Fairness in Pricing
Chloe Paillot, Kevin Wenzel
IFoA GI Standards & Consultations Committee

What has the FCA looked at so far?

Previous FCA publications which raised concerns on GI firms’ pricing practices

Latest FCA publications on pricing

Pricing Practices in Retail GI – Household TR18/4

Increasing transparency and engagement at renewal in GI PS16/21

Provision of Premium Finance to Retail GI customers TR15/5

Price discrimination and cross subsidy in financial services OP22

FCA publishes 1st GI Value measures pilot

FCA publishes 2nd GI Value measures pilot

FCA announces 3rd GI value measures pilot

Gi Pricing practices Market study MS18/1

Pricing Practices in Retail GI – Household TR18/4

Value in the distribution chain

Call for Input on Access to Insurance FS18/7

Citizens Advice Super Complaint to CMA

Delegated authority: Outsourcing in the GI market TR15/7

Call for Inputs on Big Data in retail GI FS16/5

General insurance value measures FS16/1

Provision of Premium Finance to retail GI customers TR15/5

2014

2015

2016

2017

2018

2019
Latest FCA Publications – Key Highlights

- Ineffective and inadequate strategies, governance, control, and oversight of pricing practices.
- Inability to reliably assess and prove whether customers are treated fairly.
- Differential pricing: same risk and observable characteristics, but one group paying significantly higher prices than the other group.
- Risk of discriminating against consumers through use of rating factors in pricing based (directly or indirectly) on data.

What does fairness mean?

- Not that easy to define
  - Fairness in process: are contract terms fair and is the representation of product true?
  - Fairness for consumers or firms?
  - Treatment of vulnerable groups – insurance or policy making?
  - Customer disengagement
Loyal vs New Customers – household insurance

- Higher margins from loyal customers help subsidise the low margins from new customers.
- What level of differential is acceptable?

Source: General Insurance Pricing Practices: Terms of Reference MS16/1.1

How is the industry responding?

- AvivaPlus: renewal price guaranteed on monthly scheme
- Piloting different initiatives and testing propositions
- 3 year price promise
- Cashback rewards at retailers to offset renewal premium
- Closely monitoring the outcome of the study

Institute and Faculty of Actuaries
Considerations

- Extent of pricing transparency
- Responsibilities of customers to find the best price
- Quality and adequacy of the cover
- Are products too complex?
- New data
- New technologies
- Leading to new products?

Is capping prices an option?
- May have unintended consequences
- What level of difference between New Business and renewal prices is acceptable?

What could firms consider now?
- Have you got your governance sorted?
- Is MI appropriate and well understood by stakeholders?
- Think about vulnerable customers

IFoA response background

- IFoA response to consultations – the Public Interest approach
- Key messages:
  - Concept of cross subsidy in a group of policyholders is fundamental to insurance
  - Uniform price for all → highly individualised price
  - Societal benefits of insurance noting affordability impacts take up
  - Time poor vs cash poor but vulnerable customers/access to best deals/level risk aversion
  - New vs Renewal – different risk & spread cost of acquisition
  - FCA has 3 objectives (securing protection for consumers, protect/enhance integrity of financial systems, promoting effective competition)
IFoA response to proposed remedies

• Degree of pessimism on demand-side
  – Support greater transparency: price, freedom to move provider, discounts;

• Concerns on supply-side:
  – Relative price cap or no price discrimination — directly addresses issue but leads to higher
    new business prices for all (inc. cash poor and vulnerable); reduces competition (?); what
    is fair differential / cap?
  – Removing auto renewals leading to uninsured (drivers, home owners, travellers etc.)
  – Breaking up packages leads to less coverage
  – Simplifying tariffs doesn’t stop the price differentiation issue

• Other remedy of addressing through improved culture and
  transparency at firm

ABI activity

• 2016 – Code of Good Practice to help vulnerable customers at renewal
• 2018 – ABI and BIBA Guiding Principles:
  1. do not support excessive differences between new customer premiums and subsequent renewal premiums that unfairly
     penalise long-standing customers.
  2. will take action so that customers' tendency to shop around at renewal is not used to lead to excessive pricing differences
     that unfairly penalise long-standing customers.
  3. The ethos and approach to better outcomes for long-standing customers will be given Board or senior management
     priority and formally incorporated into firms' procedures for determining the premium at renewal.
  4. review their pricing approach for customers who have been with them longer than five years and assess whether this approach delivers a fair outcome.
  5. publish a report in no more than two years' time that demonstrates how members have sought to tackle excessive
     differences between new customer premiums and subsequent renewal premiums that unfairly penalise long-standing customers.
Wider regulatory context

• Is the FCA a regulator of price?
  – April 2017: requirement to show current and new premiums on renewal documents
  – 10th April 2019: thematic review (TR19/02) of the GI distribution chain, proposed guidance for manufacturers and distributors (GC19/2) and a Dear CEO letter
  – 3rd year of value measures; consulting (CP19/8) to extend to further products
  – Insurance Distribution Directive: duty to act in customers’ best interests; no longer implementing a “Duty of Care”; stating that “IDD is a game changer”
  – 7th June 2019 FCA announced reforms to fix dysfunctional overdraft market
  – 12th June 2019 FCA bans back dated interest on Buy Now Pay Later loans

• What will interim report in the summer say?