

## Citizens Advice response to the Competition Commission Payment Protection Insurance Market Investigation: Emerging Thinking

**27 November 2007**

Citizens Advice welcomes this opportunity to respond to the Competition Commission Payment Protection Insurance (PPI) market investigation emerging thinking document. The Citizens Advice Bureau service is a network of 432 independent advice centres providing free, confidential and impartial information, advice and advocacy from over 3,000 locations in England, Wales and Northern Ireland. In 2006/07 the CAB service dealt with around 5.7 million new problems of which around 6,000 related specifically to Payment Protection Insurance (PPI). However, while problems with PPI are a small part of the overall number of enquiries seen by the CAB service we believe that features of the PPI market are producing severe detriment for consumer on a systematic basis.

In 2005 Citizens Advice published an evidence report *Protection racket* that formed the basis of the super-complaint we made to the Office of Fair Trading. CAB evidence highlighted four main problem areas with PPI as follows:

1. The cost of PPI seemed excessive and often involved borrowers having to take on additional credit to fund PPI premiums
2. The content of policies often failed consumers either because benefits were insufficient to prevent debt problems or because blanket exclusions from cover denied borrowers access to benefits
3. In many of the cases we saw PPI had been seriously mis-sold to borrowers who would never have been able to benefit from either some or any of the cover set out in the policy. Often the lender or intermediaries clearly had sufficient information about the borrower's circumstances to know the policy would be inappropriate, but sold it anyway.
4. Poor claims administration or a lack of forbearance by lenders pending payment of a claim often results in otherwise avoidable debt problems.

Point three and four of the above relate to the sales and administration processes regulated by the Financial Services Authority by both high level principles and by the Insurance Conduct of Business (ICOB) rules book. It is noteworthy that the FSA has recently consulted on proposed amendments to ICOB that would introduce specific additional rules for sales of protection products (including of course PPI) as these are seen as being *high risk* relative to other general insurance products. Here it is also noteworthy that enquiries about PPI make up 22 per cent of all inquiries about insurance products received by the CAB service. Only motor insurance produces more enquiries but the issues of cost and detriment are not generally as severe as with PPI cases.

We would also point out that the FSA as also carried out three thematic reviews of PPI selling and has continued to find evidence of widespread problems with the way PPI is being sold. This includes what the FSA describes as 'little or no progress' by firms in giving consumers clear information on either the cost of PPI products or key elements of product content such as cover and eligibility. This is despite reasonably detailed ICOB rules setting out requirements on how

information on key product features should be presented to consumers at the point of sale. Recent CAB evidence shows how such requirements may do little to protect consumers from buying PPI policies that they will not be able to benefit from.

A CAB in Yorkshire saw a 41 year old man who had taken out a personal loan of £9,000 with a bank. He did not realise that he had also taken out payment protection insurance and did not want it. The PPI added an extra £2,600 to the outstanding loan and an extra £60 to the monthly payment. The man said that the PPI was not explained at time of taking out the loan agreement or discussed as being optional. PPI was, however, clearly stated as an additional amount in the loan agreement paperwork.

A CAB in Wales was visited by a woman who had three credit cards and four personal loans with the same lender. She had been sold a PPI policy in respect of each of these credit agreements despite the fact that she had been unable to work and in receipt of incapacity benefit throughout the whole period. The PPI had greatly increased her repayments and she fell further into debt as a result. She told the bureau that she was considering suicide.

A CAB in Nottinghamshire saw a 39 year old woman who had taken out a credit card. At the time she was an agency worker, but the lender told her that she would be covered by the PPI policy sold with the card. Some time later she lost her job due to lack of available work, but when she tried to claim on the PPI she was told that she was not eligible as she was an agency worker.

A CAB in Somerset saw a man and woman who had recently separated. While they were a couple they had taken out a joint loan to consolidate their debt. The loan was for £66,500 to be repaid over a 25 year term. They also took out a PPI policy in respect of the loan with a premium of £16,591. The woman was first named on the loan and insurance policy. The clients were under the impression that the insurance would cover the term of the loan (25yrs) and would cover them both on death, injury, and unemployment. However the small print in a tiny box on the loan application stated that the cover was for 5 years only, and covered both clients in the event of a death but only the first named client for illness and employment. The clients said they felt rather stupid for not realising that the premium was high and that they had not read the small print more carefully. However at the time they had taken out the loan they were very distressed and were relieved to find a company that said it could solve their debt problem by a quick phone call.

