FINANCIAL CONDUCT AUTHORITY

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Dear CEO,

Insurance Market Priorities 2023-2025

We want to update you on the FCA's priorities for the Insurance market 2023-2025, the specific risks of harm we are most concerned about, what we want firms to do about them and where we intend to focus the majority of our work in this area.

The insurance market is essential to the UK economy, providing a vital service for millions of consumers and businesses. The market has 3 key sectors: personal and commercial lines insurance, wholesale insurance and life insurance. The wide variety of products and services within it includes personal and commercial lines products such as home and motor insurance that provide financial protection, wholesale products and services that price and underwrite risks from around the world and life insurance products that provide income to millions of customers before and at retirement, as well as long-term protection products.

In personal and commercial lines markets, our 2022 FCA Financial Lives survey shows 84% of adults surveyed hold an insurance product with over two-thirds (68%) of them reporting they always or usually shop around for these products. The wholesale insurance market is a fundamental enabler to the UK and global economy allowing risks to be pooled and covered with around £55bn of Gross Written Premiums (GWP) written in 2021 alone. Life insurers manage circa £2.35trn of customer assets across c.90m policies (at end 2022). The health of the UK Insurance market remains significantly important to the UK economy.

As with all financial services, the insurance market has faced, and continues to face, significant challenges such as the aftereffects of COVID-19, supporting customers with cost of living pressures and adjusting to higher inflation and interest rates. Additionally, climate change, artificial intelligence, resourcing challenges and strains on profitability have the potential to materially increase the existing risks of harm about which we are concerned. Ensuring we have the right data to assess both current and emerging risks of harm is a key priority for us.

Our strategic objective under the Financial Services and Markets Act (FSMA) is to make financial services markets function well. A key aim for the UK insurance market is that it continues to be a successful industry that helps customers achieve their long-term financial goals and is there for consumers and companies when the worst happens. Where insurance works well, we see claims being met quickly and fairly at the time of the customer's greatest need.

However, when we take a closer look at specific areas, too often we find significant failings. For example, in the last year we have taken supervisory action against firms where we have seen:

- the continued sale of products not providing fair value
- paying away significant amounts of commission to third parties where it was not clear how those commission levels had been assessed as being consistent with fair value
- discriminatory pricing practices
- undervaluation of motor claims
- failure to implement general insurance pricing practices rules
- weak identification of vulnerable customers
- poor business interruption claims handling, and
- instances of very long waiting times/settlement delays.

As a regulator, we are required to comply with our statutory obligations, we do this by focusing our resources on ensuring firms achieve good outcomes for consumers, to meet their needs and to ensure the market is functioning well. We expect Boards to do the same and oversee firms and ensuring their objectives are in line with our priorities. While we generally see good intent from Boards, we are concerned that not enough action is being taken to ensure good outcomes. We therefore expect firms' Boards to ensure concrete, proactive action is taken throughout the firm and not to treat them as a compliance exercise or wait for us to force action.

Market-wide priorities

While the UK insurance market covers a broad and diverse range of firms, our focus is on 4 market-wide priorities, alongside sector-specific priorities under our strategic outcomes and commitments:

Setting & Testing Higher Standards

Putting consumers' needs first: Embedding the Consumer Duty

We have a strong focus on Consumer Duty implementation especially in the current tough macro-economic environment - for both consumers and firms. We expect firms to assess and address issues with Products & Services, Price & Value, Consumer Understanding and Consumer Support. We also expect firms to put the consumer at the centre of their business to ensure they are delivering good consumer outcomes - both for open products and services now and in readiness for the Duty applying to closed products and services from 31 July 2024. We set out our expectations on implementing the Consumer Duty for Personal & Commercial Lines Insurance and Life Insurance earlier this year. We will consider using our range of regulatory tools to assess the effectiveness of this implementation, which may include mystery shopping exercises across different sectors.

Strategy for positive change – our Environmental, Social & Governance priorities: Governance and Culture

Poor governance and culture in the Insurance market leads directly to poor outcomes for consumers, market participants and employees and these have been key root causes of recent major conduct failings.

