

Competition Commission Inquiry into Payment Protection Insurance

Position Paper - 2 March 2007

Cattles plc

1. Introduction

- 1.1 Cattles plc ("**Cattles**") is a listed FTSE 200 company with a market capitalisation of around £1.4 billion. Cattles is based in Leeds and operates throughout the UK providing non-standard financial services.
- 1.2 Cattles specialises in providing financial services to non-standard consumers who either choose not to or do not have access to mainstream credit facilities. Cattles believes that the availability of the non-standard financial services offered by Cattles is crucial to non-standard consumers both in terms of meeting their credit needs and enabling those consumers to rebuild their credit history and gain access to mainstream services should they wish to do so. Cattles considers that Payment Protection Insurance ("**PPI**") plays an important role in enabling its customers to rehabilitate their finances.
- 1.3 Cattles employs approximately 5,000 people across the UK in its central lending units and in its network of branches which are located close to Cattles' customers.
- 1.4 Cattles is a member of several UK Trade Associations that represent the consumer credit industry including the Finance and Leasing Association ("**FLA**"), the Consumer Credit Trade Association ("**CCTA**") and the Consumer Credit Association ("**CCA**").

2. Executive Summary

- 2.1 Cattles considers that there are a number of factors which should be taken into account by the Competition Commission (the "**Commission**") throughout its inquiry. Cattles' position is summarised as follows:

- 2.1.1 First, Cattles considers that many aspects of the OFT's report¹ and criticisms of the PPI market are not well supported and do not apply to the way in which Cattles provides PPI.
- 2.1.2 Cattles provides good value PPI policies on terms which are fair to the consumer. In particular it should be noted that Cattles' policies do not exclude pre-existing medical conditions including back pain and mental illness.
- 2.1.3 Cattles is committed to providing a high quality service to its customers and seeks to compete with other lenders on both the price and the terms of its PPI policies in order to attract new business and ensure that its existing customers are satisfied.
- 2.1.4 PPI is an important product that is valued by consumers. This is demonstrated by the OFT's own research, the FSA and is acknowledged in the OFT's report.
- 2.1.5 Cattles believes that the behaviour and characteristics of non-standard finance customers and their payment profiles have implications for PPI products sold to those consumers that were not acknowledged by the OFT and which should be taken into consideration in this inquiry.
- 2.1.6 Cattles considers that non-standard PPI constitutes a distinct segment of the market and that this segment is more competitive and better value for the consumer than some other mainstream products and that this fact should be reflected in Commission's analysis.
- 2.1.7 As stated above, PPI is an important and valued product for all UK consumers; Cattles believes it is of particular importance for Cattles customers and for all customers of non-standard finance. Cattles' customers, as non-standard finance customers are amongst the most likely to experience periods of fluctuating income patterns and less secure employment and, therefore, have a greater need for PPI than consumers of mainstream PPI.

¹ Payment Protection Insurance - The OFT's reason for making a market investigation reference to the Competition Commission February 2007, (the "OFT Report")

2.1.8 Cattles considers that the OFT has misunderstood and misrepresented the levels of competition in the PPI market and, in particular:

2.1.8.1 Cattles does not accept the OFT's analysis of the relative value of different types of insurance and, in particular, consider that the claims ratio analysis is flawed.

2.1.8.2 Cattles also considers that the OFT has underestimated the competitive constraint imposed by stand alone lenders; and

2.1.8.3 failed to acknowledge the existence of strong competition for the supply of PPI policies on the upstream market and that the cost savings which are subsequently passed on to consumers.

3. Cattles' PPI Policies

3.1 As will be seen from the information to be submitted in response to the Commission's request of 7 February 2007, Cattles sells Norwich Union PPI policies to its direct debit loan customers². Cattles' customers enter into the contract with Norwich Union directly and claims are handled by a third party.

3.2 In selling the product, Cattles complies with applicable regulatory requirements. PPI is regulated by the Financial Services Authority ("FSA") and as such, Cattles delivers the product to its customers in a clear and transparent manner in accordance with the appropriate Insurance Conduct of Business Rules ("ICOB"). The delivery process is audited on a regular basis.

3.3 All Cattles' employees who have contact with customers are trained and accredited to sell PPI in line with FSA regulation. All Cattles' PPI customers are provided with all necessary information in a clear and transparent manner; customers have ample opportunity to review the terms and costs of the policy and are able to cancel the policy in the cooling off period if they wish.

3.4 PPI is always presented as an optional insurance product and does not affect the acceptance of the loan application. Cattles does not discuss PPI with

² i.e. not home credit customers.

customers until the process for the sale of the loan is completed and so there is no scope for customers mistakenly thinking that the purchase of PPI will increase the chance of a successful loan application.

