# Sales Regulation for Healthcare business

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# Agenda

1. Regulation of distribution and advice — John Maud
2. TCF and product design issues — Bernie Hickman

- What's changing and has changed?
- Impacts on market structure and behaviour
- Impact on consumers
- Impact on products

# Shifting regulatory boundaries

- Most term and health policies outside scope of FSA 1986
  - but included within scope by Lautro
  - and treated as investment business by most providers/distributors
- PIA general waiver December 2000
  - subject to conforming with ABI Selling Code of Practice
- FSA regulation January 2005
  - implements Insurance Mediation Directive
  - extends to most non-investment insurance sales and administration
  - all Long Term Care treated as investment business

# Impacts of regulatory change: Housing market

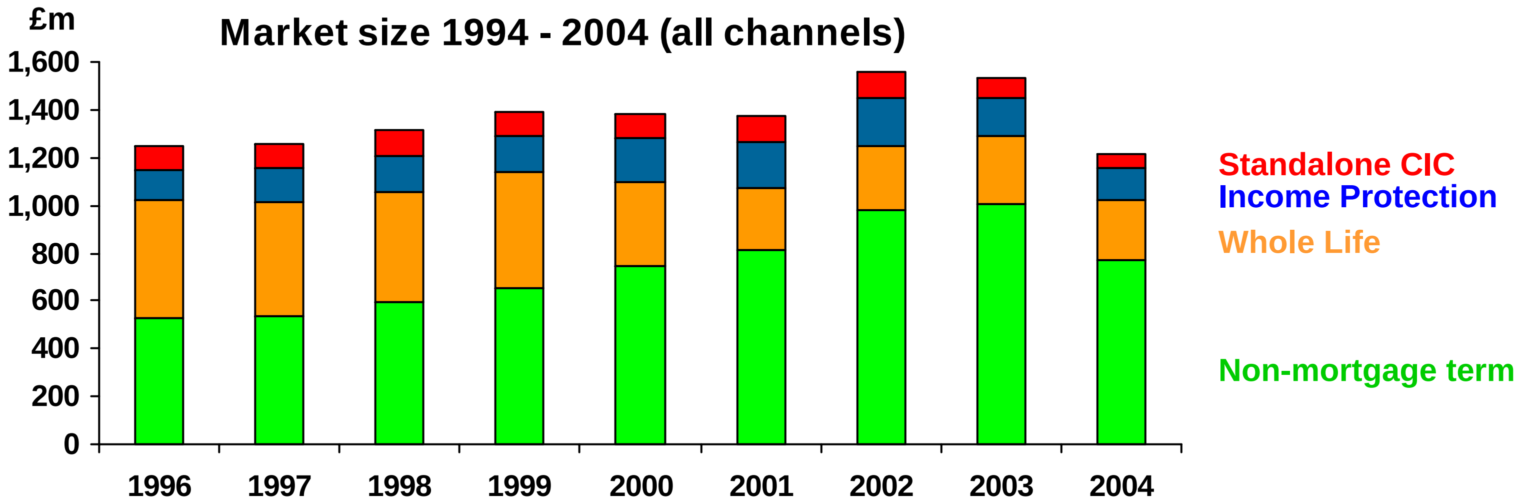
- 2000/1 deregulation followed endowment mortgage demise
- Shift in mix of mortgage adviser earnings:
  - from endowment to additional protection
  - from protection to mortgage
- Expansion of mortgage adviser numbers:
  - more limited training requirement
  - simpler process + increasing use of technology
  - mortgage term assurance sales trebled 2000 - 2002
  - 42% with critical illness in 2000 - down to 35% by 2004
- Single-tied model survived “depolarisation” in 2000/1:

| | 2000 | 2004 |
|---|---|---|
| • Tied mortgage protection as % sales | 61% | 51% |
| • Other tied individual L&P as % sales | 35% | 22% |