Firms should be able to show how they are actively working towards having a diverse workforce at all levels in their organisation. This will help firms understand customers' diverse needs and make the market an attractive career proposition for future talent. We expect firms to assess and address their drivers of culture, considering leadership, purpose, governance and your approach to recruiting, managing and rewarding employees. We have seen encouraging market commitments in this area but remain disappointed on the general lack of progress within the market overall, especially in the wholesale market.

Minimising the impact of operational disruption: **Operational resilience and the increasing reliance on Third Parties**

Operational resilience is the ability of firms, financial market infrastructures and the financial sector as a whole to prevent, adapt and respond to, recover and learn from operational disruption. We have recently seen incidences of a lack of operational resilience within firms to the detriment of customers and the wider market. We are particularly concerned with the level of governance, oversight and contingency planning on outsourced services where, if a problem occurs, customers suffer harm because adequate controls and contingency plans are not in place.

Our Operational Resilience Policy (PS21/3) came into force on 31 March 2022. After that firms needed to as soon as reasonably practicable and no later than 3 years, show that they are able to remain within Impact Tolerance (ITol) in severe but plausible scenarios for their Important Business Services (IBSs). To meet this requirement, firms must have scenario tested their IBSs to identify any vulnerability in their operational resilience and acted on any findings before March 2025, when the 3-year transitional period ends.

It is good practice for firms to have credible plans in place to manage and recover from operational problems, take remedial action where necessary and notify the regulators promptly as appropriate. In particular, we draw attention to the risks of cyber-attacks and the need to ensure you have adequate controls in place where information is held by third parties.

Reducing and preventing serious harm

Improving oversight of Appointed Representatives

Many firms in the insurance market operate as principals with Appointed Representatives (ARs) to bring benefits such as supporting innovation as some firms use the model to trial new services and propositions, providing increased customer choice and driving competition by providing market access for smaller firms. However, we have seen a wide range of harms where firms operate with the AR model, as set out in our policy statement last year. Our strengthened rules which came into force on 8 December 2022, give principals more responsibility to ensure their ARs are fit and proper. We are using data and analytics to help us identify higher risk principals and taking appropriate action on outlier firms. We will be testing that firms are properly embedding the new rules across the AR regime and increasing and improving our engagement with principal firms and other stakeholders. We expect principal firms to ensure high standards both within their firm, and at their ARs. Principals need to take steps to ensure their ARs operate within those high standards and to take assertive action with those ARs that fall below the principal firm’s standards.

In addition to the Market-wide priorities, we will also be focused on wider regulatory priorities over the next 2 years. These include the Future Regulatory Framework and its impact on the Insurance market, our new secondary competitiveness objective – with a focus on the wholesale market - and climate change risks. On climate change risk, we encourage firms to be systematically informed about the climate change risk impact across their organisation and continually challenge inputs and outputs of the climate change models they use. We also encourage personal and commercial lines insurers to pay particular attention to the effect of climate change on pricing, access and affordability.

We will also be focused on the following areas in your sector.

Personal & Commercial Lines Insurance specific priorities

Setting & Testing Higher Standards

***Putting consumers' needs first:* Price and Value**

Value is a key issue in the insurance market. Firms must look at the relationship between the overall price paid by the customer and the quality of the service or benefit provided. Firms must comply with our rules around offering fair value and deliver good outcomes for their consumers under the Consumer Duty. These rules require firms to understand customer outcomes and the value of their products. This requires a cultural shift in the market, with manufacturers and distributors sharing data and collaborating to ensure that what parties charge for a product or service is reasonable compared to the overall benefits consumers can expect to receive. In our view, firms need to do better at clearly demonstrating how fair value is being delivered, including justifying their prices and commission levels.

We are concerned that when reviewing firms' Consumer Duty implementation plans, we continue to see weaknesses in MI, examples of insurers and intermediaries not sharing information, and distribution chains that are longer than necessary. We will act where we see that a failure to properly implement and embed the Duty is causing harm to customers.

