Protection racket

CAB evidence on the cost and effectiveness of payment protection insurance

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1. Introduction

1.1 Anyone can lose their job, fall ill or experience bereavement or the breakdown of a relationship at almost any time. A change in circumstances can lead to a dramatic and sometimes permanent fall in income. For those people with outstanding credit agreements a cut in income raises the serious possibility of unmanageable debt. None of us have perfect foresight and so credit carries an inherent risk of falling into debt.

1.2 It is not therefore surprising that a large payment protection insurance (PPI) industry has developed to help borrowers offset the credit risk they face. A DTI – led working party concluded that PPI can "provide valuable protection against changes in a consumer's financial circumstances.[1] Industry estimates for the UK PPI market put the number of live policies at around 20 million, with between 6.5 and 7.5 million new policies being taken out each year. PPI premiums are said to total approximately £5.3 billion per year.[2] In comparison, property insurance premiums total £8 billion and motor insurance £9.5 billion.[3]

1.3 In recent years the number of claims made on policies each year has been significantly lower than the number of new policies taken out. Figures from 2002 estimate 450,000 new claims each year, around one claim for every 15 policies taken out (or seven per cent), meeting the cost of 2.5 million monthly loan instalments[4]. However, insurance industry figures show that around 85 per cent of PPI claims are approved. This relates to a period of relatively benign economic conditions when insurers have faced a period of low risk.

1.4 However, the scale and extent of PPI does not necessarily mean that PPI products provide consumers with good value for money, or that the market is working well for consumers. Most borrowers purchase PPI linked to the credit product. Borrowers enter into these *secondary sales* with little opportunity to shop around and no real choice. As the Financial Services Authority (FSA) has pointed out, there is a danger that secondary sales lead to customers buying products that are poor value[5].

1.5 Stories of the credit industry making large, even excessive, profits from PPI premiums and commission regularly appear in the finance press. For instance the Guardian reported that Barclays made £240 million from PPI sales in 2000/01, with a margin of 70 per cent on payments made by consumers.[6] Lloyds TSB plc report income in 2004 from creditor insurance premiums of £114 million and commissions from broking creditor insurance at

[1] *Review of the Consumer Credit Act: progress report,* DTI, August 2002
[2] Figures supplied by the Association of British Insurers, August 2005
[3] *UK insurance - key facts*, Association of British Insurers (2004)
[4] *Regulation of General Insurance – Creditor Insurance – An industry approach to consultation*, ABI, BBA, BRC, CCTA, CML, FLA, Protect and Retail Motor Industry Federation, 2002
[5] *CP 160 Insurance selling and administration-the FSA's level approach to regulation;* Financial Services Authority, 2002
[6] *The Guardian*, Saturday March 6 2004

£377 million.[7] The report comments that overall general insurance broking commission had fallen reflecting lower profit sharing income from other insurance broking. However at the same time income from creditor insurance increased by £26 million. Our analysis of six fairly widely available policies suggests that borrowers could spend as much as £85 over a year to obtain only a £12 reduction in their debt in a similar period. Two different estimates suggest that PPI premiums are about three times the cost of providing cover. This implies that borrowers could be overcharged by as much as £3 billion per year for PPI cover.

1.6 CAB evidence suggests that both the sales process and design of PPI products fail to meet the needs of many CAB clients and often just increases their indebtedness. A survey of CAB debt clients in 2001 found significant limitations of PPI in resolving debt problems when they arise.[8] In cases where our clients had PPI on their lending, the limitations of the policy held meant that clients could only make claims for just over a quarter of these debts. The most commonly cited reason (73 per cent of those not claiming) for not claiming on the policy was that there was no ability to claim, for example because the client was in debt due to a relationship breakdown. In those cases our clients had paid for insurance that did not meet their needs. Even when a claim is made, few CAB clients surveyed were successful. Claims were not successful in 85 per cent of those cases where the credit had PPI cover and a claim was made.

1.7 These figures contradict claims by the creditor insurance industry who state that 85% of PPI claims are successful.[9] But CAB clients are more likely to be on low and sometimes unstable incomes and to experience health problems than the general UK population.[10] This suggests that PPI products fail the most vulnerable in society, i.e. those who are most in need of the protection it offers.

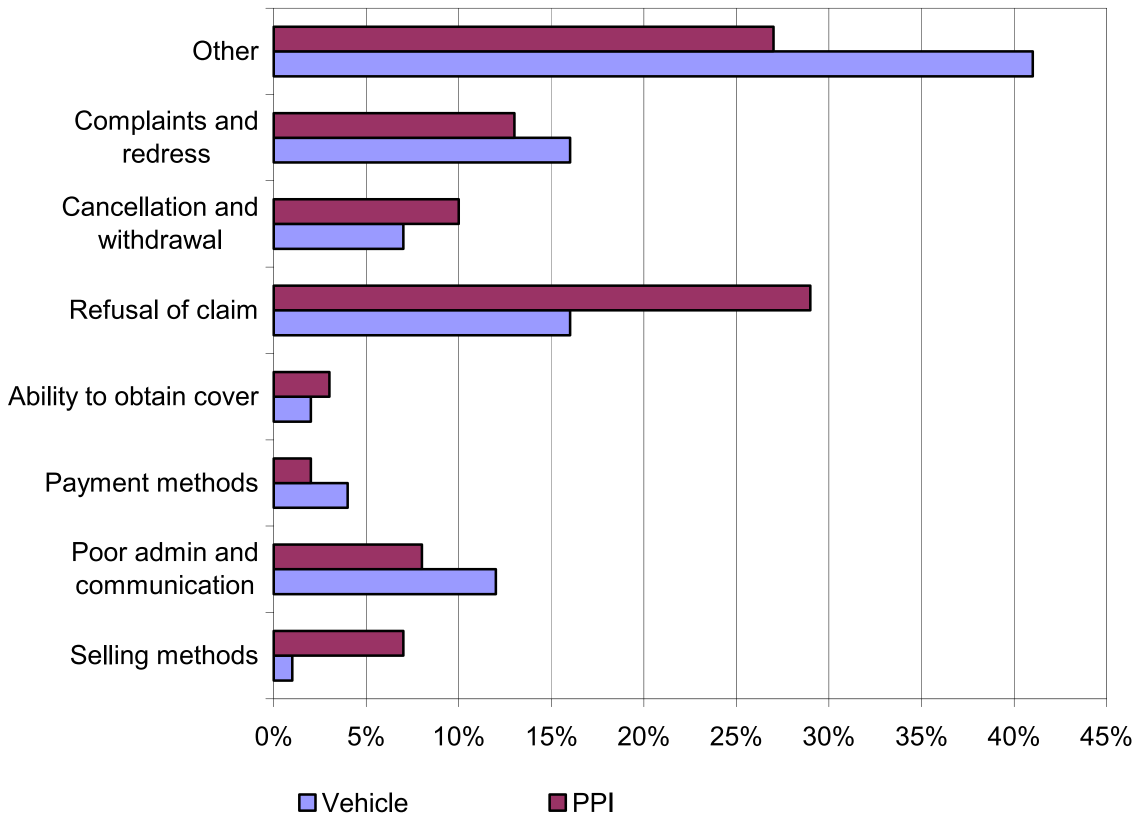
1.8 CAB enquiry statistics show how PPI fails our client group. Table 1.1 shows that the profile of CAB client problems about payment protection insurance differs in a number of respects from that of CAB enquiries about car insurance. CAB clients enquiring about PPI problems are twice as likely to have had a claim refused as clients enquiring about motor insurance.

1.9 A case reported by one CAB shows how these problems of high cost insurance and barriers to claiming can combine to produce devastating consequences for borrowers:

A widow in receipt of pension credit sought advice from a CAB in Lincolnshire about debts of £27,000 to seven creditors. The client had got into debt when she moved to be nearer her adult children. The moves were expensive, so

[7] *2004 results,* Lloyds TSB Group plc (2005)
[8] *In too deep – CAB clients' experience of debt,* Citizens Advice, 2003
[9] Presentation by Protect to Citizens Advice, December 2004
[10] *Unmet need for Citizens Advice Bureaux,* MORI, 2004

Table 1.1: A comparison of CAB enquiries about PPI and vehicle insurance in first quarter of 2005 - 06



Base: 350 enquiries about payment protection insurance and 653 enquiries about vehicle insurance made to 73 Citizens Advice Bureaux in England and Wales from 1 April to 30 June 2005.

she asked her bank for loans. The bank lent her £14,500 and insisted that she took out payment protection insurance even though she was in receipt of benefits and would not be able to claim on the insurance. This increased the debt to £16,500. The total repayments were £304 per month, leaving her only £160 per month to live on. As a result the client:

- had to take on an ironing job at £10 per week to pay for food
- used her credit cards to make ends meet, thus increasing her debt
- could no longer afford to heat her small bungalow
- had to give up her involvement with the local Women's Institute, her only social activity, because she could not afford to go on the trips they arranged, and
- was worrying endlessly about all the letters she was receiving from her creditors, particularly her bank.

At the time she sought advice, the client had developed heart problems and was contemplating suicide as the only way to get out of her financial difficulties.

1.10 Unmanageable debt is not just a problem faced by individuals, but also has a wider social cost. For instance the Department of Trade and Industry estimates that the cost of output lost through the reduced productivity of over-indebted individuals could be as high as one per cent of GDP.[11] This makes a compelling case for insurers, creditors and government to ensure that there is an accessible, affordable and effective safety net for borrowers against the risk of debt.

1.11 Citizens Advice also considers that more concerted action from the relevant market regulators is necessary. The failure of PPI points to a regulatory gap. A wide-ranging review of the role and nature of payment protection insurance in the UK consumer credit market is now essential and urgent.

About this report

1.12 This report is based on an analysis of 564 cases submitted by 269 Citizens Advice Bureaux in England, Wales and Northern Ireland for the period January 2004 to April 2005. Chapter two looks at the costs of PPI and the benefits that borrowers can expect in return. Chapter three will present evidence on the risks that seem to be commonly excluded from PPI policies. Chapter four looks at the PPI selling process and reports from CAB clients who have been sold policies that were unsuitable for their needs. Chapter five highlights problems with the administration and adjudication of claims that have prevented CAB clients from benefiting from the policy they had purchased. The final chapter argues for regulatory action to produce a better safety net for borrowers.

