General insurance pricing practices

Citizens Advice response to the FCA's interim report

Dear colleague,

We are pleased to respond to the FCA's interim report on 'General insurance pricing practices.' Citizens Advice provides free, independent and impartial advice to anyone who needs it. In 2018-19, our staff and volunteers provided advice to consumers needing help with more than 16,000 problems with mortgages, savings, retail banking and insurance.

We have long been concerned about unfair pricing practices across consumer markets, particularly as people who come to Citizens Advice can often be the hardest hit by unfair pricing practices. In September 2018, Citizens Advice made a super-complaint to the Competition and Markets Authority about the excessive prices charged to dis-engaged consumers in 5 markets[1]. This complaint detailed the evidence we collected on the loyalty penalty faced by consumers. We estimated that across 5 markets, 8 out of 10 households pay a loyalty penalty, equating to £4.1bn annually. The CMA found this to be a plausible estimate of the loyalty penalty and urged regulators to take remedial action.

We welcome the FCA's study of general insurance pricing practices, and the opportunity to comment on the analysis and the proposed remedies. Given the scale of the problem identified and its impact on vulnerable customers, it's crucial that the remedies the FCA introduces do not fall short. Our response is structured as follows:

- The need to act to protect consumers in the insurance market - particularly vulnerable consumers
- Assessing remedies and their suitability
- The principles and outcomes that remedies should lead to
- Applying this framework to the FCA's proposed remedies
- Concluding remarks.

[1] Excessive prices for disengaged consumers A super-complaint to the Competition and Markets Authority. Citizens Advice 2018 (Unless otherwise stated, all evidence in this response is taken from this Citizens Advice report).

1. The need to protect consumers in the insurance market

Concerns about the pricing practices of the insurance market have been expressed for a number of years. The market is opaque, and much of the evidence to date has been based on survey data and case studies. Citizens Advice's super-complaint identified a £709 million loyalty penalty in the home insurance market. Previous research conducted by the FCA and the National Audit Office (NAO) has found that engagement in essential markets is particularly difficult for those in a vulnerable or insecure state due to the complexity of tariffs and information.[2]

The FCA's market study builds on the existing evidence base. It uses data from insurance providers, and finds conclusive evidence that pricing practices in the motor and home insurance market are unfair and that the markets are not working well for consumers. The FCA found the extent and level of detriment was higher than our super-complaint. It found £750m of detriment in the home insurance market alone.

In particular to vulnerable customers, the FCA found:

- Lower-income consumers pay higher margins for combined buildings and contents insurance;
- Loyal consumers pay higher margins than new customers. Our analysis shows that vulnerable consumers are more likely to be loyal consumers;
- Consumers who are less comfortable buying financial products online, or have low levels of knowledge, are more likely to pay higher margins. These are characteristics of vulnerable consumers.

It's crucial that the remedies the FCA introduces in the New Year go far enough to fix this harm and stop vulnerable customers from being ripped off for their insurance.

Applying the FCA's framework for assessing fairness to the insurance market

The pricing practices of home and motor insurers create unfair outcome for many consumers. We've applied the FCA's fairness framework to the findings of the interim market study. It leads to an obvious conclusion - pricing practices are unfair, of great concern and regulatory action is needed.

- **Who is harmed by price discimination?** Many of those paying high prices are loyal customers who have remained with the same provider for a number of years. For example, 25% of home insurance policies had been held for 7 years or more with an average profit margin of 35%; by contrast insurers make a loss of around 40% on policies sold to new customers.

  However, the FCA's latest analysis shows that it is not just loyal consumers who are discriminated against, but also some consumers who switch provider.

[2] NAO, Vulnerable consumers in regulated industries, March 2017; FCA, Consumer Vulnerability, February 2015.

Overall, 6 million policyholders paid higher prices in 2018; 2 million of these consumers exhibited at least one characteristic of vulnerability.

Vulnerable consumers are less likely to be aware of the pricing practices than other consumers. Making pricing practices more transparent will not necessarily help vulnerable consumers. Their vulnerability means that they are less likely to be able to take action to mitigate the pricing practices, and even if they did, they may still face higher prices. For example, the FCA's analysis shows that not all consumers who switch get a good deal. It shows that lower income consumers (incomes of less than £30,000 pa) pay higher profit margins than higher income consumers for combined buildings and contents insurance.

