Premium Finance Market Study Update Paper Fair4All Finance response

About Fair4All Finance

Fair4All Finance is a not for profit organisation set up through government in 2019 to increase financial inclusion. We work across three key areas to make sure financial services provide what people need to manage their money, build their resilience and lead richer lives:

- **Influence** key actors across the system to prioritise, enable and deliver financial inclusion
- **Transform** the market to test and deliver the right products for all customers who need them
- **Scale** fair and affordable products to meet the needs of millions of customers

Our response

We welcome the opportunity to provide our views on the update paper as part of this timely Market Study (MS24/2.2). We are pleased to see the FCA exploring premium finance and we share the FCA's concerns that premium finance may not represent fair value for some customers, and that competition may not be operating well in the market. We have focused our response on financially vulnerable consumers' access to appropriate and affordable insurance and protection products.

The poverty premium

We believe that premium finance contributes to people in financially vulnerable circumstances having low access to insurance products. According to the Financial Lives Survey, almost one in six (8.6m) adults do not hold any general insurance products - this rises to one in four adults in financially vulnerable

circumstances[1]. Not only is insurance critical to financial resilience, but as motor and home insurance are often compulsory products, ensuring access to affordable options is essential for many households.

Currently one in ten people in the UK have no cash savings at all, and another 21% have less than £1,000 in savings[2] - meaning that a substantial part of the population do not have a savings buffer to manage 'lumpy' costs like annual insurance premiums. And our research shows that people in financially vulnerable circumstances are far more likely than the general population to pay for their insurance in monthly instalments[3]. As the Market Study notes, in 2024 60% of motor and 41% of home customers who paid in instalments 'did so because they could not afford to pay in a single annual payment'.

Our central concern is therefore that customers who cannot afford to pay upfront in a lump sum for insurance are charged an additional premium, compared to those who can. As such, premium finance is a significant driver of the 'poverty premium' in insurance, compounding the additional costs faced by individuals on low incomes or in poverty when navigating the insurance market. The Market Study suggests that it costs consumers typically between 8% and 11% more to pay monthly rather than annually (across both home and motor), which is a significant price differential.

The analysis in the Market Study also shows that paying in instalments is more common among younger customers, women, black people, those in financial difficulty, customers with mental health conditions, those with low financial resilience, renters, and lone parents.

We question whether it is fair that customers who cannot afford to pay upfront are required to pay significantly more, and whether the additional costs passed on to them are proportionate to the risks taken by lenders or insurers.

We were interested to learn that interest-free payment plans are much more common across home insurance than motor, with more than a third of home insurance customers paying no more for paying monthly, compared to just 3% of motor insurance customers. We welcome the commitment to perform further analysis of these two approaches, and the effect this has on fair value and competition. We also note that customers who pay in instalments and exhibit a vulnerability characteristic are less likely to have an interest-free payment plan to pay for motor insurance (8%), compared to more financially resilient customers (15%).

Transparency and consumer understanding

The market study's initial findings indicate that while most customers paying in instalments recall their provider explaining the cost difference, a significant proportion of contents insurance policyholders (19%) did not know whether paying in instalments or paying annually was cheaper. We agree that firms could do

[1] Fair4All Finance Segmentation Survey 2024
[2] FCA, 2024, Financial Lives Survey
[3] Fair4All Finance Segmentation Survey 2024. 'I pay monthly for my insurance': financially vulnerable consumers 68% vs. control group 56%

more to clarify premium finance costs to customers. Furthermore, we believe the process of taking out premium finance should be more transparent, ensuring consumers understand they are entering into a separate credit agreement and are aware of its implications, such as impact on their credit file or the consequences of missed payments (ie, loss of insurance product).

Unlike many other forms of credit, premium finance functions more like a subscription: if someone misses a payment, their insurance can be withdrawn, leaving them without protection. This creates confusion, as customers may not always realise they are entering into a loan agreement rather than simply spreading payments.

Double dipping

We welcome the FCA's commitment to firm based supervision to ensure the choice to pay monthly is not used as a risk indicator (often described as 'double dipping'). A customer receiving a higher quote due to a choice to pay monthly, as well as then charged 20-30% extra to pay for this 'choice', cannot be consistent with the principle of fair value. It is difficult to understand a reasonable justification for the choice to pay monthly being used to increase the price a consumer pays through two different avenues.

Increasing margins through premium finance

An additional concern raised in the Market Study update paper is that, while the profit margin on a core insurance policy might be low, margins on premium finance can be significantly higher, with some firms potentially recovering returns on lower-margin insurance products through elevated interest (2.13). We believe this practice is inconsistent with the principle of fair value.

Recommendations

To further develop the findings of the market study and promote fair outcomes for all consumers, Fair4All Finance recommends the following:

Assess impact on access

The market study should specifically explore the cumulative effect of premium finance costs on cohorts of customers already paying more due to their circumstances, such as younger drivers, people of colour, and those in financially excluded postcodes, and how this impacts overall access to insurance.

Promote transparency

The market study should actively seek to remove the ability for insurers to cross-subsidise between premium finance and insurance policies, ensuring that the cost of premium finance is priced transparently and not hidden within the policy. We also note that consumers currently have no choice over which premium finance provider they use, as this is selected by the insurer. We would encourage the FCA to consider whether firms might, if premium finance is offered, provide a consumer with a range of quotes from different providers, to enable consumer choice.

We also welcome the further analysis set out to understand how different approaches to setting pricing

(credit risk priced into the cost, or set out transparently and separately) effects fair value.

Address 'Double Dipping'

We agree that the practice of factoring the decision to pay monthly into the pricing of the underlying insurance premium (described as 'double dipping'), without an objective and reasonable basis, should be addressed through supervisory action.

Scrutinise disproportionate costs / difference in prices

We urge the FCA to scrutinise why providers take such a different approach to charging for customers paying monthly, given the low credit risk involved and the insurer's ability to cancel the policy if payments are not made. The market study should actively explore why providers who do not charge a premium for monthly payments are not more common, and why customers are not migrating to these providers.

Further analysis of market-wide remedies

While the FCA has provisionally ruled out market-wide remedies, we believe that such interventions, or other strong regulatory action, should be revisited if the Consumer Duty fails to prevent profiteering and ensure fair value. We would encourage the FCA to publish more detailed analysis of the potential effect, including possible second order effects, of the remedies explored.

Examine the role of commission

The market study should explore whether commission payments factored into premium finance costs are appropriate, proportionate, and genuinely contribute to a more competitive market and improved outcomes for customers.

Facilitate new market entrants

The FCA should explore ways to facilitate and encourage the entry of alternative lenders, such as credit unions, into the premium finance market. Credit unions, with their 'save as you borrow' model, could offer competitive rates, increase access to protection, reduce costs for consumers, and foster greater financial resilience.

We welcome the FCA's commitment to further analysis and active engagement with firms, industry groups, and stakeholders. We would be very pleased to discuss these points in more detail and to provide any additional information that may be helpful.