[11] *Fair, clear and competitive – the consumer credit market in the 21st century*, Department of Trade and Industry, 2003

2. Is PPI good value for money?

2.1 All borrowers will be interested in whether their policy will provide them with good value for money. Because people shopping for credit are offered a single choice of PPI product on a take it or leave it basis, there is no information to make a judgement on the comparative worth of their purchase. We must take it on trust that our lender will make the best choice for us.

2.2 Lenders concerned with the welfare of their customers should therefore ensure that the PPI policy they provide, either through an in-house insurer or by commercial arrangement, are effective and competitive. Borrowers should receive a level of cover that genuinely protects them against indebtedness and the policy should perform at least as well as any other product on the market against objective measures such as:

- The number of benefits that the policy offers
- The cash or other value of these benefits and their duration
- The price borrowers must pay for cover.

2.3 If this were the case, PPI products should be fairly similar in their key attributes. Evidence presented previously showed how some PPI products give people cover against a wider range of risks than others, suggesting that not all policies provide borrowers with the same value for money.

2.4 This chapter looks at two further measures of good value, comparing the value of claims for accident, sickness and unemployment in different policies and assessing the price that borrowers pay for PPI. In this chapter, we use scenarios where the borrower has had to claim on their PPI policy for a period of at least 12 months. We have done this because many of our clients have long-term financial difficulties, which last 12 months or more.

The cost of payment protection insurance on revolving credit agreements

2.5 The policies we have seen covering credit card payments vary in the costs, level of protection and value of payments they offer. Table 2.1 below demonstrates this for with six randomly chosen credit card agreements sourced between June and August 2005.

Table 2.1 – a comparison of the costs and benefits of PPI policies offered

Company	Monthly benefit	Unemployment	Initial waiting period	Subsequent payment	Cost
Barclaycard	10% balance	12 payments	14 days	Each complete 30 days	£0.79 per £100 balance pcm
Capital One	10% balance	12 payments or until credit limit	30 days	Each complete 30 days	£0.79 per £100 balance pcm
Mint	10% of balance to maximum 10% credit limit	12 payments	30 days	Each complete 30 days	£0.77 per £100 balance pcm
Lloyds TSB	5% of outstanding balance	12 payments, last to clear balance	15 days	Each complete 30 days	£0.79 per £100 balance pcm
HBOS	10% balance to maximum £2,500 per month	12 payments	30 days	Daily benefit paid monthly	£0.78 per £100 balance pcm
MBNA	3% balance to £1,200 maximum	12 payments	30 days	Each complete 30 days	£0.72 per £100 balance pcm

2.6 A number of the policies are priced at the same amount and all of them are within reasonable touching distance, with each costing less than one per cent of the value of the outstanding balance per month in each agreement. Although this does not seem to be much, this is not a particularly transparent way of stating the cost. When added together on an annual basis, a £1,000 balance throughout the year will attract an annual premium of £95 for the highest priced policy and £86 pounds for the cheapest. In APR terms, this is the equivalent of adding nine and a half per cent and eight and a half per cent respectively to the cost of borrowing (or around 0.75 and 0.7 per cent to the advertised monthly rate). Expressed in these terms, the PPI premium of these agreements seems more expensive and the difference between the most and least expensive policies more marked. For example:

> A Northern Ireland CAB reported that a man off work due to ill health sought advice about £21,000 debt, which included three credit cards. The CAB was shocked to discover the cost of payment protection insurance premiums on the credit cards:
>
> - £15.50 per month on a debt of £2,152,
> - £24.52 per month on a debt of £3,168 and
> - £14.36 per month on a debt of £1,340.

This totalled nearly £50 per month on debts of £6,600, which is equivalent to an extra monthly interest charge of 0.75 per cent.

2.7 We believe that borrowers need a clear and simple method for assessing the total cost of PPI in relation to the cost of borrowing on revolving credit agreements. The usefulness of both summary boxes and scenarios was raised by the Treasury Select Committee inquiry into credit cards and a similar level of transparency should be extended to PPI connected to these credit agreements.[12] **Citizens Advice recommends that the Key Facts document for PPI policies sold with revolving credit agreements should give brief scenarios of the overall costs of the policy.**

2.8 Policies also differ in what they offer borrowers for their money. In PPI covering revolving credit agreements, unemployment and illness/disability benefits are expressed as a per cent of the balance outstanding on the last statement date before the claim. Once again, most of the policies pay a monthly benefit at the same rate of 10 percent of the balance. However two of the policies pay significantly lower benefits at five and three per cent respectively. On an outstanding balance of £1,000, the difference between the highest and lowest paying policies is £70 per month, a massive amount considering the price difference between policies. All of the policies offered a maximum of 12 monthly payments (unless the balance cleared first) in any single claim period; although in some policies the total amount of benefit was capped at the level of the borrower's credit limit or some other monetary amount.

2.9 Clearly these six policies have been designed with some regard to each other and there is a standard of sorts operating in PPI for credit card agreements. However this does not appear to be enough to ensure a consistent level of benefits across policies with some borrowers offered a lower degree of protection than others. This translates directly in to the effectiveness of the policies in covering borrowers against the threat of indebtedness.

2.10 Borrowers who experience longer periods of reduced income through unemployment or incapacity for work through illness or disability will want to know whether the PPI they have bought can keep them clear of a long-term debt problem. Only Lloyds TSB's credit card policy appears to give this commitment by clearing the balance owing on the card with the final benefit payment. All the other cards only commit to making 12 payments in a claim period, regardless of any remaining debt. Table 2.2 below provides estimates of the balance remaining (if any) after 12 benefit payments at three different payment rates and at three interest rates that reflect segments of the credit card market. A starting balance of £1,000 is assumed at the start of the claim. It is also assumed that the borrower has to continue to pay the PPI premium payments throughout the claim period. These have been added to the balance.

[12] *Transparency of credit card charges,* Treasury Select Committee, December 2003

Table 2.2: Amount left on a £1,000 credit card balance after a continuous 12 month claim

	Monthly Interest rate % (APR in brackets)[13]		
Benefit payment rate	**1.25% (16.07%)**	**1.5% (19.56%)**	**2.2% (29.84%)**
10%	nil	nil	£5
5%	£601	£629	£713
3%	£862	£894	£988

2.11 As one would expect, a lower rate of benefit payments leads to a larger balance remaining at the end of the benefit period. A higher interest rate also reduces the effectiveness of benefits, leaving a residual debt for each benefit payment rate at the highest level of interest shown here. Given that higher interest rates are charged to people with a poor credit history or on low incomes, this method of calculating benefits perversely gives least protection to borrowers who need it most.

2.12 This is particularly evident in the policy paying monthly benefits at three per cent of the outstanding balance. As the Treasury Select Committee highlighted in their report on credit card transparency, many credit card companies have now reduced their minimum payment on credit card balances to 2 – 3 per cent of the outstanding balance.[14] Taking into account the ongoing costs of the policy itself, a borrower may only see their indebtedness reduced by £12 in the worst scenario in table 2.2. CAB evidence shows the impact of this practice:

> A CAB in Surrey reported the case of a woman in well paid employment who fell ill and had to rely on statutory sick pay. She had taken out PPI on two credit cards. The insurance would pay 10 per cent of the balance at the time the illness started but only if insurance premiums were continued for 12 months. She worked out that the balance would have to be over £950 to make claiming worthwhile. The other card had PPI costing £19 per month but only covered 3 per cent of the balance.
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> A CAB in Norfolk reported that a widow on income support owed a credit card company £3,140. She was paying £22.52 per month for payment protection premiums, but with interest, late payment charges and the PPI premiums, the minimum payment on her account totalled £105.53 per month. The insurance would only pay £105.20 per month off the account, so her debt was slowly increasing.

[13] Interest calculated on a monthly rather than daily basis
[14] *Transparency of credit card charges,* Treasury Select Committee, December 2003

The cost of payment protection insurance on fixed sum credit agreements

2.13 PPI cover on fixed sum credit agreements such as secured and unsecured loans, hire purchase and conditional sale agreements is often purchased by an up front single premium that borrowers fund by taking out additional interest bearing credit that is bundled up with the payment to the main loan. The premium and interest that accrues on it can work out as a substantial proportion of the overall cost of credit as the following cases brought to bureaux show.

> A CAB in Greater Manchester reported that a woman with multiple debts had taken out a consolidation loan for £20,000 to deal with them. Later the client read the documentation and realised that she had actually paid £27,000 as the loan included payment protection insurance. When the client investigated further she saw that her monthly repayments were £284pm over 300 months, which meant that she would have to pay £85,200 over the course of the agreement. By this time she had run out of time to cancel the loan.

> A CAB in Cornwall was visited by a woman who had taken out a joint secured personal loan. She had separated from her partner and was struggling with the repayments. Although the client had signed the application and received a copy, she was unaware of the cost of the PPI premium that increased the loan from £17,800 to £22,962. The premium attracted interest at the same rate as the initial loan.

2.14 Bureaux evidence on the costs of PPI for fixed sum credit agreements shows how prices vary considerably both within and between sectors of the consumer credit market. This is summarised in table 2.3 below showing original loan amount, PPI premium and the premium expressed as a per cent of the amount borrowed.

Table 2.3: PPI premiums by per cent of loan value: cases reported by bureaux[15]

Loan Type	Loan amount	PPI premium	Premium as a per cent of loaned value
Unsecured personal loan	£8,933	£2,217	25%
Unsecured personal loan	£11,000	£5,133	47%
Hire purchase for car	£5,059	£2,157	43%
Hire purchase for car	£6,895	£2,317	34%
Unsecured loan	£5,600	£744	13%

[15] These examples have been taken from case studies reported to Citizens Advice by bureaux during the period January 2004 – April 2005, where the bureau was able to identify the costs of insurance and the loan. It is not clear from the HP and conditional sale agreements whether the amount identified for insurance also included insurances other than PPI.

