

# FCA calls for information on insurers' use of big data

The Financial Conduct Authority (FCA) has issued a "call for inputs" to gather information on how "big data" is used in the general retail insurance sector. While not inevitable, there is a significant possibility that the exercise will lead to more detailed scrutiny in the form of a market study. Engagement with the FCA at this stage may allow insurers to shape and streamline the issues (if any) that the FCA decides to take further.

## Seeking data about data

**The call for inputs (CFI) is a research exercise, led by the FCA's Strategy and Competition unit, which identifies various issues that the FCA would like to understand, in order to better inform its future work in this area.**

The FCA uses the term "big data" to include new and expanded data sets (such as data generated by telematics boxes in consumers' vehicles, mobile phone apps, price comparison websites, grocery shopping behaviour, credit reference agencies and social media), as well as the technologies and techniques used to generate, gather, process and analyse these new forms of data.

It is proposing to focus on retail general insurance products and, in particular, private motor insurance and home and contents insurance.

### Areas of interest

Issues that the FCA is seeking to understand include:

- Micro-segmentation: as big data allows for more accurate and granular risk profiling of consumers, what are the benefits and risks? In particular, which customer categories are likely to lose out, through higher premiums, withdrawal of cover, or re-categorisation as a non-standard risk?
- Price discrimination: to what extent can insurance firms use big data to discriminate between customers on factors unrelated to risk and cost, such as their propensity to switch?
- Use of consumers' data: how do firms use data from sources other than insurance applications, such as telematics boxes and social media profiles? How does this impact consumer attitudes and behaviour, and what are the potential effects for consumers who are unable or unwilling to generate that data?
- Impact on consumers' ability to access and assess information: will big data mean consumers need to provide more information, or less? Will the greater flexibility and choice offered by new,

## Key issues

- What is the purpose of the Call for Inputs?
- What are the issues that the FCA is seeking to understand?
- What is the timeframe for the review?
- What are the potential outcomes?
- How can firms engage in the exercise, and what are the benefits of doing so?

emerging products that are facilitated by big data be accompanied by increased complexity that makes it harder to compare pricing?

- Impact on switching: how easily can consumers replicate or port relevant data when they switch providers?
- Barriers to entry: to what extent will the need to invest in generating or acquiring big data act as a significant barrier to entry for new providers?
- Horizontal or vertical foreclosure: could lack of access to certain forms of data prevent new and

existing providers from being able to compete effectively? To what extent might these foreclosure effects result from vertical integration (e.g. between an insurer and a price comparison platform), exclusivity arrangements between insurers and third party data providers, or horizontal relationships between insurers?

- **Innovation:** how is big data likely to drive future innovation, through new products, better service, increased availability etc?
- **Economies of scale or scope:** will big data afford large firms economies of scale and scope that will give them a competitive advantage over specialists?
- **The regulatory framework:** does the current framework of the FCA and other regulators inhibit or foster innovative uses of big data? What changes to the FCA's regime might be needed to better serve this purpose?

## Next steps

The FCA has invited firms to respond to the questions set out in the CFI by 8 January 2016, and is aiming to report on its findings and its proposed next steps in mid-2016. In the meantime, industry participants can request to have a meeting or call with the FCA to discuss the issues in the CFI. The FCA has also indicated that it may engage with academics and other regulators, and may also seek additional data from firms to assess certain issues in more detail.

Once it has finalised its report, it may decide to initiate a formal market study to investigate issues of potential concern, which in turn could lead to the imposition of a range of remedies, or a reference to the Competition and



Markets Authority for an (even more) in-depth market investigation.

Alternatively, it may decide to apply other approaches, or that no further work is needed. However, the only other call for inputs that has been finalised by the FCA to date has already led to two market studies into the corporate and investment banking and asset management sectors respectively.

## Comment

The FCA has been careful to avoid suggesting that it considers the issues identified in the CFI to be likely to give rise to concerns. Moreover, there is no obligation on firms to respond to the CFI, or to respond to all the questions posed.

However, firms that do engage with the FCA at this stage - before it has formed any firm views about the relevant issues - have an opportunity to shape and to streamline the scope of the FCA's future activity in this area.

In particular, respondents will have the chance to demonstrate the overwhelming benefits that may be expected to arise, as big data leads to increasingly accurate risk-assessments. These include scope

for new providers to tap innovative data sources to serve niche markets with non-standard risks and, crucially, lower overall costs and improved pricing for insurers.

History has shown that if large insurers become unwilling or unable to cover non-standard risks, that creates opportunities for smaller, bespoke insurers to fill the gap. Key to maximising those opportunities - and the broader benefits of big data - is a regulatory framework with requirements for establishing new business that are as streamlined and effective as possible.

Insurers have always sought to reduce the effective cross-subsidy of higher risk customers by those that pose lower risks. To the extent that the use of big data allows them to do so more efficiently, and provided data protection laws are complied with, it should be encouraged.

Big data has the potential to be a dynamic and disruptive force for change in the sector. Gaining a better understanding of the likely future development of the market is a valid objective for the FCA, but it should think carefully before standing in the way of change.

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