
FINAL NOTICE

To: Hastings Insurance Services Limited

Address: Conquest House
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Bexhill-on-Sea
East Sussex
TN39 3LW

Date: 24 July 2008

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("the FSA") gives you final notice about a requirement to pay a financial penalty.

1. THE PENALTY

- 1.1. The FSA gave Hastings Insurance Services Limited ("the Firm"/"Hastings") a Decision Notice on 21 July 2008 which notified Hastings that, pursuant to section 206 of the Financial Services and Markets Act 2000 ("FSMA"), the FSA had decided to impose a financial penalty of £735,000 on Hastings in respect of breaches of Principle 6 of the FSA's Principles for Businesses ("the Principles").
- 1.2. The breaches of Principle 6 relate to Hastings' cancellation of approximately 4,550 incorrectly priced customer motor insurance policies between June and September 2007 ("the Relevant Period").

- 1.3. Hastings confirmed that it will not be referring the matter to the Financial Services and Markets Tribunal.
- 1.4. Accordingly, for the reasons set out below and having agreed with Hastings the facts and matters relied on, the FSA imposes a financial penalty of £735,000 on Hastings.
- 1.5. Hastings agreed to settle this matter at an early stage of the FSA's investigation. It therefore qualified for a 30% (stage 1) reduction in penalty, pursuant to the FSA's executive settlement procedures. Were it not for this discount, the FSA would have sought to impose a financial penalty of £1.05 million on Hastings.

2. REASONS FOR THE PENALTY

Summary of conduct in issue

- 2.1. On the basis of the facts and matters described in more detail in paragraphs 2.16 to 2.66 below, the FSA consider Hastings to have failed to pay due regard to the interests of its customers and treat them fairly (in breach of Principle 6) in relation to its cancellation of approximately 4,550 motor insurance policies in the Relevant Period and in relation to certain later events arising out of those cancellations.
- 2.2. Hastings' decisions to cancel the affected policies came about as a result of quotation system errors which resulted in Hastings providing certain customers with inaccurate insurance quotations. The quotation errors meant that Hastings' customers paid significantly lower premiums for their insurance than they should have. Hastings invoked a legal right to cancel the affected policies rather than properly considering the interests of its customers, as required by Principle 6, by giving insufficient consideration to paying the shortfalls in premium to the insurance provider and/or investigating other possible remedies. The FSA considers that the cancellation clause in the policies relied upon by Hastings was not generally intended to be used to deal with such a situation and, by cancelling the policies as it did, Hastings failed properly to consider its customers' interests. There were also serious failings in the way in which Hastings dealt with customers after the cancellations, including in its complaints handling.
- 2.3. The FSA considers Hastings' conduct to be particularly serious for the following reasons:
 - (a) Treating Customers Fairly ("TCF") has been a priority for the FSA since 2004 and it has stressed repeatedly the importance of regulated firms ensuring they focus on TCF initiatives. Despite this, Hastings decided to cancel the affected policies without employing a proper and demonstratively objective decision making process that took account of the possible implications for its customers affected by the decisions. Further, after the decisions to give notice to cancel the policies had been taken, Hastings failed to provide its customers with customer service of an acceptable standard and as they might reasonably expect.

Accordingly, Hastings' customers could not be confident that the fair treatment of customers was central to Hastings' corporate culture during the Relevant Period and that their claims for compensation would be handled properly. In this regard, the FSA considers Hastings' actions to be contrary to the TCF consumer outcomes (first published in March 2006) which the FSA expects regulated firms to be focused on delivering.

- (b) Hastings is a large insurance broker and has approximately 500,000 customers. Its actions, therefore, have a large impact on customers, which makes it all the more important for Hastings to ensure that it is meeting its obligations in respect of treating customers fairly. In this particular matter, Hastings' decisions to cancel the under-priced policies impacted approximately 4,550 customers, consisting of 1,850 customers whose policies had not incepted and 2,700 customers whose policies were live.
- (c) The overall impact of Hastings' decisions to cancel cannot easily be quantified and it is therefore difficult to assess any financial cost to customers of rectifying the detriment caused by its breaches. Although approximately 1,900 customers received a period of cheaper motor insurance of up to a year. However, all affected customers suffered inconvenience from Hastings' decisions to cancel the insurance policies and there may be a continuing detrimental effect on the affected customers in that they are now obliged to declare, when seeking new insurance, that they have previously had insurance cancelled. Hastings' customers may, therefore, experience difficulty in obtaining future insurance, or even pay increased premiums, despite the cancellation being through no fault on their part; and
- (d) Hastings failed to advise the FSA of the problems it experienced with its quotation system, or of the implications of these problems for its customers, and only informed the FSA of the cancellation after it had taken the decision to cancel the affected policies.