(Debtor/creditor/ supplier)			
Secured loan	£25,000	£12,127	49%
Secured loan	£35,000	£10,150	29%
Conditional sale for car	£4,300	£2,394	56%
Unsecured personal loan	£13,000	£3,367	26%

2.15 Lending for PPI policies contribute considerably to the amount owed in each of these cases, with agreements that tend to be marketed at people on lower incomes often attracting the highest PPI costs by proportion of loan size. Policies connected to hire purchase agreements seem disproportionately expensive in this evidence. It is also important to note that people taking out more than one credit agreement will face these charges more than once. Someone who buys an unsecured loan and goods on hire purchase in the first and third examples in table 2.3 would see their indebtedness of £14,000 grow by an additional £4,500 through payment protection premiums alone.

2.16 In a series of seven quotes obtained on-line for a loan of £5,000 to be repaid over 60 months the monthly loan repayment was increased by an average of £23.30 with PPI costs. As these costs eat into the income of multiple credit users, their financial vulnerability becomes greater. Paradoxically this might make PPI disproportionately attractive to people who are at greater risk of indebtedness. In these circumstances it is not clear whether PPI provides relief from indebtedness or is a factor in its cause.

2.17 As with PPI covering credit cards, there is variation in the amounts that policies pay in respect of illness, disability or unemployment. Monthly payments in respect of fixed sum loan agreements tend to cover the loan instalment amount, although some policies (particularly some mortgage protection policies) take an income protection approach in replacing a proportion of lost income or paying a set amount of benefit that is more than the loan instalment. Several policies offer *cashback* marketing incentives where a proportion of the premium is repaid to borrowers who reach the end of their loan term without claiming on the policy. All of the policies we have seen pay unemployment benefits for a twelve month maximum in an unbroken claim. Some policies will pay sickness/disability benefits up and until the end of the loan term if needed while others will only pay these benefits for a maximum of 12 months in one unbroken claim.

The need to make an effective price comparison

2.18 The variation in both the price and extent of cover in PPI products sold with both fixed sum and revolving credit agreements suggests that some lenders are selling better value policies than others. Borrowers with access to comparative PPI product information might be in a better position to put pressure on those lenders selling polices that are more expensive or which offer lower standards of cover. Equally, greater awareness of alternatives such as stand alone PPI, income protection policies or a suite of separate insurance products might aid people to get better protection against the risks of credit default at a lower price. **We recommend that, as a minimum, the Financial Services Authority (FSA), who regulate general insurance, establish and publicise comparative tables for PPI and alternative products insuring against credit risks.**

2.19 This would be a welcome addition to the consumer information provided by the FSA encouraging those that are able to shop around to do so. **A health warning in PPI marketing alerting prospective buyers that a better deal might be available elsewhere and directing their attention to FSA comparative information would be help to generate take-up.**

2.20 However most people are primarily shopping around for credit rather than for insurance and it is unlikely that the price and content of PPI will have more than a marginal effect on their choice of credit product. For many borrowers better information will not alter the choice of taking the insurance offered by their lender or not being insured at all. When even mortgage payment protection insurance has a take up of only 37 per cent of new borrowers (25 per cent for all borrowers), more needs to be done, by lenders in particular, to make PPI a more attractive proposition for borrowers. [16]

One-off and monthly premiums

2.21 PPI premiums on credit cards are usually credited monthly to the balance. Likewise mortgage payment protection insurance is paid monthly. But PPI for fixed sum credit agreements is often paid up front as a single premium. This pushes borrowers into funding the premium by increasing the amount borrowed. This would not be necessary if borrowers could pay by monthly instalments as they go along. Lenders are squeezing extra loan business out of borrowers who are effectively being penalised for trying to minimise the risks of credit use.

2.22 Citizens Advice recommends that relevant credit industry codes of practice including the Banking Code, Finance and Leasing, Consumer Credit Trade Association codes, are amended to require lenders to offer borrower the option of paying PPI premiums on fixed sum credit agreement by monthly instalments instead of a one-off premium. In order that borrowers can exercise an informed choice, lenders should be required set out the cost of each option, including interest charged on single premiums.

2.23 This has two advantages for borrowers. Firstly if an individual is unable to keep up with payments for a reason which is not covered by the insurance, the PPI premium does not add to their indebtedness. Secondly if the borrower wants to settle the loan early, the insurance policy simply ends, rather than forming part of the early settlement rebate calculations.

[16] *Managing risk and sustainable home ownership in the medium term: Reassessing the options*, J Ford and S Wilcox, Joseph Rowntree Foundation (2005).

2.24 Given that lenders increasingly price credit products according to risk, one might expect borrowers to be offered an interest rate discount as an inducement to take out PPI as this reduces the risk of credit default rather than being charged additional interest for the benefit of the lender. However such discounts are not commonly offered. Indeed, in some cases where lenders have offered such a discount the OFT have had to intervene as the price of the (effectively compulsory) PPI had not been included in the credit cost calculation thus giving a misleading illustration of the value of the discount to borrowers[17].

2.25 It would appear that the credit industry is more interested in the profitability of PPI than its effectiveness as a safety net against indebtedness. The Competition Commission Inquiry into the store card market found that sales of PPI account for between nine and 20 per cent of card providers' total revenue. The premiums paid by consumers were typically three to four times the net rate charged by the underwriter to the card provider.[18] Recent estimates for mortgage payment protection insurance suggest that the annual premium income for £100 worth of cover is nearly three times the cost of that cover to the insurer before administration charges, albeit in benign economic conditions.[19]. This implies that borrowers could be overcharged by as much as £3 billion per year for PPI cover.

2.26 Taken with the evidence cited above, these figures suggest that there are savings that could be passed on to borrowers if there was a more competitive PPI market, particularly as lenders capture part of the benefit of PPI in reduced bad debt provision. **Therefore we recommend that the FSA establish a PPI *stakeholder* product with charges capped at an economic level.**

Conclusions

2.27 Citizens Advice believes that our evidence and figures from other sources suggest that savings can be made on the cost of PPI which could be passed on to borrowers as an incentive for more people to insure themselves against credit risk. These savings must come from the profits that lenders are taking from PPI policies as it is their responsibility to ensure that PPI products reduce the risks of indebtedness. In the next chapter we look at the content of policies and how they could be improved.

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[17] *Discounted APRs and PPI*, Office of Fair Trading, 2000
[18] *Store card market inquiry. Emerging thinking, Annex E,* Competition Commission (2005)
[19] *Managing risk and sustainable home ownership in the medium term: Reassessing the options*, J Ford and S Wilcox (2005)

3 Exclusions

What would happen if you became unable to cover your card repayments? You can rest assured that your card repayments will be taken care of…"(HSBC card protection)

"So for just a few pence a day you could enjoy additional peace of mind, knowing that your …monthly repayments are covered, should you be unable to work…" (MBNA card cover)

"Our aim is to combine value for money with peace of mind to make insurance straightforward for you" (Bank of Scotland unsecured loan cover)

"Optional Loan Protection could cover your loan repayments if you can't work due to illness, accident or unemployment. You can only take out this valuable reassurance when you apply for your loan so remember to tell us that you want it – otherwise it'll be too late." (Lloyds TSB personal loans)[20]

3.1 Lenders' information about the PPI products they sell often opens with a marketing statement that describes the product in a way to appeal to prospective borrowers. Prominent references to "peace of mind" and "repayments taken care of" suggest a guarantee to meet the borrower's commitments under the credit agreement should anything go wrong. Not just a product, *payment protection* here evokes the idea of a relationship of trust, mutual support and value between lender and borrower.

3.2 In reality, payment protection is a misnomer. Our evidence is that the protection borrowers pay for is partial, conditional and subject to exclusions, which may prevent a successful claim. It is precisely because consumers cannot plan for sudden change of circumstances that exclusion clauses so badly undermine the value of payment protection insurance. This chapter examines CAB evidence on the common exclusions in payment protection insurance policies:

- Age
- Bad backs
- Mental health problems
- Pre-existing conditions
- Employment patterns
- Risks which are seldom covered

Age

3.3 Upper age limits on some or all of the risks covered by the policy are a common feature in the PPI policies we have seen. For instance, some

[20] All the above quotes were taken from internet promotional material from these lenders during the period May – August 2005.

policies will limit cover for unemployment, illness and disability to borrowers under 65; in other policies borrowers above an age threshold such as 65 or 70 become excluded from any cover under the policy. Evidence from bureaux shows how borrowers who are affected by these age limits are still sold policies that they cannot benefit from.

> A CAB in Bedfordshire reported that a client who was widowed and aged 65 had bought windows, under considerable pressure from a salesman. Included in the contract was payment protection insurance. The total value of the contract was £6,240 payable in 120 monthly instalments. Following his wife's death, he tried to claim on the PPI but was told the cover only applied to the first person on the contract, which was him. The client then went on to read the small print and he discovered that the PPI could only be taken out by someone under the age of 60 at the time of contract. The credit provider's agent was aware that the client was over 60 because the client had to provide details when applying for the credit agreement.

> A CAB in Cambridgeshire reports the case of a woman who had been paying a PPI agreement in respect of a credit agreement for some years. The woman had had to go into hospital and attempted to make a claim. However, the woman was told that as she was 93 she was too old to be covered by the PPI. The bureau was told that the woman had made payment to the PPI of £1,200 over the years.

3.4 The age limits found in many PPI policies seem to take no account of the actual credit risks borrowers affected by these exclusions actually face. The employment rate for people over 65 in 2004 stood at 5.9 percent and 14 percent of the income of pensioner households headed by someone under 75 derived from earnings.[21] The assumption found in many PPI policies that people over 65 (the most commonly found age threshold) do not need cover against the risk of involuntary loss of earnings is incorrect in point of fact and discriminatory in its affect. **Citizens Advice believes that PPI policies should cover involuntary loss of earnings without age limits.** As the proportion of income derived form earnings drops to two per cent for those households where the head is over 75 this would not represent an unlimited extra cost for insurers. [22]

Bad backs

3.5 Many PPI policies contain clauses that exclude claims where the consumer has lost income as a result of back problems. In some cases this exclusion is total; one policy we found excludes all cases of "backache", other policies place a high burden of evidence on claimants that in some cases leads to seemingly unreasonable refusals of claims.