- 3.5 Cattles regularly reviews its products by comparison with competing products and in response to customer demand. Cattles has recently revised its policies to enable customers to claim for periods of illness which are due to pre-existing medical conditions including back ailments and mental illness (including stress and nervous disability).
- 3.6 It is suggested that some lenders offer low cost credit on their loans in order to attract customers who are subsequently sold high cost PPI policies. Cattles does not operate any such strategy and sets the APR on its loans by reference to cost and does not use APR as a tool for selling PPI.
- 3.7 Cattles provides single premium PPI to its customers so the customer is protected throughout the life of the loan. As discussed below, Cattles' customers are more likely than mainstream finance customers to miss monthly repayments and experience periods of financial difficulty which may lead to missed repayments.
- 3.8 Cattles considers that monthly repayment policies would not be appropriate to the majority of Cattles customers who may default on the payments which would result in higher costs for Cattles which could in turn result in an increase in the price of Cattles' PPI. Customers who defaulted on PPI payments may also forfeit their right to claim under the policy and loan repayments would not be protected.
- 3.9 Cattles believes that the terms of its PPI policies offer effective payment protection and are tailored to meet the particular needs of its customers. Cattles believes its policies are both highly competitive and good value for consumers.

4. PPI is a product valued by consumers

- 4.1 The OFT recognises that PPI can provide "worthwhile cover against unforeseen events that cause repayment difficulties and it can offer valuable peace of mind whether or not a claim is made".³
- 4.2 Cattles agrees with this statement and it is clear from the volume of policies bought by UK consumers that there is demand for PPI in order to protect loan repayments in the event that a borrower experiences a change in their financial circumstances.
- 4.3 Customer satisfaction with PPI is demonstrated by Cattles own customer surveys and the fact that Cattles does not receive significant numbers of complaints regarding PPI.
- 4.4 Cattles considers that the OFT has failed to acknowledge the extent of customer satisfaction which was demonstrated in its own consumer research⁴. Key points of note are:
- 4.4.1 61% of respondents agreed that PPI is value for money⁵;
- 4.4.2 87% of respondents agreed it gives peace of mind⁶;
- 4.4.3 89% of respondents felt they had been given useful information beforehand, which enabled them to make an informed decision about which product to take out⁷;
- 4.4.4 75% of respondents said that the sales person advised them of the cost of the insurance separately to their repayments and interest⁸;
- 4.4.5 a very high proportion of respondents, 94%, were satisfied with their PPI policy overall⁹.
- 4.5 PPI is of particular value to Cattles customers as they are most likely to require this type of cover as discussed below.

5. Non standard finance PPI

³ The OFT Report, paragraph 1.3.

⁴ Annexe B to the Payment Protection Insurance Report on the market study and proposed decision to make a market investigation reference October 2006, Research into Consumers' Experience of Payment Protection Insurance: A research report for The Office of Fair Trading, October 2006 (the "OFT's consumer research")

⁵ OFT consumer research, chart 10.

⁶ OFT consumer research, chart 8.

⁷ OFT consumer research, page 28.

⁸ OFT consumer research, page 38.

⁹ OFT consumer research, page 45

- 5.1 Cattles specialises in offering finance to non-standard finance consumers who may not be able to secure standard finance, for example from the high street banks, because of CCJs, mortgage arrears or other credit problems. Cattles provides both secured, unsecured and hire purchase loans through its Welcome Financial Services ("**WFS**") brand which are repayable by monthly direct debit.
- 5.2 Cattles also owns the Shopacheck Financial Services brand which provides home credit loans. Cattles does not provide PPI on its home credit loans and so the Shopacheck brand is not relevant to the Commission's inquiry.
- 5.3 WFS has over 400,000 customers and provides:
- 5.3.1 unsecured loans; the average advance to new customers is £1,800;
 - 5.3.2 secured loans; the average advance to new customers is £8,700; and
 - 5.3.3 hire purchase loans; the average advance to new customers is around £5,800.
- 5.4 WFS customers are typically from socio-economic groups C2 or D and are even more unlikely than the average consumer to have sufficient savings to cover periods of financial difficulty. WFS customers are also unlikely to have family members able to support them during these periods.
- 5.5 Accordingly, Cattles considers that PPI is of utmost importance to its customers who are amongst the most likely to rely on payment protection insurance.
- 5.6 Cattles customers frequently experience periods of, often temporary, financial instability. During these times, payment protection insurance policies enable them to avoid falling into arrears on their loan repayments. For these reasons, Cattles customers have an increased need for payment protection insurance.

6. The importance of acknowledging non-standard PPI in the Commission's inquiry

- 6.1 The OFT at paragraph 4.36 of its report states that it considered the possibility of "*non-prime' credit sold by lenders other than banks being a*

separate market." and refers to *"different customer behaviours and motives for buying"*. Regrettably, however, the OFT did not develop its analysis of this point and the question of what implications these differences may have on the structure of the non-standard PPI segment is simply not dealt with.