*Source: ABI*

# Impacts of regulatory change: Long Term Protection market




- Life company Direct Salesforces in decline
  - total sales 75% down from 1996 - 2004
  - non-mortgage protection sales down c. 50%
  - approx. 35% of 2004 sales - substantially Bank-based
  - investment regulation has driven down protection business
- IFA non-mortgage protection sales up just 7% since 1996
  - in effectively unchanged regulatory environment



*Source: ABI*

# Some headlines of FSA Protection regulation

- Selling practices
  - advised vs. non-advised sales
  - “demands and needs” statements
  - “lighter touch” than for investments, related to nature of policy
  - but advice does require understanding/probing of customer needs
  - consistent approach for long term/short term insurance contracts
- Commission and inducements
  - no requirement for disclosure - but generally continues voluntarily
  - no prohibition on volume overrides or profit commission
  - general prohibition on inducements that are “likely to conflict to a material extent with any duty that the firm owes to its customers”
- Firms responsible for their Appointed Representatives
  - ARs can have multiple hosts…but complex to manage

# Market impacts of 2004/5 FSA regulatory changes

- Mortgage regulation the prime driver in Housing Market
  - higher standards of advice and record-keeping
  - protection business included in e-enabled processes
  - single-tied model easy to sustain
  - Mortgage Networks with multi-tied protection emerging
  - limited or no customer choice of provider
- Multi-ties: convergence of remaining DSFs and some IFAs
  - Protection & Healthcare part of product mix to meet customer needs
  - limited customer choice

# Market impacts of 2004/5 FSA regulatory changes

- Most IFAs to stay as independent whole-of-market advisers
  - some with separate mortgage business arms
  - Protection & Healthcare propositions largely unchanged
- General Insurance intermediary market consolidation
  - smaller agents merging/becoming ARs/joining Networks
- Reinsurance impacts of depolarisation
  - IFA/tied agent split previously used as index of business quality
  - primary insurers now need to convince reinsurers of agent quality by other means
  - FSA regulation now means status clearer and placing of business more certain

# Other impacts

- On consumers:
  - improved advice processes and disclosures
  - benefits of FSA complaints process and Financial Ombudsman
  - clarity over status of advisers…?
  - more limited product and provider choices
- On products:
  - reduced availability of products classed as investments
  - impact of FSA approach to fair treatment of customers

# Treating Customers Fairly(TCF) – What is it?

**FSA requirement that firms treat customers fairly**

**FSA Principles setting out TCF:**

- **Principle 6: A firm must pay due regard to the interests of its customers and treat them fairly.**
- **Principle 1:** A firm must conduct its business with integrity.
- **Principle 7:** A firm must pay due regard to the information needs of its clients, and communicate information to them in way that is clear, fair and not misleading.
- **Principle 8:** A firm must manage conflicts of interests fairly, both between itself and its customers and between a customer and another client.
- **Principle 9:** A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement.

# What has changed?

- Looking after your customer is not new
- Recent FSA emphasis is:

  "…this principle must be adopted and supported by the leadership of financial firms, and embedded throughout a firm's operations and within its culture."
- Reaction to market failures
  - Pensions, Endowments, Precipice bonds, Split capital investment trusts
- Complex products and poor customer capability leads to an imbalance of information and understanding
- FSA papers issued:
  - June 2001
  - June 2002
  - July 2004 (Good summary)
  - Case studies
  - Cluster reports
  - Speeches

# Achieving TCF

- “Blend of regulatory and market-based solutions”
- Several sticks:
  - Authorisation
  - Standard setting
  - Supervision
  - Enforcement
  - Statements of good practice
  - Lots of documents illustrating good and bad TCF
- Two carrots:
  - If firms treat customers fairly this will increase consumer confidence in the firm and the industry
  - Increased consumer confidence will be good for firms as it will mean
    - **Higher sales from happier customers**
    - **Less intrusive and less costly regulation**

# Impact on providers

- Good common sense customer focused decision making
- TCF is big – consideration of all stages of product life-cycle
  - corporate strategy and culture;
  - product design and governance;
  - financial promotions;
  - sales and advice process;
  - information provided after the point of sale; and
  - complaint handling procedure
- Directors and senior management responsibility for fairness vs Appointed Actuary responsibilities

