General insurance pricing conduct: getting the price right

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Introduction

The recent publication of *Guiding Principles and Action Points for General Insurance Pricing* (GPAPs) by the ABI and BIBA, shortly after the *Financial Ombudsman Service April Newsletter* devoted to general insurance (GI) pricing complaints, has once more placed GI pricing in the spotlight. *The Household Pricing Practices Review* by the Financial Conduct Authority (FCA) will provide further focus on this issue when its report is published later in 2018.

Given the ongoing discussion on pricing of GI products by regulators and trade bodies, it is critical that insurers and brokers revisit their approach to pricing. In particular, firms should consider how their approach compares with evolving regulatory expectations and industry best practice.

Increased regulatory interest in pricing

Historically, the FCA has argued that it is not a pricing regulator and its level of intervention in the market has been relatively light. However, given the FCA’s objective of ‘making markets work well so that consumers get a fair deal,’ it may mean that the FCA needs to start intervening more directly in the market. There are indications that it has been increasingly doing so over the last 12–18 months:

- **Premium disclosures and addressing customer inertia:** The FCA introduced requirements for insurers to show last year’s premium on current renewal notices. In addition, the FCA set out an expectation that insurers should proactively encourage customers to shop around at the point of their fourth annual renewal.
- **Household Pricing Practices Review:** The review, currently reaching its conclusions, is wide-ranging and includes an assessment of firms’ pricing strategies, philosophies and approach, and controls including governance and oversight.
- **Pricing policy:** The FCA has indicated to a number of insurers over the last two to three years that they expect board oversight over pricing policy both from a prudential and conduct perspective. A number of firms have introduced ‘capping’ policies for renewal premiums, although the degree to which these have been applied and monitored has varied.
- **Access to insurance:** The FCA’s feedback statement on its ‘Call for Input on Access to Travel Insurance’ had a number of findings including, a lack of transparency of price. FCA findings will be used to inform their wider work on insurance pricing.
- **The FCA has considered the use of big data in recent years, most notably in relation to general insurance. The 2018/19 Business Plan sets out the intention to assess whether they need to act to ensure that insurance pricing practices support a market which works well for customers. Conclusions from the review of big data, published in September 2016, will form part of FCA considerations.**
The ABI and BIBA GPAPs

In May 2018, the ABI and BIBA launched a set of GPAPs that address how insurer and broker members intend to combat excessive premium differences between new and long-standing customers. The GPAPs apply specifically to personal lines insurance products but not pet and health insurance. The guiding principles are as follows:

► Member firms do not support penalising long-standing customers through significant differences between new and renewal premiums.
► Better outcomes for long-standing customers is a commitment of members. However, wider market adoption will be required for consistent outcomes.
► Members support the requirements to disclose the previous year’s premium prices and recognise the importance of implementation by all market participants.
► Action will be taken by members to ensure customers’ tendency to shop around at renewal does not unfairly penalise those customers who remain with their insurer year on year.
► Member firms will ensure that the impact of pricing on outcomes for long-standing customers is given board and/or senior management priority, and the approach is embedded at renewal pricing procedures.

The GPAPs require that member firms are able to evidence the steps they have taken to address significant differences in pricing for new and renewal premiums. The action points associated with the guiding principles are:

1. Members should ensure customers are clearly informed that new customer premiums only apply for the relevant year of coverage and renewal premiums may be higher. This communication can be written (including online) or verbal.
2. Members involved in establishing the final premium paid by customers should review and assess their approach to pricing for customers, who have been with them for longer than five years, to ensure it delivers a fair outcome.
3. To ensure outcomes for vulnerable customers are considered in line with these guiding principles, members will review their customers’ tendencies to shop around at renewal in line with the existing code for potentially vulnerable customers.
4. In no more than two years, the ABI and BIBA will report on the actions taken by members to combat excessive premium differences between new and long-standing customers.
5. In the event where it is found that excessive differences in premiums unfairly penalise long-standing customers, the ABI and BIBA will not seek to defend such cases.

