

GENWORTH FINANCIAL

COMPETITION COMMISSION INQUIRY INTO PAYMENT PROTECTION INSURANCE

EMERGING THINKING

1 INTRODUCTION

- 1.1 We refer to the Emerging Thinking Document and supporting working papers published by the Competition Commission (the "Commission") on 6 November 2007, and Ms. Knap's email of 5 November inviting substantive comments on the same. This response is made on behalf of Genworth Financial ("Genworth") and sets out some initial comments on the Commission's emerging thinking. It should be read in conjunction with a separate response on behalf of Genworth on various vertical integration issues. Genworth reserves the right to provide further comments on the issues discussed in this response together with comments on other matters raised in the Emerging Thinking document that are not addressed in this response.
- 1.2 This response first considers the value of the PPI product, then makes suggestions in relation to the particular topics for which the Commission has indicated it is seeking further evidence, and finally provides substantive comments on some of the thoughts that have been set out in the Emerging Thinking document as well as the factors that should be taken into account when considering possible remedies.

2 VALUE OF THE PPI PRODUCT

- 2.1 As an overarching comment, Genworth is concerned that the Emerging Thinking document seems to have somewhat overlooked the value of the PPI product. The submissions that Genworth has made in this regard, as well the OFT's and FSA's own acknowledgements of the benefits of PPI, do not seem to have been expressly recognised in the Emerging Thinking document. It would be unfortunate if subsequent documents published by the Commission did not recognise the underlying value of the product.
- 2.2 Genworth would again strongly emphasise the inherent value in PPI to consumers as a product that provides worthwhile cover against unforeseen events that cause repayment difficulties. PPI can offer valuable peace of mind for consumers - evidenced by the high levels of satisfaction expressed by respondents in consumer surveys¹ - and can provide a valuable safety net to enable consumers to maintain important loan commitments such as a house or a car, in the event of an unexpected illness or job loss. It can also act to safeguard a consumer's credit status.
- 2.3 The true value of PPI is only seen when there are downturns in the economy; Genworth has previously pointed to the significant increase it saw in the number of

¹ An estimate made by the ABI in 2002 suggested that in the region of 85-90% of claims were accepted that year. Results from an ABI initiative launched in 2002 (Creditor Insurance Claims Benchmarking) suggested that, over the last three years, satisfaction on accepted claims were consistently over 85% and in 2004/5 only 833 claims were received by the Financial Ombudsman service, suggesting that less than 2 in a thousand claims result in a FOS complaint. This seems consistent with the reports referred to by the Commission in its Emerging Thinking, which suggest that the majority of consumers choose to purchase PPI because it gives them peace of mind (paragraph 15 of the Working Paper, Characteristics of Consumers of PPI). Furthermore, surveys relied on by the Commission in considering the reasons for purchasing PPI point to the fact that some consumers consider it to be good value for money and the majority of respondents were satisfied with the cost of the policy and the extra amount it added to their monthly payments (paragraph 16 of the same Working Paper).

[Please note that square brackets indicate figures or text which has been deleted for reasons of commercial confidentiality.]

new PPI claims and the duration of those during the last recession. There has not been a severe economic downturn in the last 15 years. However, with the current economic uncertainty, the highest ever levels of consumer debt, and relatively low levels of savings, we would urge the Commission to take this opportunity also to present the value of this product to consumers. We appreciate that the Commission is not tasked with “selling” PPI to consumers but it should at least present the benefits as well as the perceived shortcomings of the PPI product.

2.4 In this regard, we would highlight two particular statements which we do not think fairly represent PPI. Paragraph 13 of the Emerging Thinking document notes that “taking out PPI can entail a significant financial outlay; the price of PLPPI can be more than the interest payable on the loan.” This view should be put into context. First, the Commission should consider a more balanced picture could be presented by mentioning the price of the PPI relative to the size of the loan and the level of benefits that a policyholder receives under a PPI policy, for example, payment of their monthly loan repayments for a number of months or repayment of a loan following the death of a policy holder. Secondly, as we have mentioned previously, it is possible for distributors to cross-subsidise a lower APR on the credit product, by utilising profits made on PPI. Genworth believes that, in practice, this cross subsidisation does occur.

