of the AR

The FCA found that most Principals had carried out some basic checking prior to contracting with the AR however this tended to be a tick box operation focused on narrow financial measures with no real understanding of the suitability of the AR. In addition this was often only undertaken at appointment and not on an ongoing basis.

The assessment of the solvency and suitability of the AR was usually focused exclusively at the legal entity level with little checks being made on the owners or key senior managers at appointment or on an ongoing basis.

### Adequacy of controls and resources

The majority of firms had little or no evidence that they formally assessed their own systems and controls and resources when appointing ARs and half did not understand this requirement.

#### **2.2.2 Set up and contracting**

The FCA found:-

- Some contracts were not always fully compliant. In many cases they were generic and failed to capture the scope, nature of activities being performed. Often they did not include appropriate parameters and limitations around these activities;
- In some cases where the contract was compliant it was not actively used as a basis for overseeing the ARs activities and relationship;
- ARs activities were not appropriately categorised and the FCA found many examples where the overall set-up of the AR relationship was not consistent with the activities being performed. This included a number of IARs of Principal firms performing activities outside of those permitted for an introducer;
- Where an AR has more than one Principal a multi-principal agreement was not always in place;
- One firm out of the 15 reviewed did not have PII insurance in place for its ARs; and
- Almost all ARs whose primary activities were general insurance had only appointed one approved person. The requirement is that all directors/partners are to be approved persons. It is only where general insurance is a secondary activity that only one approved person is required.

## 2.3 Ongoing Oversight and Termination

The FCA found:-

- The majority of Principals did not have adequate resources in place to monitor and oversee their ARs activities and enforce compliance with the contract and regulatory requirements. These firms often lacked sufficient staff with the necessary skills, knowledge and expertise and found that many of the individuals with responsibility for appointment and monitoring of ARs had little or no regulatory knowledge or training;
- There was a lack of clear policies and procedures and insufficient support to enable staff to perform their oversight role effectively;
  
- Half of the Principals failed to separate ongoing monitoring from management of the commercial relationship with their ARs. In some cases the same person was responsible for both creating a potential conflict of interest;
  
- Firms had not considered the adequacy of resources as their AR network grew;
  
- Effectiveness of monitoring frameworks varied widely. The majority of firms could not demonstrate that they had used a risk based approach to monitoring and consider the specific risks that the AR posed. In many cases a “one size” fits all approach was used. In addition many firms focused their monitoring on training and compliance of the individual sales representatives and did not have effective processes to monitor the following:-
  - Whether the AR and senior management continued to be fit and proper;
  - The financial position of the AR;
  - The quality of the sales process;
  - The quality of advice given to customers;
  - Key performance indicators;
  - Reward and incentive policies and any conflicts of interest; and
  - Compliance with the terms and restrictions set out in the AR contract.
  
- Monitoring undertaken by the majority of firms was not sufficient to appropriately identify areas of potential customer detriment and where issues were identified appropriate actions were not taken. There was an over reliance on IT systems with clearly defined processes and procedures as the primary means to control ARs activities;
  
- FCA also found instances where firms had taken on ARs whose activities were not consistent with their other ARs or had allowed certain ARs to operate outside of normal systems however they had not changed their controls to allow for this;
  
- The majority of Principals did not have adequate and appropriate management information in place to identify key risks and trends within their AR network;

- There was little MI in place to monitor sales incentives and targets and many of these schemes posed a risk of unfair treatment of customers. Often this was exacerbated where the Principal did not have adequate management information on complaints and claims;
- Financial checks and monitoring visits was low;
- One of the key issues identified was the imbalance in the AR relationship often where the AR was significantly larger entity and owned the customer relationship. In some cases the AR was able to dictate the terms of engagement with the Principal in a way which raised material risks that the Principal would not be able to effectively oversee the activities of the AR;
- Most Principals regarding training and competence of sales agents as important and this was an area of focus however the quality varied widely and in some cases the training heavily focused on product knowledge and sales process with no consideration for vulnerable customers and complaints;
- Principals need to ensure that when an AR contract is terminated that need to take appropriate steps to mitigate any risks to customers and that they complete any outstanding regulatory requirements and obligations.

## **2.4 Customer Outcomes**

The FCA expect all firms to be able to demonstrate that fair outcomes for customers is at the heart of their business however this review revealed that the majority of Principals were not able to demonstrate that customers of their ARs were consistently receiving fair outcomes. Main issues were:-

- Most Principals did not exercise effective control and oversight of their AR sales practices leading to risks of customer detriment. The FCA reviews found that there was evidence of serious potential shortcomings and in a limited number of cases they found clear evidence of actual customer detriment. These shortcomings had often not been identified by the Principal;
- Less than a quarter of the Principals could evidence appropriate post sale processes supported by complaints and claims MI and root cause analysis;
- There were shortcomings in the understanding and arrangements required to operate risk transfer effectively with ARs and in a number of cases this resulted in client money not being held correctly in line with CASS rules which poses a risk to customers protection;
- The FCA found significant issues and shortcomings with the sales processes and practices of travel insurance, warranty insurance and GAP.

### 3 Actions

The FCA expect Principals to take the following actions:-

- consider the impact of ARs on their own business model and ability to meet threshold conditions and to assess the solvency and suitability of their ARs including considering owners, directors and partners;
- take reasonable steps to put in place an appropriate risk management framework to identify and manage the risks ARs present to their business;
- put in place compliant contractual arrangements with their ARs which clearly set out the scope of the activities permitted and provide a suitable basis for effective oversight. Principals must also establish whether the AR has multiple principals and where this is the case ensure an appropriate Multi-Principal agreement is in place;
- to have adequate controls over their ARs' regulated activities and to have adequate resources in place to monitor and enforce compliance. In formulating these controls firms should assess the nature, scale and complexity of the business, the diversity of operations including geographical, the volume and size of its transactions and the degree of risk;
- ensure that the ARs are fit and proper to deal with customers in their name, and ensure that customers dealing with the ARs are afforded the same level of protection as if they had dealt with the firm itself;
- To be able to demonstrate that customers who receive products and services delivered by the ARs are being treated fairly, buying products appropriate to their needs and requirements, and receiving fair outcomes.

### 4 Next Steps

The FCA's next steps are:-

- Issuing a Dear CEO letter of relevant principal firms setting out their expectations and actions to be taken;
- Consider the need for further thematic or supervisory work; and
- consider the need for other regulatory actions including assessing whether there is a need for policy intervention or to adjustments to their approach to authorisations.

**IF YOU HAVE APPOINTED REPS AND HAVE ANY CONCERNS PLEASE CONTACT US FOR A FREE INITIAL ASSESSMENT.**