Ref: EIOPA Public consultation on supervisory statement on differential pricing mechanisms in non-life insurances
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EXECUTIVE SUMMARY

Explanations	A differential pricing mechanism in insurance contracts describes a practice by which an insurance company adapts the cost or price of the product/service on considerations other than the expected risk premia or estimated expenses. Put simply, prices will reflect how proactive or passive a client is (shop around or not) rather than the risk related to the insured event.
Detrimental effects for consumers	Differential pricing mechanisms can have detrimental effects for consumers, from mis-selling to losing trust and distorting competition on the market.
Use of big data and AI	Differential pricing mechanisms are based on personal data processing – EIOPA should closely supervise the principles of purpose limitation, data minimisation, and legitimacy of processing of data in insurance companies.
Adequate product governance mechanisms	All rules laid down in the IDD delegated regulation on product oversight and governance (Arts. 4-9) should be adequately observed by product manufacturers and distributors of insurance products.

Contact:
Stefan Voicu, Research & Policy Officer, voicu@betterfinance.eu
Aleksandra Maczynska, Executive Director, maczynska@betterfinance.eu

INTRODUCTORY EXPLANATIONS

Insurances' costs and/or premiums generally reflect the risk of the insured event exhibits and how large the insurance indemnity would be. For instance, a voluntary motor insurance for a driver who never had an accident should be lower than one who had one or more (assuming the same vehicle).

What insurance companies (should) take into account when determining the risk premium are actuarial tariffs, administrative and service costs. However, in non-life insurances (many of which are mandatory by law), some insurance companies may adjust their premiums based on the "commercial" behaviour of the client, for instance whether a client shops around for the best price or will settle with whatever demanded.

Insurance companies have the advantage of processing very large amounts of data which, with the power of artificial intelligence (AI) and actuarial expertise, enable them to determine consumer behaviours and forecast responses to price changes.

In this light, the European Insurance and Occupational Pensions Authority (EIOPA), in exercising its mandate,[1] issued a Supervisory Statement (addressed to national competent authorities) on how to implement the relevant insurance regulations and supervise companies against such practices.

As this consultation of EIOPA concerns non-life insurances, BETTER FINANCE relies also on the expertise of its German member association representing the interests of non-life insurance policyholders (Bund der Versicherten - BdV).

Q1 – Have you observed the use of differential pricing practices in the EU insurance market?

Yes, our member reported various practices in non-life insurances where price walking or differential pricing mechanisms are used. For instance, in motor insurances, aspects that should not matter (such as frequency of usage, ownership of a garage, subscription to public transportation) are taken into account when proposing the price.

In our view, it also stems from what data insurance companies process and what data is asked for the demand and needs test. EIOPA and national competent authorities should first distinguish between information essential for the performance of the contract (calculating the risk premium) and other data, which should be prohibited. For instance, a dental health insurance should not inquire about the number of visits to a general practitioner, or number of medical interventions (non-dental) as it is not relevant.

BETTER FINANCE has highlighted during the work of the High-Level Forum on the Future of the Capital Markets Union the risks of open data in financial services and data sharing. Moreover, the contagion effect exacerbates the detrimental effect to consumers when one considers the amount of data in other financial sectors to which insurances come as a complement. BdV gives the example of consumer credit scores and the approximately on 680 million data sets linked to 66 million individual customers that a consumer credit scoring company uses in Germany. This type of data, shared with insurance companies, will obviously affect the market and calculation for payment protection insurances, where several "scandals" have been observed (UK, Netherlands); and the list can go on.

EU authorities should proctor very closely the use and sharing of data, especially in the insurance sector, as it will prove much easier to monitor rather than price supervision or regulation. In essence, BETTER FINANCE links the discussion on differential pricing mechanisms to open data and free, unconstrained consent when concluding contracts with financial services providers. Close cooperation with the European Commission's Directorate-General for Justice and Consumers (DG JUST) is necessary to adequately implement the provisions of the General Data Protection Regulation (GDPR), particularly the principles of purpose limitation and data minimisation (Art. 5(1)(b) and (c) GDPR), as well as the lawfulness of data processing (Art. 6(1)(b) GDPR).

[1] As per Art. 29 of EU Regulation 1094/2010.

In other words, if financial services providers conclude standardised adherence contracts with consumers, where the collection and processing of data "for the performance of the contract" is included, although not necessary, it is by default an issue that paves the way for price walking or differential pricing mechanisms.

Q2 – What types of differential pricing practices are you aware of?