2.5 We would also point to paragraph 96 of the Emerging Thinking document, which notes that “it was put to us by Which? that a customer may end up paying interest on the premium even though they are no longer covered because the PPI policy covers a shorter period than the total loan period.” However, this seems to us to imply a rather unfair criticism of PPI and does not recognise that a significant number of PPI policies are monthly premium rather than single premium. For example, if a customer purchases a car with the assistance of a loan but then sells that car, the original debt is still outstanding and needs to be repaid. Similarly, a loan taken to pay for a holiday does not cease to be repayable once the holiday is over. The position with PPI is the same. A customer who wishes to purchase PPI borrows an additional amount in order to take out the PPI for a specified duration. Once the policy ends, the original loan will still be outstanding and the repayment premiums will continue until the amount borrowed is repaid (and the customer can choose to repay that loan at any time). Genworth also believes that insufficient value is placed by the Commission on the advantages that single premium PPI policies can offer to certain individuals, notably certainty of price and cover. Genworth notes from paragraph 99 of the Emerging Thinking document that the Commission intends to consider the extent to which single premium policies may be a barrier to switching. Genworth would urge the Commission to consider the advantages of single premium products and the recent changes relating to single premium rebates (discussed in paragraph 97 of the Emerging Thinking document) in its analysis.

3 FURTHER EVIDENCE

There are a number of issues in the Emerging Thinking document in relation to which the Commission has indicated it might find additional information helpful.

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3.1 Price variations

- 3.1.1 In paragraph 105, the Commission invites evidence to explain the appearance of (a) large price variations between what appear to be often very similar PPI policies, and (b) very little price variation for a given type of policy over time.
- 3.1.2 In Genworth's view, some of these price variations are due to factors such as the different populations being covered, differing distribution costs or commission levels.
- 3.1.3 However, Genworth believes that much of this is due to the lack of competition at the point of sale ("POS"). The POS advantage experienced by distributors significantly restricts the level of competitive pressure at the key point at which customers purchase insurance. Stand alone providers have difficulty accessing consumers and insurers are also unable to provide competitive pressure by selling direct to consumers. Whilst it is essential that the credit provider should continue to be allowed to sell PPI at the POS (as this is when consumers are most receptive to the product and its inherent value), the Commission should consider how consumers can be made aware of a greater choice of products and providers. This would increase the ability of consumers to compare prices across a range of PPI products and, ultimately, would increase price competition (and, indeed, innovation and service levels).

3.2 Consumer purchasing behaviour

- 3.2.1 In paragraphs 147 to 162 of the Emerging Thinking, the Commission considers whether PPI policies and their underlying credit products are in the same market: its current thinking, based on the balance of evidence received so far in the inquiry, is that they are not (paragraph 161).
- 3.2.2 Genworth agrees with this view. In particular;
- (i) the Commission's findings in paragraph 152 of the Emerging Thinking are consistent with Genworth's understanding of the position;
 - (ii) Genworth agrees with the view expressed by the Commission in paragraph 153 that there is an "asymmetric demand relationship between credit and PPI - with the price of credit affecting uptake of PPI but [the] price of PPI not impacting on the uptake of its underlying credit";
 - (iii) Genworth agrees with the results of the OFT's survey referred to in paragraph 154 namely, that "customers tend not actively to seek out information on PPI, nor do they shop around, particularly by comparison to the way they shop for credit";
 - (iv) the Commission's finding (in paragraph 157) that "firms do not perceive that an increase in PPI prices will affect their credit sales", is consistent with Genworth's understanding; and
 - (v) the findings of the quantitative research by BMRB referred to in paragraph 159 are consistent with Genworth's understanding i.e. that "in general participants had not thought at all about insurance protection when they chose their credit provider", and "in general, PPI was seen as an "add on" to the credit product, only considered once the choice of loan provider had been made and the credit application had been started".

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Competitive interaction between PPI distributors.