- **How much are these individuals harmed?** Those harmed pay significantly higher premiums in the form of much higher profit margins. The FCA estimates that £1.2bn was overpaid in 2018. Our analysis showed that insurers make all their profits from loyal consumers and over half of their profits from vulnerable and potentially vulnerable consumers.[3]

  In the same analysis we showed that a new customer might pay £172 for home insurance whereas a loyal consumer, renewing their policy for the 5th time, will pay £325 for the same cover.

  There is also the impact on consumer trust and confidence in the market. Consumers trust their provider to treat them fairly: research we carried out for our super-complaint showed that 90% of consumers think that providers should inform existing customers when they are eligible for a better deal. The reality is that few do this.

- **How significant is the pool of people harmed?** Those harmed are a significant proportion of the market - the FCA estimates that in 2018, 6 million policyholders paid high prices. This is over 13% of policies written in 2018. It is likely to be an under-estimate of the numbers affected by the unfair pricing practices as consumers may be overpaying in other ways too.

  Home/motor insurers make 84%/96% of their profits from payments made by consumers for "non-core" services respectively. These include the sale of add-ons or excessive charges for monthly payments (and weren't fully covered by this market study). In addition, the lack of transparency may mean that consumers are unknowingly having inadequate or inappropriate levels of cover. Some consumers are unknowingly paying for cover, or levels of cover, that they don't need, others may think they have cover when in fact they don't.

- **How are firms price discriminating?** Pricing practices are not transparent. Consumers are unaware that they are facing price discrimination, and even if

[3] Home insurance companies make 100% of their profits from the loyalty penalty. Citizens Advice Press Release. April 2019

they are aware, there is little they can do. Many of those paying high prices are unlikely to understand insurance or to be able to search for better prices and products that match their needs.

Those that can and do search are still penalised as prices are based on consumer characteristics. The complexity of products and prices makes it hard for consumers to get the best deal: our research showed that 36% of households paying a loyalty penalty in the home insurance market thought they were on the best deal. This complexity also makes it difficult for consumers, especially vulnerable consumers, to get the insurance that best meets their needs. Consumers may have inappropriate or inadequate levels of insurance cover.

- **Is the product/service essential?** Yes. Motor insurance is a legal requirement; mortgages often stipulate buildings insurance cover; contents insurance is a product that most consumers would regard as important and necessary.

- **Would society view the price discrimination as egregious/socially unfair?** Yes. The level and nature of price discrimination in insurance has long been considered unfair. The Competition and Markets Authority upheld our complaint and the FCA has been asked to remedy the problem.

The FCA's market study provides further evidence that pricing practices are unfair. Applying the FCA's framework for assessing the fairness of price discrimination shows that these pricing practices are of great concern. They affect many consumers who unknowingly pay high premiums. Many of these consumers are vulnerable or potentially vulnerable and are the consumers that should be protected - not exploited.

There is a pressing need for action to address the concerns, to make the markets work for consumers and to rebuild consumer trust and confidence. These concerns have been known for a while and are widely accepted. The industry has had ample time to make changes itself, but has not been able to. Swift regulatory intervention is needed. The only question now is what form this intervention should take.

2. Assessing remedies and their suitability

Remedies can be split into two broad groups - demand and supply side. Demand-side remedies are changes brought about by the regulator, are usually made by the supplier and are designed to help consumers make more informed decisions about the products on offer.

Typically, demand-side remedies address information asymmetries and make consumer search and switch activity cheaper and easier. This empowers active or engaged consumers and can make markets more competitive. It had been thought that by creating a significant proportion of active and engaged consumers, demand-side remedies could provide protection for all consumers. This thinking led to demand-side remedies that made it easier for active consumers to make informed choices, and to remedies that encouraged more consumers to become more active.

These measures have been effective up to a point. They have encouraged more consumers to be active and to shop around; and they have made it easier for active consumers to make informed choices. However, they have not directly benefited disengaged consumers, nor have they indirectly benefited them. We now know that the presence of active consumers is not always sufficient to protect inactive or disengaged consumers from exploitation. Technological advances have enabled firms to develop ever-more sophisticated pricing practices, gathering and using ever greater volumes of data about consumers and to discriminate more effectively between consumers.

