‘Earth shattering’ - The FCA’s big plans to shake up premium finance

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The proposed new rules could dramatically alter the income earned by insurance brokers

They say the devil is in the detail.

Buried deep in the FCA’s proposals for dual pricing are a couple of pages outlining fresh plans for premium financing.

It’s not a small matter.

Some believe the plans could have a devastating impact on the personal lines brokers who have gained from lucrative interest rates charged on policyholders.

‘It’s earth shattering’, saif Ravi Takhar, founder of premium finance firm Bexhil UK.

Ravi Takhar, Bexhill UK chief executive, says this report will have a big impact on brokers charging high interest

”The proposals, if finalised into rules, will dramatically reduce income earned by UK insurance brokers.”

So what are the rules and how could they impact brokers?

The biggest take away is the FCA’s plans to make brokers justify the mark up in commission from what they wholesale from the premium finance house to the final interest charged to the customer.

Furthermore, brokers will now have to report in data regularly, so the FCA can specifically monitor whether customers are treated fairly on interest charges.

Why is there such concern? Brokers typically receive rates as low as 4% to 5% from the premium finance provider.

But according to data from Consumer Intelligence taken from top brokers, the customer ends up being charged anywhere between 13% and 22%, depending on the broker.

Insurers charge a much lower rate, at between 8% and 13%, and even cheaper deals can be found if consumers look hard enough.

Takhar, a former Oxford University-educated banking lawyer, points to the killer line in the FCA's documents.

"…..where the firm proposes premium finance with a higher annual percentage rate (APR) than would be available elsewhere (for example, directly from the insurer, or from another finance provider), based on the remuneration the firm will receive, this may conflict with the firm's obligations including the customers' best interests rule."

Takhar said: "The FCA appears to be insisting on the broker offering the customer the net rate from their finance provider and not adding commission.

"This will be a devastating blow to many insurance brokers and in certain cases lead to the broker's business no longer being viable."

Takhar said another complication is that brokers will now have to understand other forms of consumer finance and the cost of finance, which is not their area of expertise.

Impact 'cataclysmic'

Consumer Intelligence chief executive Ian Hughes agrees that for some brokers, the impact is significant.

He said: "It will be varied across the industry. But for some people it is cataclysmic.

"It will be businesses that have come away from being insurance brokers and have become credit brokers, and using insurance as way to sell credit.

"If that has become their business model then this really puts a spanner in the works. Probably from a consumer's perspective it is the right thing."

However, Hughes said it could limit choice to certain customers, such as people on low incomes, if premium finance choices drop out the market.

Michael Sicsic is in a good position to understand the thinking of the regulator.

He was the former head of supervision for the UK general insurance retail sector, leaving 18 months ago to set up his own consultancy.

Sicsic said the FCA has taken this line on premium finance, and also some additional proposals around add-ons, to stop insurance firms potentially using these revenue streams to compensate for the potential loss of income from the dual pricing reforms.

With the added data reporting that brokers will have to feed into the FCA, he said the regulator has set the framework to monitor, and if necessary, intervene to ensure customers are treated fairly.

Sicsic said: ”The FCA is saying that transparency in itself is not sufficient, because it will nudge some people, but not everyone.

”So what they’re proposing is a package of measures. The first one is the ban on price increase, with transparency being a complement. And the other one they’re putting in the package is the data reporting.

”Every year they will ask providers quite a lot of detail to report to the regulator. In it, there are some details on premium finance where they will ask ‘what is the APR’ ‘what is the average cost’. So I think they want to control what is going on in the market.”

Good for customers

Premfina founder Bundeep Rangar said the FCA’s proposals are good for the customers.

“Transparency helps the market. This plays on the broker to have fair pricing for the customer. Any cost saving negotiated with premium a finance provider should be to the end benefit to the customer,” he said.

He also points out that lower rates could increase take up of premium finance.

“If it does not cost any more, it will drive the adoption of premium finance, because it does make it more affordable.”

So far, brokers have remained tight-lipped when contacted by *Insurance Times*.

One willing to comment, Eldon chairman Martyn Holman, was not overly-concerned by the report.

Martyn Holman: On the side of brokers in the premium finance debate

“My experience with premium finance is that it is transparent. It’s also competitive for the customer, you have to be to win the business.”

One source, who has worked closely with both premium finance houses and the major brokers, questioned whether the FCA would take such a hard line on brokers.

“I think there is an understanding that a lot of damage could be done to the business models of some of the big personal lines brokers if they come down too hard.

“In all the conversations that have been going on at the FCA, and between premium finance providers, I think they understand that.

“Personal lines brokers are good for the customer and we would not want to drive them out of business.”

Passnotes

Tell us in a nutshell what the plans are for premium financing?

The FCA proposes:

* Clear information about the cost of the premium finance, and that it makes the premium more expensive

* Customers must be asked more than just whether they want to pay monthly or annually

* Firms are not driven by remuneration to offer higher rates of interest than is offered elsewhere

* Increased data reporting into the regulator so it can monitor value

The regulator said, in its consultation report: “We will look closely at firms increasing the cost of premium finance to offset changes to the cost of the insurance product.

”Where the customer faces higher costs for the insurance product as a result of paying on credit, for example due to a higher premium compared to the cost if paying without credit, the additional cost may constitute a credit charge and, if so, the APR must reflect these costs.

”If it does not, firms may be in breach of the Consumer Credit Act 1974 and the associated regulations.”

What should brokers do next?

Firstly, brokers need to respond to the consultation. Secondly, brokers will need to prepare themselves to report in far more data to the FCA.

Eventually, brokers will have to justify the higher interest rates they charge to the customer, than what they wholesale from the premium finance provider.

Why is the FCA doing this?

The FCA is concerned insurance firms could compensate for losses on the changes in dual pricing by maximising revenue at the backend with add-ons and premium finance charges. The regulator wants to close off this avenue completely. It is placing a big emphasis on value as opposed to price.

The regulator has come under enormous pressure from the government and consumer groups to take action.

What's next the FCA's agenda?

Once this is sown, watch whether the regulator finally gets round to tackling property commissions.

There are similarities to the premium financing issue - namely, brokers charging extra commission at a questionable value to the customer who ends up paying.

The issue of unfair insurance charges on rent is likely to gather momentum as the government looks to protect hard-pressed tenants suffering economically from the Covid crisis.