- 3.2.3 In paragraphs 163 to 176 of the Emerging Thinking, the Commission considers the extent to which different distributors (or brands) of PPI, or PPI and credit, constrain each other. Its current thinking, based on the evidence seen to date, suggests to the Commission that it would “seem appropriate to define a series of individual markets such that each PPI distributor has a monopoly over its own credit customers at the point of sale” (paragraph 175).
- 3.2.4 Genworth agrees with this view. In particular:
- (i) it is also Genworth’s understanding that distributors “set their PPI prices relative to the PPI prices of others, with a view to avoiding being out of line by charging a bit more or less than the providers”, rather than to “undercut their competitors”, (paragraph 165); and
 - (ii) it is also Genworth’s understanding that “the vast majority of PPI sales are made at the point of sale of the underlying credit product, and that individual distributors do not compete to win each others’ point of sale customers”.

4 SUBSTANTIVE COMMENTS ON THE COMMISSION’S THINKING

4.1 The Underwriting Market

- 4.1.1 Genworth welcomes the Commission’s conclusion that there is no evidence to suggest that there are features, which prevent, restrict or distort competition in the underwriting market to a significant extent. []
- 4.1.2 []
- 4.1.3 []
- 4.1.4 The Commission finds evidence that integrated underwriters place a competitive constraint on independent insurers but notes (paragraph 30 of the Working Paper on the Underwriting Market) that there is less evidence that independents impose a constraint on integrated insurers. The Commission comments that there appear to be very few examples of integrated distributors switching to independent underwriters in practice. []
- 4.1.5 With this in mind, Genworth believes that certain parallels could be drawn between this market structure and that found by the Commission when examining the UK grocery retailing market. The Commission’s approach to defining grocery markets (as explained in its Provisional Findings) seems to us to more accurately reflect the situation here, in that this approach recognises that there may be an imbalance in the competitive constraints different types of provider place on each other. For example, the Commission recognises that large grocery stores compete with mid-range stores, but not generally vice versa (note, the Commission did not find that mid-range stores posed no competitive constraint on large grocery stores whatsoever). Hence, the Commission’s analysis of large and mid-range stores resulted in it identifying two separate grocery retailing markets: one for large stores, and one for large stores *and* mid-range stores. [] We would note that approximately half of the large underwriters in the market are part of a vertically integrated group (Underwriting Working Paper, paragraph 4), which account for a significant part (60%) of overall PPI sales []. (Essentially the PPI business of the UK’s main high street banks:

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Barclays, HSBC, HBOS, RBS and Lloyds TSB.) Genworth would therefore submit that there are currently two separate underwriting markets []

4.1.6 []

4.2 Conditionality

4.2.1 Genworth notes that the Commission has not explored in any detail the suggested introduction of some form of conditionality in relation to PPI. The proposal is that it should be made clear that lenders should be allowed to require PPI as a condition of providing a loan or mortgage, although consumers would not be obliged to purchase PPI from that lender. A form of this has already been introduced in relation to similar products, e.g. building insurance in relation to mortgages and travel insurance. Genworth has also highlighted to the Commission that conditionality in relation to mortgage PPI is an established and recognised practice in France. Genworth recognises that lenders may only wish to do this for certain types of loans and that it may be subject to exclusions (for example, the self-employed should not be required to take out employment cover).

4.2.2 There would be a number of benefits to allowing lenders to require PPI as a condition of providing a loan or mortgage. It would encourage greater personal responsibility by consumers in relation to their borrowings and would reduce the lenders' exposure to bad debts and non-payment. Reduced risk should, in turn, lower prices to consumers and would help protect the financial system from the adverse impact of large scale loan and mortgage defaults. It would bring down costs (through scale) and enhance competition. It would also provide a new platform for stand alone providers to enter the market and compete for new business. Moreover, a degree of conditionality is also in line with the Government's policy objectives of encouraging sustainable home ownership² and promoting responsible borrowing by individuals.

4.2.3 Genworth suspects that one possible reason why banks do not require some form of PPI cover to protect loans is because of a perception that it is restricted by competition law. Genworth would urge the Commission to make a clear statement that banks are, in fact, free to require this. At present, the position is unclear.

