New premium finance rules – what does it mean for the industry?

By Clare Ruel | 25 May 2021

Brokers are going 'to have to change the way they do business' around premium finance following the FCA's pricing reforms, says insurance premium finance chief executive

The FCA revealed its new rules for premium finance last month 28 May which includes guidelines for firm that use premium finance to allow customers to spread the cost of their insurance.

Due to come into effect on 1 October this year, the new rules in the FCA's *PS21/05* applies to all firms selling insurance products, not premium finance credit providers directly or premium finance arrangements without interest or additional cost to customers.

The rules do not require that insurance firms provide premium finance with 0% APR. Changes were proposed as part of the FCA's consultation on general insurance pricing practices, which closed in January.

The new guidance states:

- Premium finance sold alongside insurance provides fair value for customers and the costs associated with it will not detrimentally affect the value of the insurance produce.
- Any remuneration related to retail premium finance is consistent with the firm's obligation to act honestly, fairly and professionally in their customers best interests.
- They give clear information about the costs of the retail premium finance arrangements and make clear that this makes the contract more expensive.
- They do more than simply ask the customer to choose between paying monthly and annually to ensure customers actively choose to take premium finance.
- Firm's remuneration arrangements in relation to retail premium finance do not give an incentive to offer retail premium finance with greater costs to the customer where a better aligned arrangement with the customer's interest is available.

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Point of sale

Speaking about these changes, Ravi Takhar, insurance premium finance provider Bexhill's chief executive, told *Insurance Times*: "What the FCA does not like is insurance brokers charging high finance costs to people spreading the price of their insurance premium."

He predicts it might become like the point-of-sale market – 'buy now, pay later' – where you buy something and spread it over 10 or 12 months. Previously, for insurance, customers would probably have to pay between 10% to 20% for the right to spread the payments."

This he said could see the industry move to a payments system similar to the one used by Swedish fintech company Klarna, which allows customers to "buy now and pay later".

Takhar said the FCA would say this approach is fairer for the customer, but where does it leave the insurance industry? Likening this model to Klarna, Takhar said that if you buy shoes for example, using the fintech, the retailer would pay Klarna commission but the customer is offered 0% interest to spread the cost. "It's going to be the same for insurance – the insurer or broker is going to have to pay for spreading the payments to its customers," he added.

"This is really going to change the industry because historically insurance brokers have been used to earning huge income from interest on premium finance, so they are going to have to change the way they do business in that market."

"That is some security for the insurance policy – if the person stops paying, the insurance policy is cancelled, and the insurance company should make a payment back. It's safer for the borrower to take insurance finance," he added.

Checking customer finances

Takhar highlighted the savings that could result from such a move. He added that this would appeal to millennials.

Takhar said: "They are very wary of paying any interest, so it's right and a good development in the market."

Bexhill is offering brokers the option of using open banking to determine whether the customer can afford a policy, whether they spread payments or not. Takhar added there is a "real benefit" for brokers and insurers in knowing the quality of customers. Clients should also be keen to show they have a good financial background because this can affect the premium.

He said: "It could reduce the cost of insurance because they are financially stable".