In some markets, such as insurance, firms are now able to charge what are effectively personalised prices, based on their assessment of how much they can get consumers to pay. The FCA has tried demand-side remedies. Its own evaluation of disclosure remedies [4] shows that demand-side measures may deliver small improvements in consumer outcomes (£185m consumer savings, but consumers are still overpaying £2.1bn). It also shows that demand-side remedies alone will never be sufficient to guarantee that all consumers are protected from unfair pricing practices.

The FCA's market study confirms that vulnerable and disengaged consumers are negatively affected by unfair pricing practices used by insurers. While there may be further demand-side remedies which might make both markets work better for consumers (for example, by nudging more consumers to become active, or by making search and switch activity easier), demand-side remedies alone will never be sufficient to benefit or protect vulnerable disengaged consumers, or to restore consumer confidence in the markets[5]. Nor are demand-side remedies costless to implement.

A second set, or category of remedies are supply-side remedies. These are changes made by the supplier which can affect all consumers without consumers having to take any action. They can include price controls limiting the most that can be charged - a price cap (for example, the price caps in the energy market) - or the minimum that can be paid to consumers (for example, a basic savings rate). They can also limit the difference between the highest and lowest prices - for example, a relative price cap.

Supply-side remedies directly affect consumers and can be very effective at delivering better outcomes for consumers who might otherwise be unfairly treated - especially vulnerable and disengaged consumers. Not all consumers will necessarily gain from supply-side remedies. Just as unfair pricing practices create winners and losers, remedies to correct them may also create winners and losers. Used properly though, supply-side remedies should result in a net gain for consumers. The benefit of the supply-side remedy should be judged both by the net effect on consumers and also by

[4] Evaluation of Disclosure Remedies, 2019, FCA
[5] Section 4 of Citizens Advice;s super-complaint includes a summary of the effectiveness of demand-side remedies that have been tried to date.

the distributional impact. Which consumers gain can be as important as the value of the net gain.

The effectiveness of supply-side remedies depends in large part on the response of firms. These responses are difficult to predict and this, coupled with a belief that demand-side remedies can be sufficiently effective, has meant that regulators have tended to shy away from supply-side remedies. However, we now know that demand-side remedies cannot be relied on to protect vulnerable consumers.

Supply-side remedies have to be considered. To help inform and further debate on the effectiveness of supply-side remedies, Citizens Advice has commissioned a piece of research on supply-side remedies. This work will summarise the literature and evidence on supply-side remedies and will identify the factors that affect the effectiveness of these remedies. We hope to publish this research in December 2019.

Arguments in favour of supply-side remedies

Supply-side remedies can produce winners and losers. It is usually impossible to frame a remedy that improves the poor outcomes of some consumers, without also negatively changing the outcomes of other consumers. This argument is often made to justify why supply-side remedies should not be considered.

The unfair pricing practices in the insurance market already create winners and losers. Those that can engage with the market - typically, richer, more educated consumers - benefit at the expense of those who cannot engage with the market - vulnerable consumers (eg older, poorer consumers with health conditions). This isn't an equitable outcome and not necessarily a benchmark against which to assess whether a remedy will deliver a fairer outcome. For example, Amelia Fletcher wrote[6] *"... remedies can have winners and losers. This should not necessarily deter regulators from intervention. If canny consumers have effectively been benefiting, through lower prices, from the less sophisticated behaviour of others, who pay high prices, then intervention to address this issue may not be considered to raise significant distributional concerns."* [7]

A second argument often levelled at supply-side remedies is that they may distort the market and ultimately deliver worse outcomes for consumers. This is a possibility if done badly, but should not be used as an excuse not to do anything. Regulators should use best available firm and consumer level data to model the likely effects of a remedy and should always commit to ex-post evaluation. We expect the FCA to maintain its oversight of the insurance markets and to commit to monitor, evaluate and review the effectiveness of remedies and make changes as necessary.