4.3 Alternative products

4.3.1 Genworth notes that the Commission considers there to be "little demand-side substitutability between PPI and potential financial insurance products" (paragraph 180 of the Emerging Thinking document). Genworth agrees and believes there are valid reasons for this, with the key ones being:

- (i) Not all of the potential alternative products cited by the Commission protect the same risks as PPI products. For example, life insurance products do not incorporate cover for unemployment.
- (ii) Some PPI products incorporate elements of the alternative products, for example, some PPI policies contain life and/or critical illness covers.
- (iii) PPI is commonly sold at the same time as the underlying credit product as it is at this point that consumers' need for protection is greatest. PPI is

² In 2000 when the Government launched its Sustainable Home Ownership Initiative, it set a target of 55% of new mortgages being protected by mortgage PPI products. According to figures collected by the CML, just 22% of new mortgages in 2006 were protected by mortgage PPI.

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generally not an individually underwritten product so can be sold effectively as point of sale. All of the alternative products cited by the Commission tend to be individually underwritten so it is not practical to sell them at the point of sale of a credit product.

- 4.3.2 Genworth believes that the alternative products cited by the Commission should be viewed as complementary products not potential substitutes. Accordingly, Genworth does not think that the Commission should consider the availability of these products in reaching its conclusions on the PPI market.

5 REMEDIES

- 5.1 Genworth appreciates that the Commission's thinking on any possible remedies is still at an early stage. However, Genworth felt it would be helpful to set out the following key factors which the Commission should consider as it develops its thinking on the need for remedies and the scope of any possible remedies.

- 5.1.1 It is essential that in considering possible remedies, the Commission has regard to the unintended consequences any remedies may have. Genworth strongly believes that any de-linking of the sale of PPI products from the sale of the underlying credit product would significantly reduce access to PPI products. As noted above, PPI is a valuable product and easy access to it by consumers should not be discouraged as reduced take-up of PPI products has negative implications for competition and/or individuals, the Government and the wider economy.

- 5.1.2 There are extensive industry initiatives being delivered aimed at improving the PPI market and increasing transparency and consumer choice. These include a commitment not to apply nil refund terms in single premium products and the launch of the ABI consumer guide to PPI and guide to protection products.³

- 5.1.3 As the Commission will be aware, the FSA is currently reviewing the existing Insurance Conduct of Business Rules and is currently proposing to enhance the existing rules applicable to PPI products. Genworth believes that, if implemented, these new rules will address a significant number of the problems identified in the PPI market. The FSA is also planning to publish comparative tables on PPI in March 2008. These tables will help consumers "shop around" and switch PPI products.

- 5.1.4 The PPI market is facing greater empowerment of consumers resulting from the growing availability of information and products on the internet and the growth of alternative distribution channels such as intermediaries. The PPI market will need to adapt to these changing market conditions and Genworth believes that this will result in more consumer focused products, greater consumer choice of products and providers and enhanced competition.

- 5.2 All of the factors identified in paragraphs 5.1.2-5.1.4 above will take some time to have a positive impact on the PPI market. Genworth would therefore urge the Commission to consider each of these and the time that is needed for them to have a positive impact when considering the need for any further remedies. It is also important that any remedies are proportionate and do not lead to a duplication of regulation.

³ Genworth understands that the ABI's response to the Emerging Thinking document contains further details of these initiatives.

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6 CONFIDENTIALITY

- 6.1 This response has been excised to delete information that is confidential. In order to assist the Commission, Genworth provided confidential information in its response. This included Genworth's views of the market in which it operates, which are not in the public domain, and the disclosure of which were likely to be prejudicial to Genworth's commercial interests.
- 6.2 If the Commission receives a request (including, but not limited to, a request under the Freedom of Information Act 2000 ("FOIA") (or similar legislation) to disclose any information contained in this confidential response, Genworth would ask that the Commission (in accordance with Part IV of the Access Code under section 45 of FOIA) promptly consults with, and takes into account any comments from Genworth prior to making any disclosure, and works with Genworth to ensure that any exemptions or other legitimate means of preventing or limiting disclosure are used to the fullest extent necessary to protect Genworth from prejudice to its commercial interests.

**SJ Berwin LLP
27 November 2007**