Institute
and Faculty
of Actuaries

CP19/8: General Insurance Value Measures Reporting

IFoA response to the Financial Conduct Authority

30 April 2019

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We strive to act in the public interest by speaking out on issues where actuaries have the expertise to provide analysis and insight on public policy issues. To fulfil the requirements of our Charter, the IFoA maintains a Public Affairs function, which represents the views of the profession to Government, policymakers, regulators and other stakeholders, in order to shape public policy.

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Institute and Faculty of Actuaries

Tony Stubbs
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

30 April 2019

Dear Tony,

IFoA response to CP19/8: General Insurance Value Measures Reporting

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the FCA's consultation paper (CP) on general insurance value measures reporting. Given the scope of the FCA's proposals within the CP, our General Insurance Standards and Consultations sub-Committee and General Insurance Board have been involved in the drafting of our response. Members of the Committee and Board work for a range of product providers and consultancies in the general insurance sector.

2. It is important to note that, as for any IFoA consultation response, we have considered the issues relevant to the FCA's proposals from the perspective of the public interest.

General Comments

3. The IFoA supports the FCA's intention to deliver better consumer outcomes by addressing poor product value and quality, and reducing the risk of unsuitable general insurance products being bought or sold. We support the use of value measures in principle, and we set out a range of constructive points in this response which we hope the FCA find helpful.

4. We welcome greater information and transparency for consumers through value measure reporting. Such reporting could be helpful to consumers where it is succinct and clear in purpose. However, we would urge the FCA to consider the consequences of overloading consumers with information: it will be easier to recognise the value of the reporting if it is targeted, relevant and accessible. It is also important to convey to the consumer that lower price does not always equate to better value.

5. As explained in the CP, the proposals are essentially the extension of an earlier pilot of value measure reporting. It would therefore be useful to understand whether the FCA had undertaken any research or otherwise gained feedback on how effective the publishing of the pilot data had been, including the impact on consumer behavior, before deciding to expand the reporting.

6. We also encourage the FCA to consider any potential unintended consequences and wider considerations which could arise following the implementation of its proposals. These include potentially misleading comparisons and possible issues relating to the use and publication of

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the proposed measures. We cover these in the next section, before answering the consultation questions.

7. Given potential unintended consequences we recommend that, before publishing value measures, the FCA collects the metrics and then analyses them, considering their potential policyholder and market impacts. Careful interrogation of the data and its implications – prior to publication – would obviously not prevent data collection in the first instance. We would be delighted to engage with the FCA to provide our perspective on such analysis in due course, if that were helpful.

Potentially Misleading Comparisons

8. Comparing metrics at a market level is beneficial to understand trends. However, there are a number of limitations which may distort the results of such comparisons. These limitations include, for example:

   - **diversity in insurance cover**: there is a variety of levels of insurance cover ranging from enhanced to basic and the policyholder may have made an informed choice over the level of cover depending on premium levels;
   - **diversity of insurers:** recognising the impact of the proposed data thresholds, the size of insurer and volume of business written may still impact the reliability of metrics, with an impact on the comparability between firms;
   - **variety in cover excess**: insurance costs may differ due to the impact of different policy excess levels. Again, the policyholder may have made an informed choice over excess in order to lower their premium;
   - **impact of fraud management:** should an insurer be more effective at monitoring and managing fraud, they may then appear worse than other insurers from a claims (payout) frequency perspective, which is counter-productive;
   - **dynamics of niche markets:** should an insurer enter a niche segment of the market, the frequency and average costs may naturally be different. Were these dynamics to drive consumer behaviour, it may mean that an insurer is less likely to enter the niche, which would lead to a reduction in market competition.

9. Avoiding misleading comparisons could potentially be addressed by describing appropriate factors to consider when comparing value metrics. However, care would need to be taken to ensure such caveats did not obscure the message/ purpose of the reporting.

Understanding of Metrics

10. It would be interesting to understand the extent to which customers accessed the data produced through the pilot, and the extent to which these pilot metrics were valuable to customers.

11. It is important for users of metrics to understand their context, to help interpret them in a useful manner. For example, not all metrics are directly comparable, as has been noted above. Understanding data context also extends to being aware of caveats relating to data, such as the danger in reaching conclusions based on a limited number of data points.

12. There is also the risk that the users of the metrics may not understand that systemic factors could affect large numbers of claims, such as a recession, when insurance cover may be particularly valuable. This would by nature impact the value measures reported and may not be recognised accordingly.