Below, we reiterate the example given by BdV on the study of "dynamic pricing" mechanisms:

"Recently in one of the most prominent German insurance journals ("Zeitschrift für das Versicherungswesen") a study on " Dynamic Pricing" was published (Heft 13/14, S. 377-378, Juli 2022). Following to this study "Dynamic Pricing" is a new version of "predictive modelling" used by insurers since the 1980s. The latter already tried to combine foreseeable market price developments with adjusted risk calculations. "Big Data" may push premium calculations even more focused on special target markets. By using ever more precise "customer categorizations" the insurers may be enabled to base premium calculations on "probability of contract conclusion, rebate potential and cross-selling-possibilities". In this context "cross" or "up" selling is understood in that way that other products of other insurance classes are sold additionally (or premiums of existing contracts shall increase). These are just three examples how to enlarge to the possible use of "dynamic" or "differential" pricing practices not only at the point of renewal of a contract but at the point of sale and at the pre-contractual phase as well by insurers and intermediaries".

Q3 – Do you agree that the use of differential pricing practices is expected to increase as a result of competition in the markets, greater availability of data (Big Data) and/or technological advances (e.g. AI systems)?

We concur with the conclusions presented by BdV and add that Big Data and Open Finance will bring much more pricing issues, which in essence breach consumer protection rules. Moreover, Big Data and Open Finance may bring stability issues as these can distort competition on the market.

Q4 - Do you agree with the risks identified from differential pricing practices?

Yes, we concur with EIOPA's assessment and, in light of Q1 and Q3 above, we wish to add risks to distortion of competition, mis-selling, financial exclusion, and data protection.

Q5 - Do you agree with the scope of the Supervisory Statement?

Yes, we agree with EIOPA on the scope of the Supervisory Statement (paras. 2.18-2.26) and welcome the initiative as now supervisory action and escalation of investigations are needed to signal bad practices to market participants and act as a deterrent in the future. If not, then we run the risk of seeing new mis-selling "scandals" with consumer financial products.

Q6 - Do you agree with the objectives of the Supervisory Statement?

Yes, BETTER FINANCE agrees that EIOPA should not attempt to interfere directly on pricing, but that the internal practices, particularly what influences risk premiums, should be supervised.

Q7 – Do you agree that the following practices would result on unfair treatment of consumers:

- **Increasing the price of the insurance product at renewal stage based on the customer's low propensity to shop around (low probability of churn);**
- **Increasing the price of the insurance product at renewal stage based on the customer's low-price elasticity (also known as "willingness to pay");**
- **Advising or nudging consumers to buy one insurance product vs. another one because of very low initial on-boarding price, which then result into sudden, unexpected and significant price increases for consumers at renewal for reasons unrelated to risk or cost of service**
- **Other types of differential pricing practices?**

Please explain.

Yes, we agree with all the above stated practices.

Q8 - Do you agree that the IDD's Product Oversight and Governance requirements are an adequate tool for addressing the use of differential pricing practices?

Further clearance from EIOPA (to be implemented by national supervisors) would bring added value, particularly if differential pricing mechanisms would be spelled out.

Q9 - Do you agree that adequate governance measures should be put in place for the product approval process in order to ensure that differential pricing practices do not have a detrimental impact for consumers?

Yes, Art. 4 and 5 of the IDD Delegated Regulation on product oversight and governance must be adequately implemented and supervised.

Q10 - Do you agree with the governance measures described above for the product approval process?

Yes, we agree with EIOPA's assessment.

Q11 - Which other governance measures could be established for the approval process to ensure that differential pricing practices do not have a detrimental impact for consumers?

Insurance's pricing mechanisms must comply with the principles of ethical and trustworthy use of AI in the insurance sector.

Q12 - Do you agree with the governance measures described above for the target market?

Yes, we agree.

Q13 - Which other governance measures could be established for the target market to ensure that differential pricing practices do not have a detrimental impact for consumers?

Yes, see our comment on Q2 in relation to the different practices observed.

Q14 - Do you agree with the governance measures described above for product testing?

Yes, we agree.

Q15 - Which other product testing governance measures could be established to ensure that differential pricing practices do not have a detrimental impact for consumers?

The measures outlined in the Supervisory Statement are sufficient.

Q16 - Do you agree with the governance measures described above for product monitoring and review?

Yes, we agree.

Q17 - Which other governance measures could be established for product monitoring and review to ensure that differential pricing practices do not have a detrimental impact for consumers?

N/A.

Q18 - Do you agree with the documentation governance measures described above?

Yes, we agree.

Q19 - Which other documentation governance measures should be established to ensure that differential pricing practices do not have a detrimental impact for consumers?

We agree.

Q20 - Do you agree with the governance measures described above for the distribution channels?

Yes, we agree.

Q21 - Which other governance measures could be established for the distribution channels to ensure that differential pricing practices do not have a detrimental impact for consumers?

We recommend specifying that all governance requirements related to differential pricing mechanisms must be abided by both manufacturers and distributors of insurance products.