- 6.2 Whilst Cattles does not consider that sub-prime or non-standard PPI constitutes a different market, Cattles does consider that the differences discussed above and acknowledged by the OFT should be taken into account by the Commission throughout this inquiry and in its report.
- 6.3 Conclusions and assumptions which may be appropriate to the standard finance PPI market and consumers and may not apply to non-standard consumers. Accordingly, Cattles submits that it would not be appropriate for the Commission to take a uniform approach to the whole of the PPI market in its analysis and disregard the distinction between the non-standard and mainstream segments.

7. The OFT report

- 7.1 Cattles disagrees with the conclusions drawn by the OFT that PPI is a poor value product. Cattles considers that certain aspects of the OFT's analysis of the PPI market were flawed. In particular, Cattles submits that the OFT was wrong in its approach to the following issues:

Claims ratio is a poor comparator

- 7.2 The OFT argues that PPI policies are poor value for the consumer on the ground that PPI claims ratios are low when compared with claims ratios for other types of insurance. Cattles does not accept that the claims ratio is a valid basis for comparison for the following reasons.
- 7.3 It is clear that different types of insurance form distinct and entirely separate markets. These markets have different structures, different regulatory regimes and the different types of insurance meet different needs. Consumers are motivated by different considerations when purchasing different types of insurance and these factors result in different levels of claims ratio.
- 7.4 The OFT cites the claims ratios in the motor insurance industry as indicating that motor insurance is better value for the consumer than PPI insurance.

Cattles considers that such a simplistic comparison between entirely different products and markets is not meaningful.

- 7.5 Motorists are required by law to take out motor insurance and as such, consumers do not have the freedom to choose whether or not to insure themselves against such risks and so every motoring accident results in a claim; this is not the case for PPI. The factors which influence the levels of claims in the motor industry have no bearing on the levels of claims under PPI policies and vice versa. These differences mean that it is not possible to draw meaningful comparisons between PPI insurance and motor insurance.
- 7.6 Cattles submits that the Commission cannot use claims ratios as a means of comparing the competitive condition on the market unless it undertakes an assessment of each of the comparator markets to determine what factors determine the level of claims and to determine whether the competitive conditions on that market are desirable.
- 7.7 For example, in the case of the motor industry, which the OFT cites as a good value, it is clear that this industry is currently suffering serious losses and could not be described as a 'healthy market'.
- 7.8 According to the Datamonitor report "UK Motor Insurance 2005 'Going into reverse'", the UK motor insurance market is not expected to be profitable until 2010 and, in 2007, an underwriting loss of £326 million is predicted.
- 7.9 Cattles submits that it is not appropriate to suggest that PPI claims ratios should be adversely compared with claims ratios for the motor insurance industry when that industry is suffering serious losses.

Independent suppliers are an effective competitive constraint

- 7.10 Independent 'stand alone' insurers do exert a competitive constraint and, Cattles believes, will continue to consolidate their position on the market. Cattles considers that PPI customers can and do switch their policies from those sold by their loan provider to stand alone providers.
- 7.11 Cattles considers that the current regulatory environment and media focus on PPI will result in an increase in consumers seeking policies from independent

lenders. A simple internet search¹⁰ reveals a range of providers offering standalone cover and websites comparing financial products.

7.12 Cattles considers that the increase in new stand alone entrants on the market is indicative of both the extent to which stand alone providers act as a competitive constraint on other lenders, and the extent of competition on the PPI market as a whole.

Competition on the upstream market for the supply of insurance

7.13 The OFT in its report entirely disregards the fact that there is vigorous competition at the level of the supply of PPI to lenders. Cattles periodically reviews the terms of its PPI supply and would switch provider if it were commercially beneficial. Cattles always negotiates with providers in order to secure the best price from suppliers. This upstream competition results in lower costs for consumers and is a further illustration of the competitiveness of the PPI market.

8. Conclusion

8.1 Cattles asks that the Commission take into consideration the particular characteristics of the non-standard PPI segment throughout the inquiry and that the needs of Cattles' consumers are considered with equal weight to those of mainstream credit consumers. The Datamonitor UK non-standard and sub-prime consumer credit 2006 report "Challenges ahead" published in June 2006 estimated that the UK non-standard population of working age stood at 9.1 million and will increase to 9.42 million (25.6% of the adult population of working age) by 2010.

8.2 Cattles would be delighted to meet with the Commission to discuss these issues in more depth at a later stage of the inquiry.

¹⁰ Typing "PPI" into google reveals paymentcare.co.uk; britishinsurance.com; antinsurance.co.uk; and moneysavingexpert.co.uk as the top 4 sponsored links.