2.4. Hastings' failures therefore merit the imposition of a substantial financial penalty.

2.5. In deciding the level of financial penalty the FSA recognises, in mitigation, that Hastings now accepts that its conduct was in breach of Principle 6 and has expressed regret about the effect of its actions on its customers. In addition, Hastings has taken a number of steps to remedy the potential ongoing detriment including writing to all affected customers to clarify that the cancellation was through no fault of the customer but arose out of Hastings' systems errors, and to invite customers who have not previously been compensated to contact Hastings to claim compensation for any financial detriment and/or inconvenience suffered. The FSA also recognises that Hastings has subsequently taken substantial remedial action in relation to its systems and controls on pricing of policies and changed its senior management and Board of Directors.

Statutory and Regulatory Provisions and FSA Published Materials

Relevant Statutory Provisions

- 2.6. The FSA's statutory objectives, as set out in section 2(2) of FSMA, include maintaining confidence in the financial system and the protection of consumers.
- 2.7. Section 206(1) of FSMA provides:

"If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, ... it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate."

Principles

- 2.8. The Principles are a general statement of the fundamental obligations of firms under the regulatory system. They derive their authority from the FSA's rule-making powers as set out in Chapter I of Part X of FSMA (Rules and Guidance) and reflect the FSA's regulatory objectives.
- 2.9. The following Principle is of particular relevance to this matter:

Principle 6: Customers' interests

A firm must pay due regard to the interests of its customers and treat them fairly.

Treating Customers Fairly

- 2.10. Since 2004 the FSA has published considerable material on the importance of regulated firms treating customers fairly. In particular, in March 2006, the FSA published a notice setting out that firms should be focused on delivering the six TCF consumer outcomes which include the following:
- (a) Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture (Outcome 1); and
 - (b) Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and also as they have been led to expect (Outcome 5).
- 2.11. In July 2006, the FSA set a deadline for all firms to be at least implementing TCF in a substantial part of their business by the end of March 2007. In May 2007, the FSA detailed firms' progress against that deadline and stated that a sizeable number of firms had failed to demonstrate that they are implementing TCF. This meant that senior

management at firms had failed to take sufficiently seriously the need to address TCF risks in their business. The FSA warned that, where firms have failed sufficiently to engage with TCF, it will use its enforcement powers where necessary. The events which are the subject of this Notice took place between June and September 2007.

- 2.12. The FSA expects all regulated firms to be able to demonstrate that they are consistently treating their customers fairly by the end of December 2008.

Determining the level of the financial penalty

- 2.13. In deciding to take the action, the FSA has had regard to the guidance published in the Decision Procedure and Penalties Manual ("DEPP"), which forms part of the FSA Handbook. In particular, the FSA has taken into account the general criteria for determining whether to take disciplinary action and the factors relevant to determining the appropriate level of financial penalty set out in DEPP 6.2 and 6.5.
- 2.14. The FSA has also had regard to the guidance published in the Enforcement Manual ("ENF") and, in particular, Chapters 11 and 13 which set out the relevant guidance in force until August 2007 (i.e. for most of the Relevant Period). In this case, there are no material differences between the guidance and factors to be taken into account when determining whether to take disciplinary action and the factors relevant to determining the appropriate level of financial penalty that were previously in force and those presently in force.
- 2.15. The FSA has also set the financial penalty in accordance with its announcements since September 2007 that it will be seeking to increase generally the level of fines imposed to provide a strong deterrent to others.

Facts and matters relied on

Introduction

- 2.16. Hastings is an insurance intermediary specialising in retail motor and household insurances, with a head office located in Bexhill-on-Sea, East Sussex. Hastings also sells ancillary products, including payment protection insurance and breakdown cover, through call centres and on the internet.
- 2.17. The company was established in 1997 and was acquired by Insurance Australia Group (IAG) in December 2006. Hastings now forms part of IAG UK. Following the acquisition by IAG and the Relevant Period in this Notice, both the senior management and the Board of Directors of Hastings have been changed.
- 2.18. During the Relevant Period, Hastings had a panel of insurers that consisted of 3 parts:
- Fully delegated insurers – all policy and claims administration including pricing is carried out by Hastings.

- Delegated insurers – bespoke insurance products are built by insurers with Hastings' IT department that are uploaded on to the Hastings IS2000 system. Insurers provide ratings data to Hastings, which is responsible for entering it onto the system. This category of insurers includes insurance products that are underwritten by Highway Insurance Company Limited (“Highway”).
- EDI (Electronic Data Interchange) Panel – uses a link to a proprietary system, where the data inputting is done by software houses to offer standard products on EDI basis from insurers.

Highway One

- 2.19. The events referred to as "Highway One" resulted from an error in a post code file for a comprehensive motor insurance product that was uploaded by Hastings on to its ratings data system (IS2000) on 15 June 2007. On 15 June 2007, Hastings' IT department identified an increase in the quotation of competitive premiums for the Highway comprehensive product and reported this information to the Hastings underwriting department. The underwriting department checked the premium calculations for Highway products and did not identify any errors. On 25 June 2007, an underwriting report showed an increase in Highway quotations for comprehensive motor insurance and a reduction in other panel member quotations, which indicated to the IT department that there may be an error with the post code data. The error was identified and fixed on 26 June 2007 and the Hastings management team were notified.
- 2.20. The error in the ratings data resulted in 90,000 quotations and approximately 1,880 policies being sold between 15 and 26 June 2007 with incorrect premiums; on average each policy was under priced by £222. 27 of the under-priced policies had incepted and approximately 1,850 policies were due to incept on or after 1 July 2007. Of these 1,850 policies, 380 were due to come into force on 1 July 2007.