13. Consumers may compare products which have very different features e.g. a product which is low frequency/ high severity of claim with another product that is high frequency/ low severity of claim. It is then possible that a consumer could compare only the frequency of the claim and then infer that the low frequency product is of low value, which may not be the case.

14. Undue focus on low frequency/ high severity claims could have an adverse market impact, which may not be in the public interest. Products with a low frequency/ high severity claim feature could well remain highly valuable, but if market volumes were to decrease as a result of misinterpretation of value measures, then this could lead to potential significant protection gap consequences.

Publication of Metrics

15. As noted in our general comments, the IFoA suggests the FCA considers analysing value measure metrics and their implications, prior to publication.

16. We also encourage the FCA to consider whether the proposed approach should be considered in conjunction with other data already collected by industry bodies (e.g. ABI statistics), to avoid duplication of reporting.

17. We suggest the FCA considers whether there is potential to derive metrics from information included within the Solvency II Solvency & Financial Condition Reports (SFCRs), including the publicly-available Quantitative Reporting Templates (QRTs) already produced by firms. In particular, were the solvency regime in the UK to evolve (either with Solvency II changes or possible changes post the UK exiting the EU), this then may provide a future opportunity to align the information produced to reduce duplication for firms.

18. There will often be reasons for why a firm may seem out of line from the metrics of peers, other than related to the insurer providing poor value. We therefore suggest that it would be in the public interest for firms to have the opportunity to comment, for public consumption, on context and potential reasons why specific measures may seem to be out of line with peers.

Consultation Questions

Q1. Do you agree with our proposals for the product scope?

19. We believe the proposed split of products is very granular. Whilst this has a potential to provide useful information for consumers, there is a significant risk that the granularity becomes confusing for consumers. The highly granular split of business is also likely to present challenges for data collection for insurance firms. Some of these products may be more detailed than the claims/ product data classes adopted by firms, and such granularity might present challenges for insurers when separating out all these elements from their existing claims/ product data systems.

20. With this level of granularity, there is also a risk of a reduced ability to draw conclusions and transparency on how comparable the products are between insurance firms. For example, *loss of keys* can be an add-on for some policies, or otherwise be included in some extended levels of core insurance cover.

21. Whilst the original pilot covered largely short-tail business, the current proposal includes a range of products which have different dynamics. For example, long-tail bodily injury claims

and extended warranty insurance covers will naturally lead to more delays in reporting from the policy inception date, than in the original pilot. Such delays would also impact values of average claim pay-out built on historical claims.

22. Some of the additional classes may be more likely to have partial payments which could distort the average claim pay-out metric. Periodical Payment Order claims for motor insurance in particular would be a significant example.

23. One potential unintended consequence of having a very broad product scope is that consumers compare products which have very different features, and reach flawed conclusions in such a comparison.

Q2. Do you agree with our proposals on reporting responsibility?

24. We would recommend that all insurers writing business in the UK should report the information, to provide as complete a view of the UK experience as possible.

25. As the FCA will realise, the impact of Brexit is currently uncertain in relation to what is expected from EEA countries. An approach on how the FCA's requirements will be updated as clarity on the outcome of Brexit emerges would be useful.

Q3. Do you agree with our proposal to require data to be split by the largest distribution arrangements?

26. Whilst we support the intent behind reporting metrics by distribution, there are a number of considerations to note:

- different measures may exist across different distribution arrangements which may not relate to the value of the product being provided. For example, there may be higher average excess levels (and hence lower claim frequency) for some distribution arrangements. There is then a risk that a consumer may deduce (incorrectly) that some distribution arrangements represents better value over those with higher excesses;
- we would welcome greater clarity over how the distribution arrangements are defined. Taking extended warranty as an example, would the top five partnership arrangements need to be reported, or would all partnership arrangements be combined as one?;
- presenting these metrics for both each product and different distribution arrangements may bring further challenges in terms of the level of granularity being presented. Again this has the potential to confuse consumers.

Q4. Do you agree with our proposals for the treatment of add-ons and optional extras?

The IFoA does not have any points to raise in answer to this question.

Q5. Do you agree with our proposals for the granularity, reporting periods and frequency?

27. We note that the calendar year end is already a busy time for firms due to numerous reporting requirements and deadlines. It may be useful for firms to produce the information after they have produced their year-end report and accounts and Solvency II SFCR. A staggered timing may allow firms to allocate appropriate available resource to produce the proposed values metrics. Such timing would also be helpful if there were scope to leverage off Solvency II or other existing metrics, after they had been produced.