Typically when considering the case for and against a possible intervention we consider the worst case. This is a perfectly sensible approach, but needs to be balanced with the likelihood of it being realised. For example, it has been argued that price interventions

[6] about demand-side remedies, but which equally applies to supply-side remedies
[7] The role of demand-side remedies in driving effective competition. A review for Which. 2016

are bad because they reduce the gains to consumers from search and switch activity and can discourage such behaviour. The argument is that this in turn reduces competitive pressures in the market and leads to worse outcomes for consumers. However, while possible, such an outcome is not inevitable. Price interventions never impose a single price.

Consumers that search or switch can still be rewarded through lower prices or with a product that better matches their needs. Early evidence on the default energy price cap has shown an increase in switching activity since it was introduced in January 2019. Furthermore, price controls can stimulate competition by changing the focus of competition away from solely on price and onto other elements such as the product offering or customer service. In turn, this can lead to new products and services which can benefit consumers. For example, by enabling them to find products that provide the most appropriate level of cover.

Some argue that price controls in insurance could lead to a reduction in the availability of low-cost insurance. This would affect consumers' access to insurance and deliver a worse outcome for them. Competitive markets will always provide products where there is demand and profit to be made. Further, the FCA's analysis shows that there is little evidence that current pricing practices are increasing access to insurance for consumers with low-income, and so the argument that price-controls might lead to a reduction in low-cost credit is weak. Similarly, FCA analysis points to demand for insurance being insensitive to price, suggesting that price controls are unlikely to affect capacity in the markets or the supply of insurance.

Another argument made against supply-side remedies is that they are a disproportionate response. In this case, some may argue that because the FCA did not find any evidence of excess profits, a ban on price walking or other price controls is disproportionate; instead the industry should be given time to improve its practices and police itself. However, concerns about pricing practices in the insurance industry are not new. The industry has had ample time to improve its practices and to take remedial action. It has not done so and it's clear that the incentives in the market are such that effective voluntary action will never be a realistic option - there is too much to be gained for individual firms by overcharging customers. It is now time for the regulator to take remedial action. Every year it doesn't, customers - including vulnerable customers - are losing £1.2 billion.

The FCA's analysis shows that there are a lot of costs in the insurance industry that are ultimately paid for by consumers. For example, £2.3bn is spent on customer acquisition - against £18bn of gross premiums. Only a proportion of consumers shop around or switch providers, thus a lot of money is spent trying to acquire a fraction of the 45m policies written. Added to this, active consumers face considerable search and switch costs (£38 and £42 a year for home and motor respectively). Both price comparison websites and websites have operating profits in excess of healthy levels. These costs should be included in any consideration of the costs and benefits of the market currently compared with a regulated outcome.

3. The principles and outcomes that remedies should lead to

The market study confirms that strong regulatory intervention is needed in both the home and motor insurance markets. Providers in both markets operate pricing practices that are unfair to consumers, that produce inequitable outcomes and which are not transparent. These pricing practices disadvantage one third of policy holders including vulnerable consumers, disengaged consumers and also some engaged consumers. The scale of the detriment is significant - £1.2bn was overpaid in 2018 as a consequence of these unfair pricing practices. The unfairness of pricing practices in this industry is widely known. The industry has had ample time to police itself and to change its practices. It hasn't done this and so firm regulatory intervention is necessary.

Demand-side remedies alone are insufficient to protect vulnerable and disengaged consumers. Further, they will not be sufficient to tackle the unfair pricing practices in this industry. The FCA has tried demand-side remedies. Its own evaluation shows that these have had limited effect and even after these measures consumers are still over-paying £1.2bn. Supply-side remedies will be needed, either on their own or as part of a package of remedies. Only supply-side remedies will ensure that vulnerable consumers are protected.

There are a number of supply-side remedies that could be adopted. It is unlikely that there is a perfect remedy. Each remedy will have advantages and disadvantages and ultimately an informed judgement will need to be made as to the remedy, or group of remedies, that best address the problems identified and which are likely to be most effective (factoring in firms' potential responses to them). In this section we summarise what we expect a remedy to deliver and the factors that should be considered when choosing between remedies.

Our primary concern is to ensure that all consumers are treated fairly, and that vulnerable consumers are protected from unfair practices. This will require firms to change their behaviour. As part of this we will look for remedies that:

- tackle and prevent price discrimination;
- put fair treatment of consumers central to the pricing decisions and services of the insurer;
- lead to fairer pricing for all consumers;
- enable customers who want to engage with the market to make informed decisions while protecting those that don't want to, or cannot, engage with the market;
- restore consumer trust in the market; and
- are implemented in a timely fashion, are supervised, enforced and evaluated.

