Financial Conduct Authority

Regulator Assessment: Qualifying Regulatory Provisions

Title of proposal: Finalised Guidance: FG16/8 Fair treatment of long-standing customers in the life insurance sector and Thematic Review TR16/2 Fair treatment of long-standing customers in the life insurance sector

Lead regulator: FCA

Date of assessment: 6 March 2017

Commencement date: 9 December 2016

Origin: Domestic

Does this include implementation of a Cutting Red Tape review? N/A

Which areas of the UK will be affected? The rules apply to firms in the life insurance sector in all areas of the UK

Brief outline of proposed new or amended regulatory activity

• The Finalised Non-Handbook Guidance FG 16/8 (the guidance) arose from a thematic review carried out in 2014 and 2015, which identified widespread practices which the FCA considered created an increased risk of unfair treatment of long-standing customers (which were defined for the purposes of the guidance as being generally customers with products sold before 2000 and which are closed to new business).

• On 3 March 2016 we published a thematic report, TR16/2, setting out the findings from this thematic review. We found a mixed picture with most firms demonstrating good practice in one or more areas and poor practice in other areas.

• We also proposed non-Handbook guidance to improve firms' behaviour in order to drive better outcomes for customers. This provided detailed information on the actions they should take in order to treat closed-book customers fairly. We want to ensure that closed-book customers, who have life insurance products that are closed to new business, do not receive less attention than customers who have recently taken out a new product.

• The finalised guidance was published on 9 December 2016.

• The guidance aims to help firms reduce the future risk of unfair treatment of long-standing customers by setting out in more detail FCA expectations in respect of: 1) how long-standing customers are treated within a firm's strategy and governance; 2) communications to long-standing customers; 3) management of fund performance and policy values; and 4) the ability of customers to move from products that are no longer meeting their needs.

• Prior to the publication of the guidance the FCA had not set out in one place its expectations in respect of how firms should treat their long-standing customers.

• Whilst guidance, rules and principles did exist regarding firms' obligations in this respect, they were to be found in various places and were not specific to long-standing customers.

• As a result of the guidance, firms should be much clearer regarding the FCA's expectations and the actions they should take to ensure compliance with the relevant guidance, rules and principles.

Which type of business will be affected? How many are estimated to be affected?

The guidance applies mainly to firms in the life insurance sector. We estimate that approximately 40 firms or groups will be affected by the guidance. We estimate that there are about 70 small friendly societies that are not included in this number. The FCA does not routinely collect sufficient information to enable us to determine how many of these smaller friendly societies will be affected by the guidance.

Price base year	**Implementation date**	**Duration of policy (years)**	**Business Net Present Value**	**Net cost to business (EANDCB)**	**BIT score**
2016	9 December 2016	10	13.9	1.5	7.5

The BIT score is the net cost to business for five years.

Please set out the impact to business clearly with a breakdown of costs and benefits

Regulatory uncertainty

Prior to the publication of the guidance the FCA had not set out in one place its expectations in respect of how firms should treat their longstanding customers. Whilst guidance, rules and principles did exist regarding firms' obligations in this respect, they were to be found in various places and were often incorporated within wider guidance pertaining to customers in general. This included, among other things, FCA Principles 6 & 7 and the Non-Handbook Guidance Responsibilities of Product Providers and Distributors (RPPD). The publication of the guidance will add value by providing firms with a clear and integrated source of information covering the FCA's expectations in this area. Consequently, firms should be much clearer regarding the FCA's expectations and the actions they should take to ensure compliance with the relevant guidance, rules and principles.

Basis for calculation of the BIT score
As stated in the Thematic Review (see TR 16/2), we were not required to perform a CBA under s. 138I FSMA because we did not make any new rules. However, we acknowledged that, for some firms, it was likely that our guidance would result in significant additional costs relative to their existing processes. Therefore, in TR 16/2, we provided a brief analysis of the costs and benefits arising from our guidance.

In the CBA, published in the Thematic Review (see TR 16/2), we stated that '[we] consider that the expectations set out in this document are reasonably predictable from existing FCA rules and Principles'. We reiterated this message in the finalised guidance and accompanying feedback statement (FG16/8). Costs resulting from firms improving processes and practices in order to come into compliance with existing standards are not attributable to the guidance and are not reportable towards the BIT.

In addition to the guidance consultation, TR16/2 also contained project findings and good and poor practice tables. The finalised guidance said: 'Firms are recommended to review the findings, as well as the good and poor practice tables in TR16/2, in conjunction with the guidance and the feedback statement to inform this process.'