  "The responsibility for delivering TCF lies with firms' senior management, who need to be **intelligent**, **thoughtful** and **effective** in their implementation of the TCF requirement"
- On the agenda for FSA visits
- Evidence of effective delivery required

# How do you evidence effective delivery across whole business?

- Establishing TCF programmes
- Formal committees with documented decisions
- Product development check lists
- Research projects to evidence customer understanding
- Systematic consumer risk “brainstorming” meetings
- Comprehensive reviews of existing products and processes
- Processes to ensure learning points remembered and addressed
- Reviews of all literature and documentation
- Training for staff on TCF
- Internal communication programmes
- Formal sign off for all external communication
- Complaint handling processes and training

# Consumer impact

- Products, literature and processes influenced by consumer research
- Literature clearer and more explicit
- Better customer experience throughout life of product
- Simpler more transparent products
- Less discretion in management of products
- Fewer products?
- Higher premiums to pay for higher costs?
- Fewer providers – only the big can afford the high fixed cost of product manufacture?

# Challenges of TCF(1)

- Imbalance of customer understanding capability with unavoidable complexity of products
  - E.g. Reviewable premiums
  - Customers need to understand the bargain they are entering into
  - How much do you tell the customers – enough to truly understand would not be understood or welcomed by customers
  - Communication that premiums are reviewable must be as clear as possible
  - Beneficial to explain the choice between guaranteed and reviewable
  - Providers need to be explicit about the “valid reasons” for a change in premium
  - Amount of discretion in process needs to be minimised
  - Documentation is vital
  - Expect interest from FSA if increases in existing premiums are out of line with the market or new business premiums
  - No wording and process can be incapable of challenge but substantial steps can be taken to attempt to mitigate risks of challenge
  - Papers will be emerging soon from both FSA and ABI in this area
  - Treatment of existing business

# Challenges of TCF(2)

- Prevailing customer apathy towards financial products
  - Clearest literature of no use if customer doesn't read it
- How to enhance consumer understanding?
- Methods are subjective: Non-disclosure and not meeting CIC definitions
- "*Standard Life is ready to fight the cause of critical illness cover with the publication of its declined CIC claims*" Financial Advisor 21/04/05
- Does TCF imply releasing declined claims stats?
- "*If companies are reluctant to issue this data, it could be because what they have to say will look bad. If they cannot defend it, it is not treating the customer fairly. I think silence implies guilt*." Kevin Carr, Lifesearch
- Pros: highlights the important issues of non-disclosure and understanding CIC definitions in a high profile way
- Cons: potential to unnecessarily alarm existing and new CIC customers who have carefully and completely answered the application form questions and are worried about getting a critical illness which is covered by their CIC policy

# Challenges of TCF(3)

- Focus on meeting likely consumer need or consumer/advisor demand?
- Requirement to develop products that do what the **customer thinks** they say on the tin?
- "Balancing the commercial objective of increasing sales with the objective of TCF"
  - Occupation related TPD vs FATS/ADW based TPD
- Only sell products customers understood – what would we be selling?
  - Suicide clause on life policy: "If, within the first year of the policy, either Life Assured commits suicide, the policy will be void. This condition shall not prejudice the interests of any third party who has bona fide acquired an interest for valuable consideration"
- Starting set of products and terminology
  - E.g. Income Protection

# Going forward

- TCF is here to stay
- FSA needs to be realistic about challenges
- Redesigning products and wordings will require courage and calculated risk taking
- Are more TCF industry initiatives required ?
  - Identify as an industry areas of potential customer risk
  - Reviewable premiums?
  - Non-disclosure and underwriting process?
  - Critical Illness Cover including TPD?
  - Standardise and improving terminology?
  - Communication/Training for advisors?
- For protection products what presents the biggest risk of customer (and their dependants) detriment?
- Not having enough cover?