[21] *Labour Market Trends, Volume 112,No 6: 20 July 2005*, Office of National Statistics (2005); *The Pensioners Incomes Series 2003/4*, Pensions Analysis Directorate, Department for Work and Pensions (2005)
[22] *The Pensioners Incomes Series 2003/4*, Pensions Analysis Directorate, Department for Work and Pensions (2005)

A man with three credit card debts sought advice from a CAB in Wiltshire. He was unable to work because of a fractured spinal disc and had claimed on the payment protection insurance on all three of his credit cards. However the insurance company refused to accept the medical evidence supplied by the client, which included normal x-rays and hospital disability letters. The insurance company said that the only evidence they would accept was MRI scans. During the course of this dispute about acceptable evidence the client's debt continued to mount through interest accumulating on the debt and PPI premiums continuing to be charged to his accounts.

A Worcestershire CAB saw a client who was off work with back problems. The client had put in a claim on his payment protection insurance, but the small print of the policy stated that medical evidence needed to be backed up by an x-ray. However, the client's GP disputed that the client's condition would actually show up on an x-ray.

3.6 It is pertinent to point out here that the Health and Safety Executive state that back pain is the leading cause of sickness absence from work.[23] A significant cause of loss of earnings is therefore excluded from PPI cover in many policies.

Mental health

3.7 Common exclusion clauses in PPI policies make claims on the basis of poor mental health either impossible or extremely limited in scope, for two reasons. Time off work due to experiencing mental health problems is excluded from some PPI policies. For instance, a personal loan cover policy sold by one high street bank states that claims resulting from 'any psychotic or psychoneurotic illness, mental or nervous disorder or stress or stress related condition' will be excluded. Evidence from bureaux shows the detriment that such exclusions cause CAB clients.

A client of a Hampshire CAB had bought a car on a Hire Purchase agreement that included payment protection insurance. The client had to take time off work because of stress. However stress is specifically excluded from the sickness cover in the payment protection policy.

A client of a Somerset CAB was told that he could not claim on his payment protection insurance. The client had been off work suffering from anxiety and stress; however the insurance company would not pay out on claims resulting from any mental health problems.

A CAB in Surrey advised a woman who came to them after her son had been sold a bank loan with payment protection attached. However, the client's son was already off work due to serious mental illness and

[23] *Initiative Evaluation Report: Back in Work*, Health and Safety Executive, 2002

claiming incapacity benefit. The policy that the bank sold him did not cover mental health problems.

3.8 As in the case of back problems, some policies allow claims in respect of mental health problems but make this conditional on fulfilling further requirements. One policy excludes mental health claims unless the claimant is under the care of and receiving treatment from a consultant psychiatrist. We explore this issue further in Chapter 5.

3.9 Given that estimates suggest between one in four and one in six people suffer from a mental health problem at any one time, and that in February 2005, 925,700 of the 2,387,000 claims for incapacity benefit were as a result of mental or behavioural disorders, another significant reason for claiming is not covered in the PPI policies sold by some large, well known, high volume lenders. [24]

Pre-existing conditions

3.10 It is also common for policies to exclude claims made as a result of pre existing medical conditions that the claimant either knew about when the policy started or which the claimant had either shown symptoms of or received treatment for within a specified period before the policy started. This may appear to be reasonable, but often these exclusions were not brought sufficiently to the borrower's attention at the time of sale:

> A CAB in Lancashire reported that a client with four unsecured debts had had to give up work due to longstanding health problems. He had claimed on the payment protection insurance on all four debts that included payment protection insurance. One of the loans was for £8,000 with a payment protection premium added to make a total owed of £13,786.08. The company questioned the client about his medical condition, stating that this was probably the result of a long-term pre existing condition.
>
> A Staffordshire CAB saw a client who had bought a second hand car on credit, with payment protection insurance. When he became ill with asthma and depression he made a claim. The insurance company told him that he was not covered by the policy because asthma was a pre-existing condition and that his policy did not cover depression.

3.11 There are particular problems with the length of this period, which varies between policies. Typically mental health problems are subject to longer limits on pre-existence than are other physical disabilities, with the exception of back problems. For instance, the PPI policy sold by a well known credit card company specifies that claims will not be paid when the medical conditions

[24] N Singleton, R Bumpstead, M O'Brien, A Lee and H Meltzer, *Psychiatric Morbidity Among Adults Living in Private Households*, 2000, (London, The Stationery Office, 2001); *Incapacity Benefit and Severe Disability Allowance Quarterly summary statistics*, February 2005, DWP

giving rise to the claim pre existed the claim by up to two years; this period is extended to five years in the case of mental health and back problems.

Employment

3.12 Exclusion clauses in PPI policies also affect benefits paid for income loss due to unemployment. Policies usually exclude claims arising from involuntary unemployment, unemployment following dismissal for misconduct and other circumstances where the loss of employment stems from the non – economic conduct or behaviour of the claimant. These conditions are generally reasonable and only present problems with interpretation and adjudication disputes. However, another set of exclusions apply to the self employed, people working on temporary contracts and casual workers where it can be difficult to demonstrate that unemployment is involuntary.

3.13 Typically the self-employed are not covered for reductions in income, whether protracted or temporary, unless they cease trading and wind up the business. Even if this is the case, policies will differ on the circumstances of business failure considered reasonable to attract benefit. For some policies, the trader must have ceased trading because they could not find enough work to satisfy reasonable business and living expenses. In other policies the trader has to prove that the business ceased trading because it was unable to pay its debts when they fell due. Many self-employed people will be unincorporated sole traders with personal liabilities for business debts. It seems perverse that the gateway to protection from indebtedness on personal lending should be proof of indebtedness on their business lending. For example:

> A CAB in Kent reported that a client came to them concerning payment protection insurance. The client was no longer working and he made a claim on his insurance. His claim was been rejected because the insurance does not cover people who are self-employed. However, the client stated that the salesman knew this when he was sold the policy.

> A CAB in Cheshire saw a client with arrears on a secured loan. The client sought to get the payment protection insurance refunded as he was self-employed and this is specifically excluded from cover under the policy.

3.14 For consumers employed on non-permanent contracts cover is also limited in a way that varies between policies. In some policies all unemployment resulting from the termination of fixed term contracts is excluded, regardless of the term of the contract. In other policies, employees on fixed term contracts are covered only where they have worked for an employer for a set period of time, usually 24 months or where the employee is under a renewed 12 month contract.

> An Oxfordshire CAB saw a client who had taken out a loan with a high street bank, together with payment protection insurance to cover him in the event of redundancy. During the term of the loan, he changed his job to work for a temping agency at higher pay. He was then made

redundant but the bank refused to honour his claim as temping work is listed as an exclusion.

A CAB in Warwickshire was visited by a client who had taken out a loan for £5,000 together with PPI costing an extra £500 to cover him in case he was made redundant. As part of the loan application process the client had to send in his contract of employment, which clearly stated that he was a casual worker. He subsequently had to make a claim on the PPI policy but was told by the insurance company that he was not entitled to benefit, as the policy does not cover casual workers. The lender did not point this out when the policy and the loan it supported were sold.

3.15 People in self-employment make up 12 per cent, or one in eight, of the UK labour force and people in temporary employment about 6 per cent, with just under half of these on fixed term contracts.[25] This represents another large section of the credit default risk that is not effectively covered by PPI.

3.16 We believe that PPI policies should do much more to protect the self-employed and those who are employed on non-permanent contracts. Insurers are entitled to reasonably protect themselves against unreasonable claims. However, the breadth and nature of PPI exclusion clauses seem to go beyond what is reasonable. The effect is that many extant policies fail to provide adequate protection against genuine financial hardship and in some cases actually provoke indebtedness. While no one would deny that assessing claims from self employed and non-permanent contract workers presents difficult questions of evidence, cause and classification, we would be surprised if a fair system of adjudication could not be established by an industry suitably motivated to do so.

Risks that seldom get covered

3.17 Borrowers also face common risks to the level of their income that are completely outside the cover offered by most policies. Relationship breakdown and having to give up work to care for a sick or elderly relative are commonly not covered by PPI policies:

A Buckinghamshire CAB saw a client who took out a cash loan with a high street bank. The client was paying for insurance as part of the repayment plan. When she tried to claim that she had lost her job she was informed that she was not eligible, as she had lost her job not through her own health but because she had had to look after her son who has severe asthma.

3.18 It has been estimated that there is a 6.6 per cent chance of an adult in the UK becoming a carer, with one survey finding that six out of ten carers had given

[25] *Labour Force Survey Quarterly Supplement* April 2005, Office of National Statistics

up employment in order to provide care.[26] However of the policies cited above only those offered by Bank of Scotland and MBNA cover carers. The fact that more than one policy can offer this cover suggests that it is not an uninsurable risk, merely one that PPI seems to disregard.

3.19 Relationship breakdown was cited as a contributing factor to indebtedness by 20 per cent of CAB debt clients who responded to a survey question on the reasons for their debt problems.[27] However none of the polices cited above included an element for relationship breakdown. This is generally regarded as an uninsurable event as its occurrence depends heavily on a decision of the insured. However we have seen one policy that provided cover for martial breakdown, but only one. This suggests that insuring for relationship breakdown might be difficult but may not be impossible.

3.20 In the same survey, around 9 per cent of CAB clients reported that a drop in income contributed to their debt problem. PPI polices do not tend to cover temporary reductions of income unless they are caused by a major event such as job loss. Although a reduction in work hours is a potential cause of credit default, borrowers are currently unable to find insurance against it in any of the PPI polices we have seen.