28. We do not believe that reporting more frequently than once per annum would help users, due to the volatility and seasonality of the data being reported. We think it would also be unnecessarily onerous to ask firms to produce the metrics more frequently, for little potential gain.

Q6. Do you agree with our proposals for reporting thresholds?

29. We suggest it would be useful to understand what feedback was provided from participants in the pilot to ensure the reporting thresholds are appropriate.

30. It would also be useful to understand how many companies would then need to produce the metrics based on the suggested thresholds. We note that the division of data means that for many classes, they will need to be reported by individual insurers. Conversely, there is the potential that for some lines of business, there will be a very small number of insurers who would need to report due to the thresholds. This could limit the usefulness of any comparisons in these markets.

31. One of the proposed thresholds relates to written premium in a reporting year. Although a single premium-based threshold is simple to apply, we suggest the FCA considers whether the premium threshold should vary by (broad) product type.

32. Although it may be unlikely, there is a potential incentive for 'arbitrage' in volumes of business between the elements in order to avoid reaching the threshold on specific products. This has a potential to reduce competition.

Q7. Do you agree with our proposals on the value measures metrics?

33. We refer to the value measure metrics proposed, i.e.:

    - claim frequencies;
    - claim acceptance rates;
    - average claims pay-outs; and
    - claims complaints as a percentage of claims.

34. As we mentioned in our feedback to '*General Insurance Market Add-ons Market Study – Remedies: Value Measures'* in 2015, we do not consider that these measures would meet the FCA's stated objectives. Given the complexity of the insurance value chain these measures may not directly expose poor value. A range of values in reported metrics may instead be due to differences between firms due to different business models, different products, levels of cover and customer segments. One such example would be third party claim frequency for a young driver motor portfolio will be significantly higher than that of the industry average.

35. More generally, the use of average claim payments will fail to highlight the potential wide range of claim payments that can take place in individual claims. Examples of this can again be found in motor insurance where a severely injured claimant could have a multi-million pound claim, or in home insurance where a severe flood could produce an individual claim payout of many hundreds of thousands of pounds.

36. Furthermore, the metrics rely on settled claim data. This can create distortions for long-tail products as the value measures metrics may be reflective of policies sold several years previously, rather than policies sold recently.

37. The value measure metrics do not provide a view relative to premiums. As mentioned previously, the suggested metrics would not enable a fair comparison between policies providing enhanced cover and those providing basic cover.

38. The new measure being proposed (claims complaints as a percentage of claims) is also subject to the challenge that some policyholders purchase their insurance policy based on price, rather than quality of cover. This means that whilst this measure may reflect concerns over mis-selling, it does not relate to the level of premium paid nor quality of cover provided. A more useful measure may be to consider claim complaints *upheld*, as a percentage of claims.

39. As we mentioned earlier, one approach could be for the FCA to collect further value measures data, but then consider its potential implications before any publication. Any such analysis could help inform potential refinement of the data considered necessary.

Q8. Do you agree with our proposals on metric definitions?

40. We have a minor comment in relation to this question. Insurers may have limited information to identify so-called ‘walkaway’ claims; this may then lead firms to treat them as nil settled claims.

Q9. Do you agree with our proposals for the publication of value measures data in bands?

41. We would welcome additional clarity over the proposed bands in order to form a view on this question.

Q10. Do you agree with our proposals to add a specific requirement to our rules to cover the use of value measures data in the product oversight and governance process?

42. The IFoA agrees in principle that value measures data is relevant to product oversight and governance. As mentioned earlier, we would encourage the FCA to recognise that the provision of information does not in itself ensure better outcomes for consumers. It is also important to communicate to consumers that a lower price does not necessarily equate to better value. However, company peer pressure, and - if policyholders pay attention and understand them - value measures data may well have a role in improving competition and consumer value.

Q11. Do you agree with our cost benefit analysis?

43. We have a general comment in relation to this question. As we have explained, we support the use of value measures data in principle, and where the impact on insurers (both in terms of producing the metrics and their impact on the market) is proportionate and in the public interest.

Should you want to discuss any of the points raised please contact Steven Graham, Technical Policy Manager at Steven.Graham@actuaries.org.uk or on 020 7632 2146 in the first instance. In particular, we would be delighted to provide our perspective on any values data collected and it implications, as noted above.

Yours sincerely,

John Taylor
President elect, Institute and Faculty of Actuaries