Decision making

- 2.21. Hastings accepted responsibility for the error in the postcode data and paid the additional premiums of £6,500 to Highway to keep the 27 policies that had incepted on cover. The total cost of the additional premiums for the remaining 1,850 policies, which had not yet incepted, would have been approximately £410,000. Although Hastings had not been asked to by Highway, Hastings decided to invoke a clause under the terms of the insurance policy which allowed it, legally, to cancel the policy subject to providing seven days' written notice of the cancellation to the customer. Accordingly, Hastings decided to give notice to cancel the remaining 1,850 motor insurance policies.
- 2.22. The cancellation clause allows insurers to cancel insurance contracts upon written notice without giving reasons. The FSA considers that this clause is generally used where customers fail to disclose material facts that would affect their insurance. Hastings, however, does not consider that its use of the cancellation clause, of itself, was unfair and it does not accept that the cancellation clause should not be used in the

event of a widespread mispricing error, particularly where there is a risk that the mispricing is of significant magnitude that customers' claims, if they arise, could not be met.

- 2.23. Hastings recognised the need to act quickly in order to cancel the insurance policies before they incepted in order to minimise the impact on policy holders and to avoid the inconvenience caused by cancellation of the policies mid term.
- 2.24. The decision to give notice to cancel the policies was made by Hastings' senior management on 28 June 2007 in respect of Highway One and Hastings started to contact policy holders the same day. Hastings notified the FSA of the error and cancellation exercise on 29 June 2007.
- 2.25. On 2 and 3 July 2007, (four days after Hastings had taken the decision to cancel the affected policies), Hastings' customer relations department contacted the Financial Ombudsman Service (FOS) technical helpdesk for its view on the appropriate levels of any redress. Hastings has stated that, after explaining the circumstances of Highway One, namely that written notice of cancellation had been issued, that premiums were being refunded in full and that CHAPS payments were being arranged for "hardship" cases, the FOS considered Hastings' award of a further £20-£30 ex gratia payment in those cases where customers sought compensation for inconvenience and stress to be acceptable and fair.
- 2.26. However, in a contemporaneous email of 2 July 2007, Hastings' customer relations department advised the compliance department that, "[i]n their[FOS'] view (again this is informal advice only) the seven days notice is there to allow the insurer to cancel the contract where for example, the insurer was unaware of certain information which would have influenced their assessment of the contract, or where information has come to light which causes them to reconsider their position after the contract has been confirmed".
- 2.27. Further, on 2 July 2007 and after it had already decided to cancel the 1,850 policies, the compliance department told the complaints department that "*the Chartered Insurance Institutes course book explains that an insurance contract has a 7 days cancellation clause that can be used by Insurers, and although it gives an example of a material fact changing, it does not limit it to that?*" In replying later that same day, Hastings' compliance department commented that "*I think the feeling from talking with others some of whom are ACII [Associates of the Chartered Insurance Institute] is that it is unfair cancellation of the contract, however, can appreciate the need to balance this up with commercial consideration due to the numbers involved*".
- 2.28. Finally, in a report written in November 2007, the relevant individual from Hastings' customer relations department summarised the contact he had had with the FOS technical helpdesk at the relevant time i.e. July 2007. That report stated that "*1. They felt that whilst in their [FOS] view our "moral" application of the invocation of the 7-day notice clause might be questionable, they felt that we were however, within our rights to invoke cancellation of the policy. 2.They mentioned that they felt that 14 days*

notice of cancellation might have been more appropriate under the circumstances, particularly as people could be away on holiday. I explained that in these circumstances I was sure that we would look favourably upon dealing with any claim that may occur if customers found them in this position. They appeared satisfied that we would treat individual customer complaint on its own merits. 3. From a compensation viewpoint, the informal advice given was that FOS would look favourably on a customers claim for compensation where they could show that they entered into a financial agreement (the purchase of a new car) as a result of our advice (quotation)".

- 2.29. After 3 July, Hastings did not receive any subsequent advice from the FOS that it was fair to invoke the cancellation clause nor did it seek any legal advice in respect of Highway One either before or after it took the decision to cancel the policies, despite Hastings' compliance department stating on 27 June 2007 in an email to the Head of Business Development Administration that it was "*crucial to get legal opinion on the situation before we get engaged in providing the directions to the call centre so that we know how we are going to be advising staff and customers*". However, these emails were not escalated to Hastings' senior executive at the time.