3.21 Some PPI policies also exclude certain borrowers because cover is restricted to the first named account holder, even though it is common for couples to take out credit in joint names. As the risks of losing income may not differ between borrowers the effectiveness of PPI as a safety net is undermined.

> A Lincolnshire CAB reported that a man sought advice about the payment protection insurance on a hire purchase agreement to buy a car. At the time of sale, he and his wife were expressly told that they were both covered if they were ill, unemployed or died. When the client started to read the small print of the agreement, he was told it was unnecessary, as all the clauses had been thoroughly explained. The client subsequently became ill and as he was self-employed his business was no longer viable. In addition his wife had also become unemployed. The creditor had turned down a claim on the PPI policy, as the client was not the first person named on the agreement.
>
> A Wiltshire CAB reported that a couple had taken out a joint loan of £15,000, plus £3,000 for payment protection insurance. His wife subsequently discovered she had cancer and had to stop work. When the couple tried to claim they were told that only the first named person was eligible. They did find this in the small print but they were not advised of it at the time.

3.22 Lenders know full well that anyone who enters into a joint credit agreement is liable to repay in full. Lenders also know that joint borrowers will often rely on

[26] *The risk of informal care: an incidence study*, M Hirst, Social Policy Research Unit, University of York (1999); *Redressing the balance: inclusion, competitiveness and choice*, M Howard, Carers UK (2002)
[27] *In too deep, CAB clients' experience of debt*: Citizens Advice 2003

a joint pooled income to meet credit repayments. It is therefore difficult to see how PPI policies with first named account holder clauses can possibly meet the needs of joint borrowers.

3.23 It is clear that by excluding some important credit risks and omitting other risks completely PPI does not provide borrowers with the peace of mind and reassurance that the promotional materials promise. We believe that people should be able to expect a better deal.

The case for a fair baseline

3.24 Treating all mental health problems, or back problems or the entire experience of the self employed as undifferentiated and uninsurable exclusions might simplify the process of adjudication and reduce the average transaction cost of claims. But this does nothing to reduce the individual and social costs of indebtedness suffered by the considerable proportion of consumers excluded from cover. A central criticism of PPI can be found in the seeming indifference to the welfare of its consumers in the commercial rigidity of many policies. It seems as if the effort needed to prove the validity or involuntary nature of these credit risks is just too much for the policy designers to be bothered with. Due to the common nature of these life events we would argue that every policy that contains the exclusion clauses outlined above is unsuitable for the needs of significant numbers of consumers. Every sale of such a policy is arguably a mis-sale.

3.25 This is not to damn all PPI policies out of hand. Variations in the range and extent of exclusion clauses are illustrated in a comparison of the PPI policies sold by a random cross section of lenders.

3.26 Lenders can, if they choose to do so, commission and sell better and fairer PPI products. However Citizens Advice questions whether it is appropriate and in the consumers' best interest to leave this choice to individual lenders. The practice of product bundling means that consumers generally buy a PPI policy tied to the credit product they have chosen and have no real opportunity to shop around for credit insurance to go with it. A guarantee of fair and responsible standards of cover across the credit industry as a whole would require a commitment from the industry to coordinated action.

3.27 There is nothing new or radical about this; the Council of Mortgage Lenders (CML) introduced a *baseline cover specification* in 1999 setting out the minimum standards of cover in mortgage payment protection polices sold by mortgage lenders. The Finance and Leasing Association (FLA) also have produced a *baseline creditor product* for PPI policies sold by its consumer finance members.[28] In principle, a baseline product developed through self-regulatory means could be beneficial to consumers. But the current trade association initiatives do not provide consumers with sufficient guarantees.

[28] See Appendix 2 for a comparison of the CML and FLA baseline products

Company	**Bad backs**	**Mental health**	**Self employed**	**Fixed term contract**	**Pre-existing conditions**	**Age**
Barclay-card	Not excluded	Not excluded	Only if business wound up	Depends on contract length	Two years, unless claim for bad back or mental health where the period is five years.	Up to 65 for accident, sickness or unemployment claims but up to 70 for hospitalisation
Citi Bank credit card	Not excluded	Not excluded	Bankruptcy, liquidation or official termination of self employed status due to failure of business	Depends on contract length	12 months	Up to 65
Capital One	Excluded	Only for psychosis	Only if business has failed	Excluded	12 months	People aged 65 or over or who have retired are only covered for accidents or accidental death
Mint	Only if MRI scan shows abnormality	Not excluded	Only if business has failed	Depends on contract length	12 months	Up to 65

Company	Bad backs	Mental health	Self employed	Fixed term contract	Pre-existing conditions	Age
Bank of Scotland unsecured loan	Benefit paid for reduced period	Excluded	Excluded	Depends on contract length	12 months	Up to 65
Lloyds TSB credit card	Not excluded	Not excluded	If business has involuntarily ceased trading	Depends on contract length	12 months	Up to 65 for ASU, 65-75 for hospitalisation benefit
HSBC personal loan	Not excluded	Not excluded	If business has involuntarily ceased trading	Depends on contract length. If contract ends early may pay until end of contract	12 months	Up to 65
MBNA card	Only if radiological evidence	Only if receiving treatment from consultant	If business has ceased to trade due to inability to pay debts when due	Depends on contract length	Excluded	Up to 65 for ASU claims but up to 70 for hospitalisation

3.28 Firstly, the two baselines set different standards in relation to risks that are covered and excluded. The CML baseline includes mental health and back problems subject to evidential requirements while the FLA baseline recommends total exclusion. Given the practice of product bundling, it does not seem reasonable that consumers should receive a lower standard of protection as a result of their credit choice; particularly as both these trade associations have members who sell secured loans.

3.29 Secondly, in some respects, these baselines are set at a very low standard, which just rubber stamps poor practice. Neither of these baselines provide an adequate response to the problems faced by self-employed and contract workers. Yet members of both trade associations will lend to people in these circumstances and sell them PPI cover.

3.30 Thirdly, these two baselines only represent certain sections of the credit industry. The Banking Code, which covers virtually all the main banks, building societies and credit card companies, is completely silent on the question of common standards for PPI. We believe that the consumer credit industry as a whole should give a commitment to produce a PPI baseline standard offering consumers a genuine and comprehensive safety net against all the risks on which lenders are willing to lend. This is not to say that there are no limits to the risks that should be underwritten, only that no common credit risk should be excluded for commercial reasons alone. Shouldering some of the costs of credit risk is surely an important part of responsible lending.

3.31 Finally the baselines are subject to voluntary, rather than statutory regulation. There are few incentives to comply. Although some trade association codes of practice are subject to effective compliance monitoring, others are not. For a baseline to be effective, it needs to be backed up by regular compliance monitoring, ideally by a regulator with effective powers to tackle bad practice.

3.32 Citizens Advice recommends that the Financial Services Authority, the regulator for general insurance, should develop a common insurance baseline product setting out acceptable standards of content for payment protection insurance agreements covering all sectors of the consumer credit market. The FSA should take this baseline into its system of rules for the conduct of insurance business. We set out our own fair baseline product in Appendix One.

3.33 The FSA is already concerned with standards for product content through the emerging *treating customers fairly* initiative that requires firms to develop and market products based on the ‘likely needs and financial capabilities of each group of customers’[29]. If this is true for long term savings products it should also be true for PPI products given their high potential for widespread consumer detriment. As is the case with *treating customers fairly* this should not restrict competition or innovation; it simply means that a fair and effective standard of cover will be an enforceable minimum standard. However market

[29] *Treating Customers Fairly – progress and next steps*: Financial Services Authority 2004

conditions can change and to be an effective product PPI also has to be both responsive to changes in customers' needs and, of course, commercially viable. The impact of a regulated baseline product should be capable of amendment and updating on a regular basis. **Citizens Advice recommends that a product baseline regulated by the FSA should be reviewed through consultation on a regular basis, and that statistical data on health problems, employment and family breakdown, as well as data on refused payment protection insurance claims, are fully considered in assessing the need to amend the baseline.**

3.34 We believe it is important that this product baseline should be drawn up with the primary intention of providing borrowers with an effective safety net. **Citizens Advice considers that the FSA must take into account a proper assessment of credit risks and only excluding from cover any risk where this can be clearly justified as uninsurable.** Such an assessment should certainly avoid treating life events as broad undifferentiated categories. Excluding all claims on the basis of employment status or type of disability is unacceptable. Indeed we note that a large number of policies do not make such exclusions, suggesting that a policy that does cannot be treating its customers fairly. **Citizens Advice believes that blanket exclusions from cover are incompatible with treating customers fairly and should be prohibited in a regulated baseline product.**

Conclusion

3.35 Evidence of the experience of CAB clients shows that, far from delivering peace of mind, in too many cases PPI lets borrowers down at exactly the point where they need help most. As a safety net, there are simply too many holes and not enough net. We are not arguing that PPI should deal with all the risks that can lead a borrower to debt – there is a separate role for both the lending industry and government here - but we believe that lenders and insurers can do a much better job of covering the risks of debt that can best be covered by an insurance product. Consumers would benefit from a fair baseline product, regulated by the Financial Services Authority, which would set out minimum standards for all payment protection insurance policies. A result could be a reduction in the number of mis-sales, which is the subject of our next chapter.

4. The selling process

4.1 This chapter examines CAB evidence on the sale of payment protection insurance. The concern of this report is with PPI policies by lenders to cover borrowers against the risk of defaulting on repayments on a specific credit agreement purchased from the lender. Although separate agreements, the two products are linked by purpose and generally sold together in common marketing and application information. At the point of application consumers might be given a complete copy of the policy terms and conditions, but more typically will receive a *key facts* policy summary that must comply with FSA rules as to form and content[30]. The key facts summary must set out the main features of the summary including any significant exclusion from cover.

4.2 However, our evidence shows that many people are buying, or rather being sold, PPI products that are objectively unsuitable for their needs as their circumstances exclude them from cover at the time of sale. Other CAB clients report being charged for insurance they did not ask for, did not need or did not actually get. In other cases, high pressure sales practices have been used to sell inappropriate insurance to vulnerable consumers. Reports of mis-selling problems are regular and relate to nearly all sectors of the consumer credit market from non-status mortgage lenders and hire purchase companies to major high street banks and credit card companies. The range of this evidence suggests widespread failures of consumer protection in both the PPI selling process itself and in the wider regulation of PPI sales.