Assessing remedies

Fair treatment of consumers through fair pricing

This will require a major shift in firms' behaviour. Pricing practices do not treat all consumers fairly and do not deliver fair or equitable outcomes. Fair treatment of consumers is not currently central to pricing practices. Firms set prices to optimise margins, rather than by reference to cost. This means that consumers with identical products and similar risk profiles can be charged very different prices.

It is not clear what information firms use to inform their margin optimisation pricing strategy, but it does seem that loyalty (or repeat custom) is one factor. Auto-renewal is linked to higher prices for home insurance (but not for motor insurance) and the FCA found that some firms use auto-renewal as a predictor of consumers' willingness to pay.

However, there will be other factors, or consumer characteristics, that the industry uses to identify which consumers it can try to over-charge. A pricing strategy that centred on treating all consumers fairly would mean an end to margin optimisation pricing strategy. It should also mean that firms only collect, use and share information about consumers that is essential to determine risk.

If insurers adopted pricing strategies that centred on treating all consumers fairly, then the most pernicious practices - eg price walking - will not continue. It would also mean that practices such as auto-renewal could only deliver benefits for consumers. And, vulnerable consumers will be protected.

Price transparency

Consumer-centric and fair pricing strategies might improve the transparency of prices, which in turn would help rebuild consumer trust and confidence. Pricing in the insurance market is opaque and difficult to understand. Consumers cannot know whether a premium is fair, as unlike in most markets, there is no reference or benchmark price against which to compare. Consumers can compare this year's premium against last year's and they can obtain quotes from different providers, but without a reference or benchmark price the consumer does not know whether the price is fair or not. This creates distrust. It may lead to higher levels of search activity and costs than is optimal and leads to unfair outcomes. Our primary objective is for remedies that improve outcomes for vulnerable consumers and deliver fairer pricing strategies. We would also welcome remedies that improve the transparency of pricing in the market and which give consumers confidence that they are being charged a fair price for cover that best matches their needs.

Protection for vulnerable consumers

Insurance is a complex product with lots of variants and product choice. This choice and variety can be good for consumers as it means there should be a product that best meets their individual needs. At the same time, it means that consumers need to spend time searching the options and in understanding the differences in products. Some consumers are unable or unwilling to do this and the analysis shows that firms exploit such consumers. Consumer-centric, fairer pricing practices will offer protection for all consumers. However, in the absence of absolute certainty that firms will change their behaviour and treat all consumers fairly, additional safeguards for vulnerable consumers are needed.

Timely remedies that are supervised, enforced and evaluated

Unfair pricing practices in the home and motor industry have led to many consumers paying significantly higher prices for many years. The FCA needs to take swift action to tackle this abuse, and also needs to commit to supervise and enforce the actions taken.

We acknowledge that there are a number of factors specific to these markets which mean that it will take time to deliver benefits to consumers. Insurance is usually sold as an annual policy; thus any benefits from changes to firms' behaviour and pricing practices will only be realised by consumers when they renew their policies, ie a lag of up to 12 months after changes are made.

Changes to firms' behaviour and pricing practices will also take time to be agreed and then implemented. This means that vulnerable consumers could be exploited for several more years. This is unacceptable. Remedies to protect vulnerable consumers need to be introduced without delay.

Any remedies that are introduced will need supervising and enforcing by the FCA. The FCA will need to monitor how firms implement remedies to ensure that the remedies are implemented as intended. This may require enforcement. Evaluation to determine what the effect was and why will also be crucial.

4. Applying this framework to the FCA's proposed remedies

We are encouraged to see that the FCA is actively considering supply-side remedies. Supply-side remedies will be essential in these markets and we welcome the opportunity to comment on those being considered by the FCA. We don't have a firm view on which supply-side remedy, or combination of remedies, would be most effective in delivering the outcomes we judge most important - fair pricing practices, price transparency, timeliness and protection for vulnerable consumers. Any one of the supply-side remedies would improve outcomes for consumers. The effectiveness of each remedy at delivering a net improvement in consumer outcomes or the outcomes of specific consumers - eg vulnerable consumers - will vary.