Cancellation process

- 2.30. Hastings briefed its call centre staff and set up two dedicated call centre teams which attempted to contact affected Highway One policy holders by telephone to notify them of the erroneous under-pricing and consequent cancellation of the policies. However, Hastings considered that, in view of the timeframe available, it was not feasible to contact all customers. Hastings therefore decided that, for those customers it was able to contact, it would provide a seven day notification letter and, for those customers it was not able to contact, it provided 10 day notification letters. Hastings also offered affected policy holders a re-broking service to other insurers on the Hastings panel although not at the original premium quoted.
- 2.31. Hastings subsequently sent the notification letters to the affected customers asking them to return their original certificate of insurance and informing them that, subject to no claims being made, a full refund would be given. The letters explained that Hastings was "*unable to offer any further cover with Highway Insurance due to a technical error which occurred during [the] original quotation process*". The letter also apologised for the cancellation and provided the customers with a new quotation from another insurer. Customers were informed that they had seven days from the date of the letter to make other insurance arrangements and told that "*no cover under this policy will be in force after this period and no further notice will be issued*". Hastings also reminded its customers that "*it is an offence under the Road Traffic Act to keep or use a motor vehicle on a public highway without adequate insurance being in force*". Where it was not possible to contact policy holders by telephone, Hastings sent the customers a letter that was identical except that it notified customers that the cancellation would take effect after 10 days. Where internet quotations had not been taken up they would be put into "refer" mode so that the original quotation could not be accepted. Hastings also put a note on its website to inform customers that "*due to a*

technical error during your original quotation process, we are no longer able to offer you the quote previously provided". Hastings apologised for the inconvenience and invited customers to obtain a new quotation.

- 2.32. Hastings re-brokered (i.e. placed with new insurers) a total of 568 of the 1,850 policies it cancelled in respect of Highway One.

Complaints handling and redress

- 2.33. As at 31 January 2008, Hastings had received approximately 252 complaints in respect of Highway One and paid redress amounting to £2,049.
- 2.34. For those customers who had paid a deposit for their policy or had paid for their policy in full, and were in urgent need of a refund, refund payments were made largely by CHAPS, which took one day. In all other cases, refunds were made by BACS, which took three working days. However, customers did not actually receive refunds until after the cancellation had taken effect.
- 2.35. Some customers complained about a number of different aspects of Hastings' handling of Highway One. For those customers who complained, Hastings awarded redress payments of between £20-£30, which it considered to be appropriate compensation for inconvenience and stress.

Highway Two

- 2.36. The events referred to as "Highway Two" resulted from two errors in the data used to calculate premiums for Highway non-comprehensive motor insurance and is unconnected to the error which gave rise to Highway One.
- 2.37. The errors relate to data that was entered by Hastings on to its IS2000 system in January 2006 and affected two groups of consumers – 19 year olds and a group of inner city postcodes referred to as "area 40". The error in the data used to quote insurance premiums for 19 year olds' policies resulted in premiums being under-priced by an average of £539. The errors in the postcode data resulted in quotations being generated for customers living in area 40 locations when the system should have declined these customers as Highway did not offer motor insurance in these areas.
- 2.38. The area 40 errors were initially identified on 11 July 2007 through testing that was carried out by Highway on Hastings' systems following identification of the Highway One error. Once discovered, Hastings moved quickly to correct the errors and the area 40 errors were fixed by 13 July 2007.
- 2.39. The ratings errors relating to 19 year olds were identified on 20 July 2007 and, once discovered, Hastings suspended the system to stop it providing inaccurate quotations. The full extent of the Highway Two errors became clear on 23 July 2007 when

Highway attended Hastings' office to investigate the misquoting. Hastings subsequently took action to correct the ratings data and, by 26 July 2007, the system was live again and providing accurate quotations. Hastings subsequently closed the panel for new business in August and renewals in September 2007.

- 2.40. The ratings errors affected 3,889 policies that had incepted since January 2006. Of these, approximately 3,449 were still live as at 31 July 2007 (consisting of approximately 1,929 policies held by 19 year old policy holders and 1,520 policies for customers living in area 40 locations). Hastings arranged for 471 customers to remain on cover with Highway (as they were within three months of renewal). Therefore, 2,978 policies were due for cancellation. However, 170 customers cancelled in the normal course of business between 31 July 2007 and 12 August 2007. Accordingly, as at 12 August 2007, 2,808 policies were to be cancelled.
- 2.41. A further 96 customers were retained on cover upon Hastings paying the shortfall in premium to Highway (consisting of 61 later considered to be too close to renewal to cancel and 35 where Hastings was unable to make contact with the customer). Therefore, in total, Hastings gave notice to cancel 2,712 policies that had incepted i.e. were live in respect of Highway Two.
- 2.42. Between late July and 6 August 2007, Highway and Hastings had a number of discussions regarding continuing cover for some or all of the affected customers. The number and type of customers for whom Highway would be prepared to continue to provide cover, and the payment Highway would require from Hastings to compensate them for the shortfall in premium caused by Hastings' ratings errors, varied significantly during this period. However, in an email between Highway and Hastings on 6 August 2007, Highway informed Hastings that, unless it paid an additional premium of £1.37 million, it had no option but to insist that the policies be cancelled.