We are particularly concerned that some distribution arrangements do not clearly demonstrate how fair value is being delivered, especially where an insurance product is sold alongside a 'primary product'. These primary products may be financial services – such as home insurance – or they may be non-financial products – such as cars, mobile phones or flights. As stated in our latest value measures data publication, across all value measures products, claims costs as a proportion of premium range from 4% for Guaranteed Asset Protection (GAP) Insurance (sold alongside a new vehicle) to 65% for motor insurance, with the median in that range at 35%. We have also seen what appears to be high commission levels where it was not clear how these have been assessed as being consistent with fair value. For example, we have seen higher levels of commission for products with a standard non-advised sale, where it was not clear how the commission levels had been assessed to support the delivery of fair value.

We have found very few instances of firms suspending or withdrawing a product due to the findings of their fair value assessment. We will continue to test firms' assessments of value and will intervene where fair value is not being provided to customers, or where a firm's processes are weak. As well as testing firms' assessment of value, we will use data to identify and tackle firms that sell products that appear to offer poor value.

Linked to this, we still see a range of practices on premium finance, where there is generally low credit risk when a policy can be cancelled due to non-payment. Firms need to consider premium finance as part of their fair value assessments and should be able to demonstrate how they have considered this additional cost, including the relationship between the total price and the quality.

We introduced the general insurance pricing rules with the clear purpose of ending the practice of price walking for home and motor insurance customers, where loyal customers would routinely be quoted higher premiums at renewal. We know this was a fundamental shift in approach for many firms. However, we are concerned that some firms appear to be earning, on average, higher margins from longer tenure customers. Where this is because of systematic discrimination we will act to stop these practices. We will continue to analyse firms' pricing data to identify where firms may be failing to meet our rules.

Firms are required to assure themselves that their pricing is not discriminatory in line with the Equality Act 2010. Firms must not use data in a way that leads to unlawful direct or indirect discrimination based on protected characteristics and we have acted where we have had concerns. Firms must have effective governance and controls, both to determine and monitor their pricing activities and to evaluate how their pricing decisions affect consumer outcomes. We will engage with firms to ensure they are confident their pricing is not discriminatory and that they monitor outcomes to identify where customers who share protected characteristics get worse outcomes than other customers.

Where firms fall short of our expectations, in line with our actions announced on the sale of GAP insurance, we will intervene to ensure our aims are met.

***Putting consumers' needs first:* Consumer Support**

Costs are increasing for both customers and firms. We expect firms to continue to support customers in financial difficulty and reflect on whether they need to do more. Our Financial Lives survey found that consumers who were female, in an ethnic minority group, younger, unemployed, working in the 'gig economy' and/or renters, were more likely to have low financial resilience. Premium increases can therefore have a disproportionate impact on these consumers.

Where firms are under financial pressure we expect that they continue to provide the appropriate level of support and service. We expect firms to consider how they can ensure operations and processes are as efficient whilst give customers the support and service that meets our expectations. With inflation and cost of living pressures remaining high, we will continue to closely monitor how firms are supporting their customers in line with our final guidance.

***Putting consumers' needs first:* Claims**

Firms should also make sure consumers have enough information to understand the implications of the different claims settlement options available to them, particularly consumers in vulnerable circumstances. With inflation and cost of living pressures remaining high, we will continue to closely monitor how firms are supporting their customers in line with our final guidance, particularly consumers in vulnerable circumstances.

A review we published in July found considerable variation between firms in the time they took to settle claims. Our 2022 Financial Lives Survey found that 1 in 12 claimants had problems, mainly with the process taking too long, or with poor service or communication from their provider, when making their most recent claim. The Financial Ombudsman Service's data for April to June 2023 shows that complaints relating to motor and buildings insurance have reached their highest level in five years, with a rise in claim delays contributing to the rise. We have also identified issues with motor total loss claims, where cars are judged total write-offs. In December 2022 we warned insurers about undervaluing cars and other insured items when settling claims. We are monitoring closely how firms are settling motor total loss claims and will continue to act where firms are proven not to be handling claims promptly and fairly. We expect to continue to focus on claims handling in firms, through multi-firm or thematic reviews, but also data-led interventions on individual firms.