Further work by the FSA might well be needed to reduce instances of severe mis-selling such as these. However the FSA do not have a remit to address the key cost and product content problems raised in points one and two above, even though these are central to the problems consumers face with PPI, including the problem of mis-selling (where exclusion clauses are often identified is the key problem by CAB clients). Moreover, the evidence above also suggests that an approach based solely or mainly on trying to change consumer behaviour by requiring distributors to provide better and more transparent information at the point of sale may meet with limited success, particularly amongst more vulnerable borrowers. CAB evidence consistently shows how the consumer protection benefits of pre contractual information can be undone by poor sales practices.

Therefore it is hard to be optimistic that that a main focus on the way that consumers behave when 'shopping' for PPI will significantly improve the quality of decision making by consumers at the point of sale. It also seems unlikely that consumers will be easily encouraged or indeed assisted to shop around among different suppliers to get a better deal.

So, with consumers able to exercise limited influence on the cost and quality of PPI policies and no current direct regulation of these issues in place it therefore seems that lenders or insurers are currently free to decide on cost and content issues for themselves. Indeed, the working paper on the PPI value chain is clear in highlighting that it is in fact distributors (and more specifically lenders) who are largely responsible for setting the price and terms of PPI policies. Furthermore, the working paper on the underwriting market points out that lenders have considerable buying power and use this to set the terms of trade with underwriters in the upstream market. This seems to confirm the point we made *Protection racket* that lenders could sell better and certainly cheaper (for the consumer) PPI policies if they choose to do so.

From this perspective we would argue that the key focus of this inquiry should be on the way that lenders are currently behaving in PPI markets and how this can be addressed to produce better outcomes for consumers. However, there is no clear sense of this in the emerging thinking document. This states that the Competition Commission does not propose to pursue further analysis or inquiry into the underwriting market. Citizens Advice would therefore be grateful for further clarification as to what this means for the forward work of the Commission's inquiry. We are deeply concerned that this might mean that the Competition Commission has already ruled out possible remedies aimed directly at the proportion of premiums that lenders award themselves or at the way that lenders design policy content that does not meet customer needs.

The emerging thinking document suggests that ongoing focus of the enquiry will be on the retail market for PPI, but it is not clear how the next stage of investigation will address what we believe to be the central question of the lender behaviour. Perhaps the exception to this is the question raised on cross-subsidy; whether profits from PPI are being used to help push credit

APRs to abnormally low levels. We would agree with the Competition Commission that this is an important question and would challenge any industry assertion that such cross-subsidisation is not a problem in the context of a credit / PPI 'bundle'. Far from forming a product bundle with a single transferable shared cost,, the price of credit and PPI clearly present opposing incentives from a consumer point of view. The price of credit helps determine consumer's exposure to credit risk and the price of PPI might (at least in theory) help determine how well consumers protect themselves against those risks. Clearly if the cost of credit is artificially low, then there is the danger of consumers taking on more credit than they otherwise might have done. Likewise if the price of PPI is artificially high, consumers will not take on enough protection against debt.

This is clearly important in the context of the large number of consumers currently experiencing debt problems. Indeed the CAB service dealt with around 1.7 million problem debts in the year 2006/07, a number that has doubled over the last ten years. Some 900,000 of these were consumer credit debt that could have been covered by PPI. Citizens Advice has argued for some time that the credit industry needs to think harder about how people might be better prevented from falling into debt. A practice of over pricing PPI to subsidise lending would seem to do very much the opposite.

If the Competition Commission's final report were to find significant evidence of such cross subsidisation, this should be a matter of grave concern to public policy makers as it questions the extent to which lenders have been mindful of their responsibilities towards preventing debt problems from arising. However, such a finding by itself, does not address the actual problems of the cost and content of PPI policies. Therefore we are concerned that the focus on the PPI retail market from this point forward should not concentrate solely or mainly on the way that consumers behave when shopping for PPI. We have argued above that such efforts might meet with very limited success and in consequence will we take this opportunity to restate our belief that the key problem to be addressed is the behaviour of lenders in the PPI market. Unless this is addressed any outcomes from the PPI Market Inquiry are likely to be something or a missed opportunity.