Decision Making

- 2.43. The formal decision to cancel the policies in respect of Highway Two was made on 7 August 2007 by the Hastings Board and the exercise to give notice of cancellation began on 8 August 2007.
- 2.44. On 2 August 2007, Hastings considered that it had a number of options in respect of the affected Highway Two policies. These included the following:
- (a) *"Tell Highway it is their error and we believe we have to honour the premium quoted under our TCF obligations"* (although Hastings considered this probably to be a non-starter);
 - (b) *"Cancel the...policies in as fair a way as possible"*.
- 2.45. However, after seeking legal advice, Hastings realised that it was legally responsible for the errors and concluded that it had *"little choice but to cancel the policies as it is*

the only route to closure" and relied on the same cancellation clause that it had used in Highway One."

- 2.46. Prior to making the formal decision to cancel, in the FSA's view, Hastings did not fully and properly consider the possible alternatives, and did not adequately take into account the implications and consequences of its decision. In particular, it did not consider other possible ways of continuing the policies to the full term such as alternative sources of funding for the premium shortfall or re-broking the policies within the IAG UK group (although there is no certainty that any other group company would have underwritten the policies other than on normal commercial terms).
- 2.47. However, Hastings has contended that it did consider various options and, in particular, that it sought legal advice as a result of which it understood that one of its options was to cancel the affected policies.
- 2.48. Hastings dismissed the possibility of paying the premium shortfall in early August when, at this stage of negotiations with Highway, the total additional premium was being estimated as approximately £750,000. Given that Hastings refused to pay the additional premium when it was estimated as being approximately £750,000, the possibility of Hastings paying the £1.37 million required by Highway on 6 August 2007 in order to continue cover for all customers affected by Highway Two must have been even more remote.
- 2.49. Hastings has argued that it may potentially have also faced unlimited claims exposure in respect of the area 40 policies if Highway made a loss on the affected policies and subsequently sought to recover that loss from Hastings. By 6 August 2007, Hastings had received legal advice that, in respect of the area 40 policies, it would either have to pay the difference in premium rates or agree to bear losses in order to avoid cancellation, albeit the legal advice noted that Highway's position on the issue was not clear at that stage. Highway later confirmed that if Hastings paid approximately £492,000 in additional premium it was happy for the area 40 customers to remain on cover. Accordingly, the FSA does not accept that Hastings would have been exposed to such potential unlimited losses.
- 2.50. In any event, Hastings failed to consider instructing its legal advisers to advise upon how they might circumvent any issues of possible liability in respect of Area 40 customers once an additional premium had been paid to Highway, nor did it discuss its concern in this respect with Highway.
- 2.51. Hastings' notified the FSA of its decision to cancel the Highway Two policies on 14 August 2007, five weeks after the initial errors were identified and one week after it had made the decision to cancel and by which time the cancellation exercise was already under way.

Cancellation process

- 2.52. Hastings' cancellation exercise in respect of Highway Two began on 8 August 2007.
- 2.53. Hastings call centre staff attempted to contact all affected policy holders by telephone to notify them of the decision to cancel their policy and the seven day notice period. Policy holders then received a letter confirming the details of the call. Policy holders were given pro-rata refunds for the remaining policy term, which were issued at the end of the seven day notice period. Initially, and in accordance with the terms of the cancellation clause in the affected policies, Hastings intended only to refund premiums to policy holders that had not made a claim. However, following consultation with the FSA, Hastings decided to refund premiums to all affected policy holders. Hastings also offered affected policy holders a re-broking service to other insurers on the Hastings panel although not at the original premium quoted.
- 2.54. Refund payments were made largely by BACS although CHAPS payments were used in 120 cases at the discretion of the customer relations department where, for example, the customer complained that they would suffer particular hardship. However, as with Highway One, the refunds were only made after the cancellation had taken effect. Accordingly, none of Hastings' customers affected by the Highway Two errors received their refund before the date on which they ceased to have insurance. This meant that, unless they were prepared to be without insurance for a period of time, Hastings' customers had to find additional funds in respect of their new insurance.
- 2.55. A total of 567 policies were ultimately kept on cover – this consisted of the 471 agreed with Highway which were cases where the policy was due for renewal before 1 November 2007 and the policy holder had almost earned an extra year no claims discount (“NCD”). In addition to this were a further 96 cases referred to Highway during the cancellation exercise where the policies were renewing in November/December 2007 and had therefore almost completed a full term, cases where Hastings were unable to contact the policy holder to notify them of the cancellation and a small number of complaint case referrals that Hastings agreed to keep on cover and who were selected on the basis that they were "*most likely to escalate and cause [Hastings] most problems*".
- 2.56. Hastings re-broked (i.e. placed with new insurers) a total of 338 of the 2,712 policies it cancelled in respect of Highway Two.

Complaints handling and redress

- 2.57. In respect of Highway Two, as at 31 January 2008, Hastings had received approximately 543 complaints and paid redress amounting to £10,400.
- 2.58. Those customers that complained to Hastings did so for a number of reasons including the fact of the cancellation mid-term and loss of NCD entitlement. Also, some customers complained about delays in receiving the refund of their premium. In any

event, all affected policy holders had to fund new insurance before receiving the refund for their cancelled insurance policy.