In many circumstances firms' adoption of approaches referred to as 'good practice' is likely to be necessary for them to comply with FCA requirements. However, there are also likely to be circumstances when firms will adopt 'good practice' in a way that exceeds the minimum standard required by FCA regulations. **We have calculated the BIT score solely from**

costs arising from these actions; for avoidance of doubt, we have not included costs incurred by firms in coming into compliance with the required standards.

Explanation of the basis for the cost estimates
During the project we visited and provided feedback to 11 firms. For the purpose of the impact assessment analysis we issued an information request to the 11 firms asking them to provide estimates of the costs of the actions they have taken, or plan to take, in response to the guidance. We used this information to calculate total expected additional costs for the 11 firms in the sample.

The project work and guidance was split between four overall outcomes. We asked firms to split their cost estimates in the same way. For outcomes where we considered a firm's existing practices at the time of the review substantively met FCA requirements we have taken the view that the additional costs relate mainly to 'good practice' that goes beyond meeting our existing standards. As described above, we have included such costs in our estimate as being additional costs resulting from the findings and good and poor practice tables in the thematic review.

For outcomes where we considered that a firm's practices at the time of the review fell significantly short of FCA standards we have taken the view that the costs estimated by firms relate mainly to remediation action to put right non-compliance with existing standards. We have not included such costs in our estimate as we do not consider that these costs result from the guidance.

We then made an estimate of the 11 firms' share of the overall market. We based this on the numbers of these firms' in-force policies for products which were within the scope of the Guidance (and therefore likely to be affected by it). The information was taken from the Annual Insurance Return for 2015, which was the most recent available data. We undertook our analysis of the data in conjunction with the LIFA Sector team.

These calculations indicated that the 11 firms that had provided cost estimates currently represent approximately 64% of the market likely to be affected by the guidance, based on in-force and in-scope policy numbers. We used this estimate to calculate the approximate additional cost to the market as a whole (resulting from the findings and good and poor practice) by extrapolating from the 64%. The methodology we used was checked by the Actuarial and Specialists team within the P&RI dept.

We estimate the net present value of costs to the industry as a whole over the next ten years to be approximately £13.9 million.

Responses from firms indicate that they expect the work to be carried out partly by their own staff, partly by external consultants and partly by outsourced service partners.

Analysis of Costs

Outcome	Description	One off cost £m	Annual Cost £m
1	The firm's strategy and governance framework results in the fair treatment of closed-book customers	0.1	0.1
2	The firm's closed-book customers receive clear and timely communications about policy features at regular intervals and at key points in the product lifecycle that enable them to make informed decisions.	0.0	0.0
3	The firm gives adequate consideration to and takes proper account of fund performance and policy values in a way that	5.2	0.4

	ensures it treats its closed-book customers fairly and proportionately.		
4	The firm's closed-book customers are able to move from products which are no longer meeting their needs in a fair and reasonable manner.	3.7	0.1

The costs in this table are not discounted. For this reason they are not directly comparable with the amounts shown in the 'Summary of Costs and Benefits' above.

The above numbers do not include small friendly societies. We estimate, based on the value of technical provisions that small friendly societies make up less than half of one percent of the sector.

The largest areas of expected increased costs are Outcomes 3 and 4. The information request did not ask for systematic analysis of costs within each outcome. For this reason we are not able to provide analysis of costs within each outcome.

Cost savings

Firms did not indicate any cost savings in their responses.

Impact on business confidence/ perceptions

Based on press coverage and discussions with firms we do not believe publication of the guidance had a significant effect on either business confidence or consumer perceptions. We expect that firms' actions in response to the guidance will improve customer outcomes and provide customers with more information about how their products are performing.

In the long-run we anticipate that this is likely to increase consumer confidence in product providers. If consumer confidence does improve, this may be beneficial to firms as a result of increased future sales and improved customer retention.

Impacts on different sizes of business (particularly smaller businesses)
The life insurance sector is dominated by a small number of large firms. Estimates submitted by firms indicate that larger and more complex firms are likely to incur higher absolute costs. Even the smaller firms affected by the guidance are relatively sophisticated.

Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.

Fair treatment of long-standing customers in the life insurance sector: FG16/8 - https://www.fca.org.uk/publications/finalised-guidance/fair-treatment-long-standing-customers-life-insurance-sector

TR16/2: Fair treatment of long-standing customers in the life insurance sector https://www.fca.org.uk/publications/thematic-reviews/tr16-2-fair-treatment-long-standing-customers-life-insurance-sector