4.3 This chapter will look at inappropriate sales of payment protection insurance linked to irresponsible lending, in particular lending to consolidate existing indebtedness.

Irresponsible lending

4.4 CAB evidence is that the mis-selling of PPI policies is closely connected to irresponsible lending practices. Evidence of such practices is particularly worrying in cases where a vulnerable person is especially reliant on the lender to look out for their best interests.

> A CAB in Surrey reported that a client had been sold a loan protection plan although he had long-term mental health problems. The total to pay on the loan agreement was £8,930 including an additional £2,200 to pay as a single premium for the PPI. At the time of signing the agreement the client was very unwell and was not aware of what he was signing. The bank was aware of the client's situation and that the client might not be eligible for the insurance protection policy.

> A CAB in Surrey was visited by a woman who took out a loan at a high street bank along with a PPI policy. She gave the branch staff full details of her mental health problems including frequency of

[30] See the FSA handbook, particularly *Insurance Conduct of Business*, Chapter 5.5 for the form and content of key facts statements.

hospitalisation, being prevented from working for six years and income details showing receipt of income support and disability living allowance. She was told that none of this would affect claims on the PPI policy. The client had to go into hospital and her income dropped because of technicalities in the benefit system. Her PPI claim was turned down on grounds of her pre existing medical condition.

A CAB in Staffordshire reported the case of a client who had taken out a loan with a high street bank of £19,000 with a loan protection premium of £3,500. However at the time of the sale the client was in receipt of income support and was registered blind. The CAB argued that as the client was unable to claim against the insurance (not in work with a pre-existing disability before insurance purchased) he should have received a refund of the premium. The bank responded that although the branch staff were aware that the client was registered blind, the fact that he had some sight and did not use a cane or a guide dog meant that the loan protection policies were sold in good faith.

4.5 When consumers are plainly unaware or misled as to the full facts about a credit relationship it is arguable that lending decisions are not just irresponsible but predatory as well. The predatory sales process goes beyond mere complacency towards the wellbeing of credit consumers by exploiting the unequal distribution of power that can exist between the parties to a credit arrangement. One group of consumers particularly vulnerable to this are people in financial difficulties who approach their creditors for help in solving their financial difficulties. As it is the nature of the credit industry to grant loans, lenders often respond to such a request for help by offering further financial products, with further loans to reschedule or consolidate existing problem debts a particularly important example.

4.6 In many, perhaps even most, cases, consolidation loans are offered with the best of intentions as an option that can offer real benefits to indebted consumers. However bureaux continue to report a number of cases where consolidation loans have been sold to consumers who will struggle to make repayments on even this rescheduled debt from the outset. In such cases PPI policies are often sold with the loan, at significant extra cost and no benefit whatsoever to the borrower.

A man sought advice from a Devon CAB after he took out a loan to consolidate credit card debts and an overdraft. The client was persuaded to take out optional payment protection because he was told that otherwise the loan would not have been approved. The original loan was £14,575. With interest of £10,660, and the payment protection insurance premium of £7,700, the client ended up owing over £32,000.

A Dorset CAB reported that a client came to see them after he had fallen into debt. His bank had advised him to consolidate his indebtedness into one loan over a 10 year period, even though he was not working at the time due to an injury. The loan was for £16,200, with interest of £16,260 and a payment protection insurance premium of £4,918, bringing the total to £37,378.

4.7 The fact that vulnerable and sometimes desperate consumers can be persuaded to purchase loan and PPI products that are clearly detrimental to their welfare seems to raise serious questions for the regulation of sales practices. The main focus of this regulation has been in helping consumers to make informed choices through the provision of prescribed information statements at important moments in the sales process. While we welcome the FSA rules requiring borrowers to be given the *key facts* about a PPI policy they are invited to take out; the experience of some consumers shows that information alone, even where it is freed from the problems of understanding and representation described above, cannot prevent all aspects of mis-selling.

Pressure sales

4.8 Further evidence from bureaux casework shows the important role of sharp practice in the problems CAB clients report with PPI. In these cases, consumers who possess a reasonable degree of information and understanding still find that they are being ripped off through the deliberate actions of sales staff applying the hard sell or simply ignoring consumers' wishes. Bureau evidence shows how CAB clients have been pushed, pressured and mislead in face to face sales

A CAB in Wiltshire saw a client who had taken out a loan and specifically stated that he did not want insurance. He received verbal confirmation from the lender that insurance would not be included with the agreement. However, insurance was included and the client paid an additional £100 per month for over a year before the problem was resolved.

A CAB in Worcestershire advised a couple with health problems in receipt of income support who were sent pre-approved applications for a credit card from with a credit limit of £600. They accepted the card but were then pestered to take out insurance despite repeatedly saying that neither of them were in work. The credit card provider said that it would provide cover in the event that the cardholder did get a job.

4.9 CAB clients also report problems where they have taken out credit by post, internet or telephone, or via a retailer, where payments for PPI policies that they have not asked for appear, as if by magic, on their bill. In these cases, the PPI policy tends to be connected to credit and storecards or catalogues, with the premium price fairly low to reflect low credit balances. However, the payments to these ghost sales of PPI policies can add up to a bigger debt problem over time.

A Gloucestershire CAB reported the case of a client whose daughter had bought goods on credit over the internet. She was charged for a PPI policy even though she had not asked for it. She informed the company that she did not want the insurance, paying for all the goods but not the payment protection. The creditor billed her each month for the payment protection plus an extra £20 per month administration charge for non-payment. The original PPI charge was £2.66 per month.

A CAB in West Yorkshire reported that an elderly client came to them after she had been charged payment protection on her catalogue for many years. She told the CAB that she had been unaware that she had been paying this until she came to settle her account and it was pointed out to her. The client had never asked for it or signed anything to agree to pay for it.

4.10 A further case involving a second hand car bought with a credit agreement illustrates how sharp practice in the sale of PPI policies and bad practice in arrears management can combine to produce worst-case outcomes for borrowers with a debt problem.

Clients who visited a CAB in County Durham had entered into a conditional sale agreement for a car. The car cost £4,700, increasing to £6,660 with the addition of interest. A PPI premium totalling £2,970 was also added, although this was neither requested nor wanted by the clients. PPI was not discussed and no price had been quoted. Despite the insurance, the clients fell into arrears and the car was repossessed leaving an outstanding balance of £5,200. The creditor immediately assigned this to a debt collector who started bankruptcy proceedings and refused to negotiate repayments. The bureau had been trying to get a copy of the PPI policy to scrutinize it further and after the involvement of Trading Standards, two pages of small print duly arrived from the insurer. Despite being referred to two further insurance companies, no insurer had any knowledge of the clients' policy. It seems that no effective PPI policy was ever taken out, despite the clients being charged £2,970.

4.11 This illustrates how bad practice is seldom found in isolation and will lead to further bad practice if given the room to take hold and develop. It was argued at the beginning of this chapter that the nature of the PPI selling process makes it particularly prone to mis-selling problems and the many cases presented above demonstrate the forms these problems can take. However, this evidence also suggests a failure of the regulatory framework to properly consider why consumers are sold inappropriate PPI policies and how these could be prevented in future. Addressing these questions should be a priority for lenders, insurers and regulators.

How selling practices could be improved

4.12 Insurance intermediaries making a personal recommendation about an insurance product are required by FSA rules to assess the suitability of the product as against the consumer's demands and needs. This takes into account factors such as the level of cover compared to the risks the consumer wishes to insure against, the cost of the policy and any exclusion.[31] However, sales of PPI by lenders are classed as non-advised sales and information provided by the lender will often start by stating that they are making no personal recommendation. In this case the assessment of demands and needs means no more than printing a statement that the product meets the demands and needs of those who wish to make sure their monthly repayments will be covered in the event of illness, involuntary unemployment and so on.

4.13 However, lenders market the benefits of PPI in no uncertain terms and evidence presented above shows how policies can be very aggressively sold. Providing a key facts document, while useful, is not a sufficient safeguard. As the FSA itself points out, “markets for financial services are characterised by an imbalance of information and understanding between financial services firms and their customers”.[32] Lenders will often include the key facts information in the credit application bundle and it is often reproduced in very small print. Key facts policy summaries may only detail significant exclusions, and usually contain a statement along the lines of “Other exclusions and limitations apply to this policy – see the policy document for details”. However the full policy document is usually not made available to the consumer until after they have signed the agreement to buy the policy. It is therefore not difficult to imagine how this protection could be undone by an aggressive and determined sales pitch as evidence presented above shows. Lenders must be required to do more to ensure that borrowers receive products that are suitable for their needs. If this results in a lack of competition lenders will have little incentive to invest in the staff training and resources necessary to ensure consumers are equipped with sufficient information and capacity to properly assess the merits of a PPI policy they are offered.

4.14 Citizens Advice therefore recommends that the FSA revise the requirements for key facts policy summaries for payment protection insurance so that all exclusions from cover are clearly stated.

4.15 Borrowers also do not receive any information about alternatives to PPI such as other stand alone income protection insurance or even doing nothing if no suitable product is available. It is notable that PPI marketing tends to sell the benefits of abstract reassurance in general rather than the benefits of that particular product against any other. This is arguably the result of a sales process that has the consumer as a semi-captive audience once they have made a choice of credit product. The ancillary PPI agreement is sold as a secondary consideration.

4.16 Premiums and commissions from PPI sales provide a lucrative second revenue stream for lenders. Borrowers do not always have a sufficient level of financial literacy or capability to question the merits and cost of payment protection insurance. In these circumstances they can only trust that lenders are not acting against their interests. However, the experience of CAB clients

[31] *Financial Sevices Authority Handbook, Insurance Conduct of Business*, section 4.3
[32] *Treating Customers Fairly – progress and next steps,* Financial Services Authority (2004)

suggests that this is not always the case. Whether this is the result of staff performance incentives that place a higher value on the volume of product sales than on the wellbeing of customers is unclear from the evidence. What is clear is that many clients are being poorly advised or simply ripped off in PPI sales to their considerable detriment.