- 2.59. Hastings placed too much weight on the fact that customers had enjoyed a period of cheaper motor insurance of up to a year, did not consider paying compensation to all affected customers for the effort of re-arranging their policies early and awarded redress only where customers complained and cited stress and inconvenience. With regard to financial detriment suffered, again Hastings did not consider compensating all affected customers but awarded redress where customers approached Hastings and could demonstrate that the decision to cancel their policy had caused them financial loss.
- 2.60. Hastings recognised that, although not all of the policy holders affected by the cancellation would have been entitled to a full year NCD, the cancellation of the policies mid-term meant that some of its customers would not have received the NCD that they would have been entitled to if their policy had continued for the full year. Hastings compensated customers for the difference in premiums which they were forced to pay as a consequence of losing their NCD, although this was done only where customers actively took steps to complain to Hastings and request compensation for their loss of NCD entitlement. Hastings did not carry out any later exercise to identify those customers who would have been entitled to a full year's NCD had their insurance not been cancelled mid-term.
- 2.61. Hastings also produced a letter for customers to provide to their new insurer explaining that the policy was cancelled through no fault of the customer and confirming that the customer had been insured for a period of time (albeit less than a full year) and not claimed during that period. However, these letters were only provided to customers when they contacted Hastings and expressed concern about finding alternative insurance.
- 2.62. Hastings carried out a quality monitoring audit on the calls made to policy holders to explain the decision to and process for cancelling their insurance policy in October 2007. The Quality Assurance Team reviewed 803 calls and identified the issues set out below:
 - In 101 calls incorrect advice was given, such as telling the customer that due to the error most insurance companies would accept proof of NCD in months;
 - In 99 calls the agent did not or refused to escalate a complaint and in some cases told the customer there is "*no point in speaking to the FSA/FOS as they told us to do [the cancellation]*";
 - 80 calls where the customer had to contact Hastings again to resolve their query, for example customers having to chase refunds;
 - 60 calls where the agent did not make it easy for the customer to obtain a new quotation, including agents refusing to give a re-quotation or estimating new premiums without calculating a quotation; and

- 6 calls where there was mis-selling of ancillary products, such as the agent adding on the ancillary products without the customers' knowledge.

Mis-selling of additional products

- 2.63. Following the quality monitoring audit referred to in paragraph 2.62, Hastings carried out a further review of the calls and identified 105 instances where, as part of the re-broking exercise, ancillary products were mis-sold to customers.
- 2.64. In respect of Highway One, Hastings re-broked 568 policies and there were 38 instances of mis-selling. In respect of Highway Two, 338 policies were re-broked and there were 67 instances of mis-selling.
- 2.65. The mis-selling was carried out by one team of call centre staff as a result of insufficient briefing of agents by the team leaders. Hastings did however contact the customers again to establish if they required the ancillary products. All of the affected customers were refunded the full premium they paid for the ancillary products and given the option to retain the products free of charge until their next renewal. Hastings also dealt with the team leaders responsible for the mis-selling in line with its disciplinary procedures.

Analysis of breaches

- 2.66. The FSA considers Hastings to have breached Principle 6 by failing to pay due regard to the interests of its customers and treat them fairly because of the following:
- (1) In relation to both Highway One and Two, Hastings cancelled the affected policies by invoking a clause in the policies that, while legal, in the view of the FSA, was not generally intended to be used to deal with the particular circumstances while failing sufficiently to consider the full implications of its decision to cancel or to explore the alternative options available to it (such as alternative sources of funding for the premium shortfall or re-broking the policies within the IAG UK group). In this respect Hastings' misconduct in relation to Highway Two was more serious because:
 - (a) Hastings, having already been confronted with the issue in relation to Highway One, should have been in a better position to appreciate whether it was appropriate to invoke the seven day cancellation clause;
 - (b) In relation to Highway One, Hastings acknowledged its TCF obligations to a degree by recognising the inconvenience that would be caused to customers by having their policies cancelled mid-term, moving quickly to cancel those that had not incepted and agreeing to bear the cost (£6,500) of keeping on cover those customers whose policies were live. By way of contrast for Highway Two, Hastings did not fully and properly consider the possible alternatives, and did not

adequately take into account the TCF implications and consequences of its decision. Hastings simply focussed on the cost (failing, for example, to consider whether the potential unlimited claims exposure in respect of the area 40 business could be eliminated or mitigated) and failed to properly consider its TCF obligations with the result that most Highway Two policies were cancelled mid-term. The FSA does not accept Hastings' contention that it did consider various alternatives although does recognise that it sought legal advice as a result of which Hastings understood that one of its options was to cancel the affected policies.

