



Out of Sight, Out of Mind

Are life insurers treating customers in closed books fairly?

Fair Treatment of Long-standing Customers in the Life Insurance Industry

What are the issues?

The FCA has recently issued thematic paper TR16/2 (Fair treatment of long-standing customers in the life insurance sector) on its review of the way in which the life insurance industry treats its closed book customers, i.e. those customers with life insurance products that are no longer open to new business, compared to customers who had recently taken out a new product. The FCA's review focused on how customers are being treated now and sought to address four key outcomes, which, in summary, are:

1. Does the firm's strategy and governance framework result in fair treatment;
2. Do closed-book customers receive clear and timely communications about policy features;
3. Is adequate consideration given to fund performance and policy values; and
4. Can customers move from products that no longer meet their needs fairly and reasonably.

The results are disappointing, showing that, although most firms were able to demonstrate good practices and behaviours in many of the areas addressed, a significant proportion of the firms reviewed did not treat all of their customers fairly. The main concern was over exit or paid up charges. Specifically, where such charges were levied, the charges were not communicated effectively to the affected customers at the appropriate time, i.e. at the time that they were incurred such as when the policy was made paid up or exited.

Firms are required to treat customers fairly by high level obligations such as the FCA's Principles for Business and by the detailed guidance in regulatory guide "The Responsibilities of Providers and Distributors for the Fair Treatment of Customers" ('RPPD'). The RPPD says that, inter alia, "providers... should consider the impact of their action (or inaction) on the customer in various stages of the product life-cycle, or the various stages of provision of the service".

Firms that did not have customers at the heart of their business tended towards over-reliance on compliance with contractual terms to secure fair outcomes without considering other actions to secure those outcomes. The FCA concluded that:

- Generally boards and senior management do not have a grasp of closed-book customers and outcomes and they may rely on management information that is not giving them a rounded and comprehensive picture. (Outcome 1)
- Most firms in the review are not giving closed-book customers important information at the time of key events with some relying on point-of-sale disclosure/policy T&Cs, which were often provided to the customer many years earlier. (Outcome 2)
- Generally, firms are identifying and taking appropriate action where poorly performing funds result in poor returns for closed-book customers. However, a minority of firms have insufficient processes for identification or lack a uniform application of good processes. (Outcome 3)
- Where firms levied exit and paid-up charges, a minority of customers are incurring relatively high charges for making their policies paid-up or exiting the investment, potentially resulting in unfair outcomes. This mostly affects personal pension customers. (Outcome 4)

What is the FCA doing?

The weaknesses identified have resulted in six of the eleven firms that were part of the review being referred to the FCA's Enforcement division. In the main action is being taken as a result of behaviour relating to the disclosure of exit and paid-up charges, although two of the six are being referred for other matters.

Improving future behaviour

The FCA will consult on non-Handbook guidance to provide firms with extra detail on the actions they should be taking in order to treat their closed-book customers fairly in the future. This will include an industry-wide discussion with a view to reaching a voluntary solution to capping or removing exit/paid-up charges. This will be in addition to the proposed new duty to make rules to cap exit charges on customers accessing their pension savings following the Government's pension reforms.

Addressing historical weaknesses

Depending on the outcome of the FCA's enforcement investigations into the six firms, the FCA may extend this thematic work to a wider population of firms, including any of the firms in the thematic review and/or other firms in the life insurance sector in order to determine if the problems identified have a wider reach.

What should firms be doing?

Firms in this and other sectors where there are closed books of business should review how they determine if they are treating closed book customers fairly. Work is likely to be needed to assess how the needs of closed book customers varies from customers who have taken out new products more recently, whether MI used in the evaluation process is valid and truly reflects customer treatment and, where there are barriers to customers moving from closed book products, whether customers have sufficient and timely information to enable them to make an informed decision. Where firms identify poor outcomes, they must take steps to ensure that they treat their customers fairly.

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