The ABI and BIBA suggest that the FCA take these GPAPs into account when performing supervisory activities and its current review of GI pricing.
Financial Ombudsman Service (FOS) setting policy on pricing

The April 2018 edition of ‘Ombudsman News’ contained a number of case studies about price-related complaints. These provide a number of principles regarding what constitutes ‘good practice’ in pricing and some of the factors to be taken into consideration when handling price-related complaints. These principles include:

► Apparent acceptance, in principle, of firms offering new business discounts, but an expectation that the discount to be made up over five years.

► A recognition that premium calculations are complex, but an expectation that premium increases should be calculated on a risk basis only, treating customers fairly in the process.

► FOS case assessments that take into account the individual circumstances of each case and what the customer would likely have done (i.e., if they had been informed they could get cheaper equivalent cover elsewhere).

► The FCA requirement, from April 2017, for insurers to take additional steps to encourage customers to shop around at the fourth annual renewal of their policy, is a consideration in case assessments.

► An increased consideration of, and making judgement calls on, the point at which a customer’s vulnerability should have become apparent to the insurer (i.e., for purposes of assessing potential detriment and calculating redress as required).

► An expectation that insurers should proactively spot the signs of customers’ inertia in relation to price and to take action accordingly (i.e., by contacting the customer when customers do not shop around or challenge renewal prices for prolonged periods of time).

► A potential good practice expectation that insurers will review premiums, if an ‘at fault’ claim decision which impacts premiums at renewal (e.g., on a motor policy) is later overturned.

► A provision to challenge the fairness of broker commission charges (i.e., whether the charge was justified and reasonable).

Redress outcomes for cases upheld by the FOS can include a refund of premiums, a refund of the difference in premiums, additional interest – usually payable from the date each premium was paid until the date of settlement – and compensation for trouble and upset.
Actions for insurers and brokers

The ABI and FOS publications provide a useful reference point for insurers and brokers, and we would expect the FCA’s Household Pricing Practices Review report to provide more definitive, and ideally detailed, reference points for regulatory expectations on pricing going forward.

However, we believe the challenge to ensure fair pricing for long-standing customers is wider than simply documenting strategy and policy standards. Whilst some insurers and brokers already have a pricing strategy and a pricing policy, the degree to which such a strategy is implemented and monitored does appear to vary. Insurers and brokers should ensure that they define, document and monitor their fair pricing policy frameworks. A typical framework would have the following characteristics:

1. A documented pricing policy setting out key pricing principles and tolerances.
2. Sign-off of that policy by the board together with an annual review of the policy.
3. Alignment of the pricing policy to other relevant policies such as vulnerable customer policy, complaints policy, data policy and conduct policy.
4. Procedures setting out how the pricing policy should be applied across the business, including:
   - Principles to be applied to pricing.
   - Requirements for the development and publication of marketing materials and customer communications.
   - Standards for quoting and addressing customer challenges of premium including the level of discretion given to internal staff and third parties to adjust premiums in these instances.
   - How to assess and manage expressions of dissatisfaction relating to pricing including regulated complaints and FOS complaints.
   - Approach to root cause analysis (RCA) in relation to pricing complaints.
5. Training for all relevant departments on the pricing policy and how it impacts their role and aligns with other policies.
6. Oversight of the implementation and operational effectiveness of the framework. This should include: monitoring of implementation and the roll out of training; establishing operational controls; key performance indicators and triggers throughout the customer life cycle; monitoring of how the firm is complying with the policy; and that customers are being treated fairly.

Diagram 1 provides an overview of the elements which we would expect to be included in a conduct-focused fair pricing framework.

Diagram 1: Pricing framework
How EY can help

EY can provide an independent assessment of the appropriateness and effectiveness of your firm’s GI pricing framework. We can assess the frameworks against known regulatory requirements, developing regulatory expectations and industry practices. This independent assessment can provide assurance to senior management and the board in the following areas:

► **Board oversight:** Assess board involvement in pricing strategy.

► **Fair pricing policy:** Review pricing policies and links to other conduct related policies and test if and how these are applied in practice.

► **Policy implementation:** Review the effectiveness of documented processes and procedures, associated training and test if and how they are applied in practice.

► **Tracking and monitoring:** Review the appropriateness of pricing MI and assess the effectiveness of the use of pricing MI and decisions made as a result.

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