- (2) In relation to Highway Two, Hastings' cancellation of policies mid-term meant that customers who would have been entitled to a NCD if they had successfully completed a full year's insurance without making a claim were deprived of the opportunity of any such bonus;
- (3) In relation to both Highway One and Two, Hastings placed its customers in the difficult position of being forced to take out new insurance at short notice and this occurred before they received the refund for their cancelled insurance;
- (4) In respect of both Highway One and Two, Hastings' decision to cancel the policies means that customers are now obliged to declare, when seeking new insurance, that they have previously had insurance cancelled. This means that Hastings' customers may experience difficulty in obtaining future insurance, or even pay increased premiums, despite the cancellation being through no fault on their part;
- (5) In relation to both Highway One and Two, once Hastings had decided to cancel the affected policies, it relied solely on its complaints procedures to ensure the fair treatment of customers. While the complaints procedures treated customers individually, the outcome was that some customers were treated more favourably than others. The associated service Hastings provided to its customers was inadequate and there were serious failings in the handling of Hastings' contact with the affected customers including the mis-selling of ancillary products, providing incorrect advice and the failure to ensure complaints were properly escalated. In particular:
 - (a) In relation to both Highway One and Two, Hastings only paid compensation for inconvenience and stress where those who complained cited them rather than paying compensation to all those customers whose insurance policies were cancelled;
 - (b) In relation to Highway Two, Hastings failed properly and proactively to consider the full implications of the cancellation on its customers and its actions after the decision to cancel had been taken were inadequate. Hastings' consideration of the costs of rectifying its errors was reactive rather than proactive. In particular:

- (i) Hastings only paid redress to customers when they complained and could demonstrate that they had suffered a financial loss as a result of the cancellation of their policy;
 - (ii) Hastings took the same approach to paying redress for the Highway Two cancellations as it had taken in respect of the Highway One cancellations, despite the different NCD positions. In respect of Highway One, Hastings recognised the need to act swiftly to avoid the inconvenience to customers of having their policies cancelled mid-term rather than before inception and the impact this may have had on their NCD entitlement. However, Hastings' general approach to paying redress in Highway Two did not sufficiently take into account the impact on the customer of losing their NCD entitlement;
 - (iii) Hastings only paid redress for loss of NCD when customers contacted them and could demonstrate the difference between their insurance premiums with and without an additional year NCD;
 - (iv) For those customers who experienced difficulty finding alternative cover, Hastings expected them to complain in order to remain on cover. Hastings failed proactively to take steps to ensure customers were not disadvantaged in this regard and only offered customers a letter to forward to their new insurer which explained that the customer was in no way responsible for the policy cancellation. This action by Hastings was again reactive and failed properly to address the inconvenience caused to customers of having to declare when seeking new insurance that Hastings had cancelled their insurance without any fault on the part of the customer.
- (c) In relation to Highway Two, Hastings arranged for a limited number of customers to remain on cover on the basis that they were the most likely to escalate their complaints and cause Hastings the "*most problems*"; and
- (d) Other than those customers referred to in (c) above, in relation to Highway Two, Hastings only agreed to pay the shortfall in additional premium for (and therefore keep on cover) those customers (i) whose policies had less than three months to run until expiry and (ii) those customers which it had not been able to contact by telephone.

Summary

- 2.67. The FSA considers that in both Highway One and Highway Two Hastings subordinated its customers' interests and expectations to its own financial interests and did not give full and proper consideration to the alternatives to invoking the cancellation clause in response to the mispricing of policies.
- 2.68. Hastings failed properly and proactively to consider the full implications of the cancellations on its customers and its actions after the decision to cancel had been taken were inadequate. This demonstrates that the fair treatment of customers was not central to Hastings' corporate culture during the Relevant Period.
- 2.69. Accordingly, the FSA considers that Hastings failed to comply with its obligations under Principle 6.

Analysis of the sanction

- 2.70. The principal purpose of imposing a financial penalty is to promote high standards of regulatory conduct by deterring firms and approved persons who have breached regulatory requirements from committing further contraventions, helping to deter other firms and approved persons from committing contraventions and demonstrating, generally, to firms and approved persons, the benefit of compliant behaviour (DEPP 6.1.2G).
- 2.71. In determining whether a financial penalty is appropriate and proportionate, the FSA will consider all the relevant circumstances of the case. DEPP 6.5.2G sets out guidance on a non-exhaustive list of factors that may be of relevance in determining the amount of a financial penalty.
- 2.72. In deciding to take the action, the FSA considers the factors outlined in paragraphs 2.73 to 2.88 to be particularly relevant:

Deterrence (DEPP 6.5.2G (1))

- 2.73. As announced on 26 September 2007, in line with its general approach the FSA is seeking to increase the level of fines where this is warranted by the nature, seriousness and impact of the breach in question, and by the likely impact on deterrence.
- 2.74. A financial penalty is required to support the message to the industry that it is vital that regulated firms should be focused on delivering the six TCF consumer outcomes which have been widely publicised by the FSA.

The seriousness of the breaches (DEPP 6.5.2G (2))

- 2.75. The FSA has had regard to the seriousness of the breaches, including the nature of the principle breached, the number of customers affected and whether the breaches revealed serious or systemic weaknesses of the management systems or internal

controls. For the reasons set out at paragraph 2.3 above and having regard to the impact on Hastings' customers, the FSA considers that the breaches are of a serious but not systemic nature in that Hastings placed undue prominence on its consideration of the financial cost rather than the impact on its customers.