4.17 Citizens Advice believes that the FSA should review the regulation of PPI sales to ensure that no borrower is sold a policy that excludes them from cover on the basis of their circumstances at the time of sale. Because of the way PPI polices are sold, lenders should be placed under a duty to assess the suitability of PPI products. The current *no personal recommendation* regime underestimates the role lenders play in PPI sales and the complexity of PPI products.

4.18 In particular, we recommend that lenders should be required to provide borrowers with a clear and simple questionnaire containing a full list of circumstances that might make the policy unsuitable. A sale should not be concluded until the borrowers have completed this questionnaire, and then assessed by the insurer or by the lender on their behalf and this assessment is communicated to the borrower for their records.

4.19 The intention of this recommendation is to place a clear duty on both sales staff and the sales process to actively assess the suitability of the products they are selling. However this will only act as a safeguard if borrowers can be sure that this disclosure guarantees the protection they believe they have purchased.

4.20 Citizens Advice therefore believes that lenders should be required to honour the cover that a mis-sold PPI policy would have provided had the borrower not been excluded by circumstances referenced in the suitability questionnaire, or where no questionnaire was completed by a borrower before the sale was concluded. This commitment should be incorporated into relevant credit industry trade association codes of conduct, including the Banking Code, the Finance and Leasing Association code and the Mail Order Trade Association Code. Giving consumers protection with a guaranteed outcome would seem preferable to offering redress for bad practice that depends wholly on consumers' capacity to complain.

4.21 The problems we have highlighted relate to lenders as much as insurers, if not more so. It is lenders who select the policy they will market to their borrowers and PPI is often sold by a lender's in-house insurer. Therefore the content and sale of the policies is an appropriate subject for consumer credit regulation. Evidence from CAB suggests that while PPI mis-selling is widespread there is a concentration of deliberate bad sales practices in certain credit sectors. **Citizens Advice believes that the OFT should develop guidance on the sale and content of PPI products that would be consistent with fitness to hold a consumer credit licence.**

4.22 Amendments to the Consumer Credit Agreement regulations that came into force at the end of May this year introduce some additional safeguards for borrowers who buy PPI with their credit agreement, most notably a form of consent that must be signed by the debtor in some cases[33]. While this is welcome, evidence from bureaux suggests that this reform might have a limited impact at preventing high pressure sales. A warning in a signature box is no substitute for clear guidance and active compliance monitoring by firms themselves and the regulator

Conclusion

4.23 CAB evidence shows that borrowers are often sold payment protection policies which are completely inappropriate for their needs. In many cases, high pressure selling or unfair practices such as inertia selling has forced people to take out insurance which they cannot afford, do not want or need. This evidence suggests a failure of the part of regulators to address these issues. We consider that action is needed to ensure that lenders assess the suitability of PPI products for all potential customers before concluding a sale.

4.24 In the next chapter we look at CAB evidence in relation to problems people experience in trying to make a claim on their payment protection insurance

[33] The Consumer Credit (Agreements) (Amendments) Regulations 2004 amend the Consumer Credit (Agreement) Regulations 1983

5. Making a claim and being paid

5.1 Problems with insurance policies will not become apparent until the time comes to make a claim. It may only be at this point that consumers become fully aware of the implications of exclusion clauses or come to understand other limitations on their cover. People going through a major life event or personal trauma can find the administrative requirements of claiming intrusive, frustrating, obstructive and might also dispute the basis and outcome of decisions on their claims. In view of the problems CAB clients report with the content and sales of PPI, evidence of problems with administration and adjudication of PPI claims is also no surprise. This chapter examines CAB evidence on:

- Medical evidence
- Proof of unemployment
- Administration problems

Medical evidence

5.2 Borrowers have found it difficult to make a successful claim on their payment protection insurance due to requirements to provide medical evidence on their circumstances. One example of this relates to the common PPI term allowing claims on the basis of mental illness only where the borrower can provide a consultant's report. However 90 per cent of people experiencing mental health problems will be treated by their GP rather than a consultant.[34] This evidence requirement has caused problems for a number of CAB clients.

> A client of a CAB in Warwickshire had taken out a bank loan together with a PPI policy for four years cover that was paid in full. He later became ill with depression and was signed off work by his GP. He made a claim on his PPI policy but the insurer did not accept this, as the client did not have a consultant psychiatrist's report. The loan defaulted and the PPI proved useless.

> A Berkshire CAB saw a client who was suffering from severe depression and was unable to work. The client had a variety of debts including defaults on car hire purchase agreement. When he attempted to claim on the insurance policy, he was told that a letter from his GP was insufficient. Instead, he had to have a letter from a consultant in case of mental illness. The consultant's report was now ready, but the client had been asked to pay a sizeable fee before the report was released.

> A Gloucestershire CAB saw a client who was off work with depression. Although she had payment protection insurance on both her credit card and on a loan, she was told that she was unable to make a successful claim unless she could prove a consultant psychiatrist was treating her.

[34] *Fast Forwarding Primary Care Mental Health*, 2001, Department of Health

However, the client was actually receiving care from both a community psychiatric nurse and a psychotherapist.

5.3 Insurers are entitled to require medical evidence in support of claims from borrowers who have had to give up work due to illness or disability; but these requirements should not be so onerous as to jeopardise the borrower's ability to ever make a claim. For some CAB clients the costs of obtaining medical evidence are also a considerable barrier to claiming:

> A man sought advice from a CAB in Norfolk about a number of debts. At the time he was off work with a back injury. One of the client's debts with a catalogue company was covered by PPI. However the insurer insisted that the client produced a sick note every month. The sick note cost the client £15 each time, and the catalogue company was not prepared to pay the fee.
>
> A CAB in Northamptonshire reported the case of a client who was currently claiming income support. He had three credit card debts, all of which were covered by payment protection insurance. However, the insurance company would only pay out on the claim if the client supplied a medical certificate, for which the client's GP charged £25. As the client was on income support he was unable to afford this charge.
>
> A client of a CAB in Warwickshire was off work due to a long-term mental illness. His only income was statutory sick pay and so he made a claim on the insurance policy taken out with his car loan company. The insurer was happy to meet the £250 per month loan instalments but only as long as the client paid for a private doctor's letter at the cost of £25 per month. The insurer would not accept the sick note supplied free by his GP and accepted by his employer.

5.4 It is not reasonable for a borrower whose income has reduced through no fault of their own to be threatened with indebtedness by having to pay charges for medical evidence to make a claim on a payment protection policy. Indeed, we welcome the commitment in the CML baseline product to the principle that the insurer should meet the costs of obtaining any medical evidence that the borrower is required to produce. Many PPI policies do clearly state that the insurer will meet the cost of any medical report or examination that it requires. **Citizens Advice welcome this commitment and believe it should be incorporated into all PPI policies**.

5.5 It is not immediately clear from policy wording if this commitment extends to the costs of providing medical evidence from a GP or consultant who might charge the borrower for any letter or report. Evidence from bureaux show that such charges are widespread because GPs do not consider that these reports form part of their NHS contract. **Where insurers require initial or continuing medical evidence reports from a GP as a requirement of the claims process then the insurer should meet any charge that the GP might make.**

5.6 The evidence from bureaux also suggests that these claims should be few and far between. In the majority of claims arising from illness or disability, a GP's standard sick note should be regarded as sufficient evidence as it is for both employers and the Department of Work and Pensions[35]. Unless there are exceptional reasons, further requests for evidence appear to be deliberate barriers to borrowers claiming on the policy.

5.7 Policy wording that requires borrowers to seek evidence from or to be under the treatment of a consultant or other specified specialist medical practitioner acts as an arbitrary barrier to consumers trying to claim on them. Although further and additional evidence might sometimes be necessary, insurers should justify the need for such evidence in each case rather than relying on a standard clause. **Citizens Advice considers that the FSA should develop clear guidelines which set out when it is reasonable to request such additional evidence and when it would be unfair.**

5.8 This would also help with the unreasonable delay in the assessment of medical evidence experienced by one CAB client:

> A CAB in Berkshire reports the case of a client who took out a loan and paid for PPI. She had a serious car accident and being unable to work made a claim of the policy. Initially she was refused but later allowed to reapply, which she did. She repeatedly rang to check on the progress of her claim as she was by now experiencing severe financial difficulties. The bureaux then rang the lender's in-house insurance on the client's behalf to be told that her claim had been with the underwriters for medical investigation for two months with no action being taken.

5.9 It is also noteworthy that unreasonable requirements to provide medical evidence in support of a claim are a barrier to people claiming as a result of mental health problems. We believe that such practices are a form of discrimination in the way they single out mental health problems in a way that is unrelated to actuarial risk. The Disability Discrimination Act 2005 removed the requirement that a mental illness has to be clinically recognised for the person experiencing it to benefit from the protection of the 1995 Act it amends. Evidence from bureaux suggests that many of the people most affected by these evidence requirements should now be covered by disability discrimination law. **Citizens Advice therefore recommends that the Disability Rights Commission amends its guidance in respect of Regulation 2(4) of the Disability Discrimination (Services and Premises) Regulations 1996 to clarify that circumstances in which less favourable treatment is justified should not extend to claim procedures or to conditions of cover that relate to the nature of medical care rather than the effect of the mental illness itself.**

[35] For the first 26 weeks of a claim period, for people unable to carry out their *own occupation*, incapacity for work is evidence by a GP's certificate or evidence from another registered medical practitioner (such as an osteopath) where this is reasonable. See *Decision Makers Guide*, paragraph 13160, Chapter 13, Volume 3, Department of Work and Pensions

Consistency of approach

5.10 CAB clients also report problems with claiming benefits for unemployment. In many PPI policies, receipt of unemployment benefits is dependent upon registering for work with the Department for Work and Pensions and receiving jobseeker's allowance. Some policies we have seen seem to recognise that there are a number of circumstances in which people can be unemployed, actively seeking work but not entitled to receive jobseeker's allowance. In these circumstances, policies provide for payment of benefit if the borrower can furnish alternative proof of their unemployment and actively seeking work. Despite this. CAB clients who have become unemployed without receiving jobseeker's allowance have still been told that they cannot receive unemployment cover from their PPI:

> A CAB in Lincolnshire reported that a client came to them about her debts. She was working 16 hours per week when she took out loans for £6,500 and £2,600. She was also sold PPI policies at an additional cost of £2,727. The salesperson was aware that she worked part-time but insisted that the insurance was compulsory. The client was subsequently made redundant and made a claim on her insurance. However she was not eligible for income-based jobseekers allowance because her husband was in full time employment.