***Putting consumers' needs first:* Access**

We continue to see examples of consumers facing barriers to easily accessing affordable or suitable insurance or being unable to buy insurance at all. Our Financial Lives Survey data shows that those who did not have any GI products in 2022 were more likely to have lower incomes and lower investible assets, making them more susceptible to harm should they suffer an uninsured event. The Consumer Duty requires firms to consider outcomes for different groups of customers. We expect firms to be able to identify and address when particular groups of customers, such as those with characteristics of vulnerability or who share specific protected characteristics, receive systematically poorer outcomes. Firms should ensure that product design appropriately considers outcomes for different groups so that consumers have access to products that provide suitable coverage at a fair price.

We know that access to insurance is a particular issue for consumers with more serious pre-existing medical conditions. In 2021 we introduced new requirements to help consumers with these conditions better navigate the travel insurance market. Firms that sell travel insurance must, in some circumstances, signpost consumers to a directory of specialist firms that provide this type of insurance. We are carrying out an evaluation of these rules.

We have also identified that insurance costs have increased substantially for leasehold property owners and have proposed rule changes which ensure that; the interests of leaseholders are properly considered when firms design their products, prices represent fair value to leaseholders as well as freeholders, and leaseholders have enough information to challenge poor practices and unfair costs. We expect firms to consider how these principles apply to other products where there may be issues around access or fair value.

Putting consumers' needs first: **Sales Practices**

Firms must ensure that marketing and sales practices do not cause poor customer outcomes. Some insurance products, such as 'essentials' home and motor policies, offer lower levels of cover. We are concerned some customers may not understand that the coverage under these policies is less than they may be used to. Under the Consumer Duty firms should 'put themselves in their customers' shoes' when considering whether communications are appropriate.

Firms must ensure that any product they propose to the customer is consistent with their demands and needs and that customers must be provided with appropriate information about the product so they can make informed decisions. Our guidance on the Consumer Duty makes clear that material conditions or limitations for policies should be clear to the target market and, where appropriate, firms should test consumer understanding.

Strategy for positive change – our Environmental, Social & Governance priorities: **Governance, culture, and non-financial misconduct**

All insurance firms should reflect on their culture to ensure an inclusive culture where employees have the appropriate channels and feel psychologically safe to be able to speak up and raise concerns without fear. This is especially important where tolerance of such behaviours can create or indicate unsafe or unhealthy cultures. Areas for improvement include improving diversity, equity and inclusion (DEI) at all levels and in preventing and handling non-financial misconduct, including discrimination, harassment, victimisation and bullying.

We are ready to use our full range of regulatory tools, including enforcement action, against firms and individuals where we see instances of non-financial misconduct. We will work to support and improve standards of behaviour in firms and hold senior managers to account for their firm's cultures.

Culture is still a key area of focus in the way we supervise firms. We expect firms to be ready to show us how they are making progress in this area.

Action for firms

You are responsible for ensuring that your firm meets our requirements, including the obligations and expectations set out above. You should take all necessary action to ensure these are met and that you are prepared for the additional requirements that the Consumer Duty brings to these priority areas. We will use the Senior Managers & Certification Regime to engage directly with accountable individuals on areas of concern.

A significant part of our activity over the next 2 years will be to test firms against our priorities and expectations. We will also continue to use data to identify outliers and, where firms are not meeting our rules and expectations, we will take action.

If you have any questions, please contact your supervisory contact or call us on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with us. Our website has further details of how you can contact us.

However, we know there may be occasions when your firm faces urgent issues of strategic importance. In such significant circumstance, please contact the Head of Department responsible for the Personal & Commercial Lines Portfolios, Lisa Sturley, at Lisa.sturley@fca.org.uk.

Yours sincerely

Matt Brewis
Director of Insurance
Supervision, Policy & Competition – Consumers & Competition