- 2.76. The FSA does, however, recognise that, under the terms of the policies, Hastings was legally entitled to invoke cancellation, subject to providing seven days' written notice to the affected customers in Highway One and Highway Two.

The extent to which the breach was deliberate or reckless (DEPP 6.5.2G (3))

- 2.77. The FSA considers that Hastings did not deliberately act in breach of Principle 6 in taking its decision to cancel the affected policies but does consider that Hastings was reckless in failing to have proper regard to the potential impact this decision may have on its customers.

The size, financial resources and other circumstances of the firm (DEPP 6.5.2G (5))

- 2.78. Hastings is a well known insurance intermediary and has a prominent position in the retail consumer motor insurance market. It has approximately 500,000 customers and has recently been ranked as the 5th largest personal lines insurance intermediary in the UK.
- 2.79. In determining the level of financial penalty, the FSA has had regard to the size and financial resources of Hastings, as well as its role within the wider IAG group of companies.

The amount of profits accrued or the loss avoided (DEPP 6.5.2G (6))

- 2.80. In respect of Highway One, Hastings decided to cancel the affected insurance policies. An alternative would have been to pay approximately £410,000 in additional premium to the insurance provider which would have been due had these policies incepted. In respect of Highway Two, Hastings could have paid £1.37 million in additional premium to the insurance provider. However, it is recognised that the cancellation exercise (and associated payment of compensation) has resulted in Hastings incurring additional cost.

Conduct following the breach (DEPP 6.5.2G (8))

- 2.81. On discovering the errors in Highway One and Highway Two, Hastings attempted to contact the majority of the affected customers by telephone to explain the cancellation, deal with any customer queries and offer to rebroke the policies. Where Hastings was unable to contact customers by telephone, in Highway One Hastings provided 10 days notice of cancellation and in Highway Two, Hastings paid the shortfall in premium to Highway in order for a small number of customers to remain insured rather than risk driving uninsured and uninformed of the decision to cancel.

- 2.82. In September 2007, Hastings commissioned a review by IAG (UK) Internal Audit, supported by independent external accountants, of its systems and controls. Additionally, Hastings has been providing the FSA with regular progress updates on the improvements it has been making to address the issues identified by the audit.
- 2.83. As a result of these reviews, Hastings has adopted a number of recommendations for improvement to its processes including reorganising its Board of Directors, senior management and its compliance regime.
- 2.84. Hastings has co-operated fully with the Enforcement investigation and has agreed the facts of this matter as set out in this Notice. It has received a 30% discount for settlement at an early stage. Without this, the financial penalty would have been higher.
- 2.85. To reduce the risk that any customer continues to suffer any detriment, Hastings has also committed to undertake a customer contact programme. This will include writing to all the affected customers advising them of the FSA's findings, providing additional complaints information and providing confirmation that the policies were cancelled entirely at Hastings' instigation and that the customer was in no way responsible for this.

Disciplinary record and compliance history (DEPP 6.5.2G (9))

- 2.86. Hastings has been authorised to conduct insurance business by the FSA since 14 January 2005, and for other regulated activities since 1 December 2001, and has not been the subject of previous FSA disciplinary action.

Previous action taken in relation to similar failings (DEPP 6.5.2G (10))

- 2.87. In determining the level of financial penalty, the FSA has taken into account penalties imposed by the FSA on other authorised persons for similar contraventions.

FSA guidance and other published materials (DEPP 6.5.2G (12))

- 2.88. In determining the appropriate level of financial penalty, the FSA has had regard to the fact that the FSA has published considerable material (in particular, as described at paragraphs 2.10 to 2.12 above) in respect of treating customers fairly. As noted at paragraph 2.3(a) above, this significantly increases the seriousness with which the FSA has viewed the breaches.

Conclusion

- 2.89. Having regard to the seriousness of the breaches and the risk they posed to the FSA's statutory objectives of maintaining confidence in the financial system and securing the appropriate degree of protection for consumers, the FSA decided to impose a financial penalty of £735,000 on Hastings.

3. DECISION MAKER

3.1. The decision which gave rise to the obligation to give this notice was made by the Settlement Decision Makers on behalf of the FSA.

4. IMPORTANT

4.1. This Final Notice is given to Hastings in accordance with section 390 of FSMA.

Manner of and time for payment

4.2. The financial penalty must be paid in full by Hastings to the FSA by no later than 7 August 2008, 14 days from the date of the Final Notice.

If the financial penalty is not paid

4.3. If all or any of the financial penalty is outstanding on 8 August 2008, the FSA may recover the outstanding amount as a debt owed by Hastings and due to the FSA.

Publicity

4.4. Sections 391(4), 391(6) and 391(7) of FSMA apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to Hastings or prejudicial to the interests of consumers.

4.5. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA contacts

4.6. For more information concerning this matter generally, you should contact Suzanne Burt (020 7066 1062) or James Lake (020 7066 7042) of the Enforcement Division of the FSA.

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Georgina Philippou
Head of Department
FSA Enforcement Division