The choice as to which supply-side remedy to implement will depend in part on decisions on the relative importance of different outcomes. It will also depend on analysis of likely outcomes and firms' behaviour. The FCA has access to both firm and consumer level data and should be able to model the relative effectiveness of different remedies, assess the overall impact of the remedy and the impact on different groups of consumers. This is work that the FCA will need to do.

In the next section we discuss some of the potential outcomes from each remedy and what these might mean for consumers. Some of the outcomes depend in large part on the behaviour of firms. We are not in a position to judge the likelihood of each outcome - but the FCA with access to firm-level data will be able to model and predict the outcomes, and judge the relative effectiveness of the remedies.

Price-walking

A ban on price-walking could address the problem of the loyalty penalty - firms passing on higher premiums to loyal consumers. As many loyal consumers are also vulnerable consumers, this remedy could tackle some of the price discrimination faced by such consumers. However, the FCA's analysis shows that price-walking is part of a wider problem of unfair pricing in the home and motor insurance markets. This analysis shows that unfair pricing affects new consumers as well as loyal consumers. A ban, or restriction on price-walking by itself would not stop price discrimination against new consumers.

Assessing this remedy against the outcomes we judge important shows that this remedy would not be sufficient by itself. It would not necessarily make pricing practices fairer and would not prevent firms from charging different prices for the same product. Its effectiveness at protecting loyal and vulnerable consumers from price discrimination could not be guaranteed as it would depend on how firms react. Firms with a high proportion of loyal consumers may decide that their best strategy would be to stop competing aggressively for new consumers, raise their lowest/new customer prices and leave highest prices unchanged (although they would likely lose customers over time). This would make the remedy largely impotent. It could also reduce the availability of cheap insurance which could be damaging for consumers.

Conversely, a firm may decide to continue to compete for new customers and increase renewal premiums rapidly such that loyal consumers pay the maximum permitted differential sooner. The most loyal consumers might gain, whilst consumers renewing for the first or eg second time might pay more. It is unclear what the net effect would be. The FCA, with its access to data at firm and consumer level, should model the most likely outcomes and to provide an assessment on the effectiveness of this remedy.

Restricting factors used in pricing decisions

Restricting factors used in price setting probably comes closest in principle to achieving the outcomes we judge important - but may be more difficult in reality.

It would mean fairer prices and would put the fair treatment of consumers central to pricing decisions. Premiums could be set using only information that is directly pertinent to the pricing of insurance, and not using information on loyalty (or likely loyalty), or on any other consumer characteristics not pertinent to the pricing of insurance. This would tackle price discrimination. It would protect vulnerable consumers. Depending on how it was communicated to consumers it could improve the transparency of pricing, help reduce search costs and restore consumer trust and confidence.

Its effectiveness will be dependent on how it is implemented and what actions firms take to circumvent it or to reduce its effect. For example, there will be a choice to be made between a rules or principles based approach. The former may be easier to develop, implement and police as it will specify what information can or cannot be used in pricing decisions. But, it may not have longevity and would need regular review to ensure it remains effective as the market innovates. A principles based approach will have longevity. It will require greater regulatory oversight and policing and may be less agile in tackling breaches and protecting consumers.

So, while this measure could work very well in principle, the FCA should make a decision over whether they would be able to effectively police the behaviour of firms in a market where price setting is increasingly technical and complex. If the conclusion is that they can't, this would be a much less attractive remedy.

Pricing restrictions relative to a benchmark

Such a remedy is broadly similar to a price cap. Its effectiveness will depend on the benchmark price chosen and the price restrictions put in place. If set correctly, it could be beneficial for consumers.

Having a benchmark price could in itself improve price transparency, reduce the costs of search activity and could improve customer trust/confidence. It would need to be reviewed regularly in light of market responses and consumer outcomes. It may tackle the worst price discrimination but a benchmark price with or without pricing restrictions may not provide perfect protection for vulnerable consumers. Vulnerable consumers could be charged the maximum price possible - which may or may not be lower than their current prices.

Automatic switching

Automatic switching has been tested with some success in the energy market. Consumers on the worst deals are periodically moved to best deals. This has the effect of capping the number of years or price-walking, or exploitation, that a consumer could face. This could be an effective measure if firms both switched consumers to the best deals they had, while still incentivised to keep prices competitive to acquire new customers.

It is possible that some firms could maintain premium income by charging higher premiums for fewer years; they could withdraw cheaper equivalent products or increase the prices of these products. Consumers could see their premiums rise sharply and then fall.

Where firms switch consumers to a better deal automatically, this could also perpetuate the practice of unfair pricing. For example, firms could still make unfair pricing decisions to calculate someone's bill and mask this by switching them to a slightly cheaper - but still artificially high - tariff. It may be that reforms to pricing should sit alongside automatic switching to ensure unfair pricing practices are stamped out.

Helping consumers find better deals

An alternative to automatic switching could be to require firms to engage with consumers paying high prices to help them find better deals. The effectiveness of this as a remedy would depend on whether firms are able to engage the most disengaged consumers and change their behaviours. Many consumers are unable to engage with this market, and efforts to help and encourage them to engage have had limited effect to date (the FCA estimates that the renewal disclosure remedies have led to only a 1 percentage point increase in the proportion of consumers searching and switching). Assessed against the outcomes we judge important, this remedy also falls short. It would not directly change pricing practices or improve price transparency, nor will it protect vulnerable consumers. It may also be difficult to implement, police and enforce.

Remedies that discourage switching

The FCA's analysis found evidence of practices that make it difficult for consumers to make informed choices and switch. These practices should be stopped. They wouldn't exist if firms had fair pricing policies that were consumer centric. However, these remedies help only consumers who can and will act: they won't help the many vulnerable consumers who are unable to act and who firms take advantage of. These remedies alone are insufficient to tackle the problems identified, but they could form part of a package of measures that included supply-side reforms.

Remedies to improve transparency

The analysis shows that firms set prices to optimise their margins. This is unfair and is made worse because consumers are not told about it. So, remedies that reveal pricing practices should make things fairer for consumers. However, it will only lead to fairer outcomes for consumers who are able to act on the information and who search out and switch to better deals. It won't help consumers unable to engage with the market. It could make outcomes for these consumers worse. For example, if firms decide to pass on even higher price increases to compensate for lower premiums made from an increasing number of active consumers.

Longer-term reform

Longer-term innovation and technological advances may deliver benefits for consumers. However, we cannot bank on this, nor can consumers afford to wait. It is also likely that technical advances would work against the interests of consumers - eg allowing more sophisticated price discrimination that is harder for regulators to detect. This may mean that immediate and interim remedies are put in place whilst more sustainable remedies are developed. We would expect a clear time frame for any longer-term work.

5. Concluding remarks

We welcome the FCA's market study. The market study provides more evidence on the unfair pricing practices in the home and motor insurance. It and other evidence already published presents a compelling case for regulatory intervention. There have been concerns about fair pricing in the home and motor insurance markets for a number of years. The industry has done little to address these concerns: even in the period since the CMA upheld Citizens Advice's super-complaint the industry has taken little action to reform itself. This is in part because it is very difficult for individual firms to move against the incentives in the market without losing out, which shows relying on voluntary commitments won't resolve problems in the market. Strong regulatory intervention is needed. There is strong and compelling evidence that demand-side remedies are insufficient to provide protection for all consumers, and especially not vulnerable consumers. Supply-side reforms are essential to tackling the unfair pricing practices. Consumers paid £1.2bn in high premiums last year: action needs to be taken quickly to stop this.

Our primary concern is to make markets work better for vulnerable consumers. We would like to see firms change their behaviour and to centre pricing decisions on delivering fair outcomes for consumers. Some of the remedies proposed by the FCA could deliver this outcome and we would encourage the FCA to model and analyse these further. Our initial assessment is that a package of remedies is needed. This package would include remedies:

- to make pricing decisions fairer and more transparent. This means measures that restrict the factors used in pricing decisions to those that are directly relevant;
- that provide the best deals for vulnerable consumers. This could mean automatic switching to ensure that vulnerable consumers are put on the best deal quickly; and
- that address barriers to switching.

Detailed assessment may show that these remedies are insufficient to tackle the unfair pricing practices identified. It may also show that other packages of remedies could be more effective. We would welcome the opportunity to comment further on a package of remedies.