> A Devon CAB reported that a client had come to see them who had successfully been claiming on his payment protection insurance. He had been in receipt of JSA and able to provide the insurers with a Jobseekers Agreement. When he reached his sixtieth birthday, the Jobcentre told him he no longer needed to sign on for jobseekers allowance, as he was now eligible for pension credit. The client therefore lost his eligibility for insurance protection payments.

5.11 Problems of understanding and meaning are not made any easier by the way that PPI is tied to a particular credit agreement. Someone with more than one credit agreement might be covered by several policies sold by the same or different lenders. The opportunity for confusion if similar terms mean different things in different agreements is clear. While the development of the *consistency of interpretations* by the Association of British Insurers (ABI) gives some assistance here, CAB clients still seem to be getting turned away by insurers even when their claims are valid under the terms of the policy.[36]

> A CAB in County Durham assisted a man who had taken out a MPPI policy that included redundancy cover. The premium payments were up to date when he was made redundant. He had phoned the insurance provider for a claim form only to be told that he did not meet the conditions for a claim. The CAB phoned the insurer on the client's behalf to complain and was told that he did meet the conditions after all.

[36] The Adviser magazine, issue 97, *Raising the Game,* 2002

> A CAB in Berkshire advised a woman who had borrowed £3,000 to help her niece who was in financial difficulties. The lender also sold her a PPI policy even though she was over 65 and ineligible for some of its major benefits. She had been working part time but had to give this up due to back trouble. When she tried to claim of the policy she was told that she was ineligible as her back problems were pre-existing. She told the bureaux that she last had back problems twenty years ago. The lender is now threatened her with court proceedings.

5.12 In other cases, claims adjudicators have refused claims on the basis of their own interpretation of events despite contrary decisions or evidence from a more competent adjudicating authority. This causes hardship to individuals and has wider implications where decisions also undermine statutory rights elsewhere.

> A CAB in Northern Ireland reports the case of a woman who had a MPPI policy that included an own occupation illness clause. She developed a serious medical problem and was unable to work in her own occupation. The insurer refused to pay out on the basis that she could still be found fit to return to her own occupation even though both her GP and employer said that she would not.

> A CAB in London reported the case of a man with PPI on a credit card. The credit card insurer was refusing to pay out on a claim arising from unemployment. The client had previously been dismissed from his job for misconduct; however he had taken his employer to an employment tribunal and had won compensation. In contrast the insurer would not accept his claim because of the terms of his dismissal, and would not take into account the tribunal decision.

> A man sought advice from a Sussex CAB about a payment protection policy. The insurer disputed his claim on the grounds that he was self – employed. Subsequently, Inland Revenue have confirmed that the client was in fact employed. The dispute caused the client to incur further debt.

5.13 Statutory rights giving protection against bad employment practices increase job security and therefore reduce a major factor in the risk of credit default. Insurers should not undermine these rights by disputing the opinion of a more competent authority.

5.14 FSA rules place insurers under a general duty to deal with claims promptly and fairly and not to unreasonably turn claims down.[37] But this does not always translate into a guaranteed standard of practice that borrowers can rely on. Because people buying PPI with their credit agreements do not exercise consumer power, transparency in how they are treated by insurers is all the more important. A public commitment to customer satisfaction would act as a signal for lenders offering PPI to prospective borrowers and to regulators in

[37] See *FSA Insurance Conduct of Business rules* ICOB 7.3.1R and ICOB 7.3.6R

monitoring the decisions of insurers and lenders alike.

5.15 In the long-term investments sector the ABI has developed a *Raising Standards Quality Mark* (RSQM) that supplements FSA regulation by committing insurers to a measurable level of customer satisfaction. **We recommend that the Association of British Insurers establish a similar quality mark scheme for the PPI sector addressing the problems with claims administration and adjudication described above.**

Problems with hire purchase or conditional sale agreements

5.16 CAB clients report problems on a specific issue relating to hire purchase and conditional sale agreements, usually involving cars. Under the provisions of the Consumer Credit Act 1974 a borrower can end a hire purchase or conditional sale agreement regulated by the Act at any time before the final payment falls due by giving notice to the lender. The borrower must return the goods but by terminating the agreement in this way they can limit their liability to half the total agreement price less the payments already due.[38] This provides a vital protection for people facing financial difficulties who can reduce their potential indebtedness, albeit at the cost of losing the goods they have been paying for.

5.17 Hire purchase and conditional sale agreements are commonly sold with PPI which is usually sold as a one-off premium added to the credit agreement. But bureaux are reporting that when clients exercise their right to terminate the hire purchase or conditional sale agreement they are told that the PPI policy cannot be cancelled. What is worse is in these credit arrangements the borrower usually pays a one off up front PPI premium funded by additional lending charged at the main agreement rate. Lenders are refusing to terminate these ancillary loans or bring about the refund of premiums as evidence from bureaux demonstrates.

> A woman came into a CAB in Yorkshire after having problems with a conditional sale agreement. The goods had to be repaired twice and then the woman had a reduction in working hours. With all this she decided to terminate the agreement. However, she received a demand from the conditional sale company for an outstanding balance that includes a PPI premium of £850 and mechanical breakdown insurance of £550, neither of which could be cancelled.
>
> A man who had taken out an HP agreement to buy a car approached a CAB in Berkshire. He said that he was also forced to take out additional insurances. The insurance was attracting interest at 29 per cent and could not be cancelled with the main agreement.

5.18 The main trade body for this sector is the Finance and Leasing Association (FLA). The FLA lending code for consumers commits the association's

[38] See sections 99 and 100 of the Consumer Credit Act 1974. The borrower would also have to pay any outstanding arrears that had already fallen due and any compensation for damage to the goods beyond that caused by reasonable use

members to tell consumers how they can cancel PPI and receive a refund of the premium if they settle the main loan agreement early. This is a welcome development of the FLA lending code. However, this is not sufficient, as this does not require FLA members to only sell insurance that does offer full refunds of the premium on early settlement or cancellation of the credit. **Citizens Advice believes that the Finance and Leasing Code of Practice needs to be amended in this respect.**

5.19 As useful as code commitments are, they are only effective against persistent bad practice if individual lenders take steps to ensure compliance and compliance is adequately monitored by independent supervision. The evidence from experiences reported by CAB clients suggests that this is not always working well at present.

5.20 We believe that the nature of this evidence calls for further investigation by industry regulators, although there appears to be a regulatory gap here. While the FSA oversees general insurance, the insurance conduct of business makes no explicit mention to the peculiarities of PPI refunds if the main credit agreement is terminated. Likewise the Office of Fair Trading (OFT) oversees consumer credit, but has no specific brief on general insurance. However, both regulators share a general concerns with good practice through principles of fairness and fitness respectively[39]. However, because this particular problem relates to a specific market sector, initial investigations by the FLA might be appropriate and efficient.

5.21 Citizens Advice recommends that the FLA should ensure active compliance monitoring of its lending code general insurance commitments as a priority. This should concentrate on the highest risk sectors and fully investigate the causes and extent of problems with PPI after the termination of hire purchase and conditional sale agreements. The findings of this report should be made available to regulators and consumers. The FSA and OFT should be prepared to take further regulatory action if required.

Delays in making payments under the policy

5.22 Compliance monitoring by industry regulators is vital in protecting consumer interests. But it is always going to be time consuming and only able to deal with bad practice after the event. In this respect, it will always be a second best option to the active commitment of firms themselves in developing and sustaining best practice in all aspects of their everyday business. We are therefore particularly disappointed to receive evidence of lenders threatening borrowers with recovery action or making additional default charges because of minor delays in receiving PPI payments. As most PPI policies are taken out to repay a particular credit agreement, it is reasonable to expect that payments from the policy should be synchronised with the dates payment is due on the credit agreement:

[39] FSA principle six requires insurance firms to pay due regard to the interests of its customers and treat them fairly. The requirement on consumer credit businesses to be fit to hold a credit licence follows from section 25 of the 1974 Consumer Credit Act 1974.

A client of a CAB in South-West Wales had two loans with PPI from the same lender. She was made redundant and the monthly loan repayments were covered by PPI. But they were debited from her current account on the second day of each month whereas the PPI payments were not paid into the account over two weeks later. In the meantime, she inadvertently exceeded her overdraft limit and the bank charged an excess overdraft fee of £80 per month. It was only after an intervention by the CAB that the lender said they would investigate the problem and organise for the payments to co-ordinate.

Another CAB in South-West Wales saw a client who became permanently disabled following an accident three years ago. The client had two credit cards, both with payment protection insurance. During the last three years the insurers had been making payments. However, they recently informed him that they have repaid the amounts outstanding at the time of his accident and that therefore ended their duty to him. The client was shocked to discover that he still owed £5,000, even though he had not used the cards at all since his accident. It transpired that both companies had been adding interest to the balances and also at times late payment charges. The client had no prospect of being able to repay the debt, which he believed was covered by the insurance.

A CAB in Hampshire advised a woman whose daughter had taken out a loan with PPI. The client's daughter was made redundant and the PPI policy covered payments of the loan. However the PPI payments were always made a few days after the due date. The lender continued to charge interest on the late payments and then passed the accrued debt to a debt collection agency who threatened court action. The client consulted the Financial Ombudsman Service who confirmed that this debt was the responsibility of the lenders in-house insurer, but the case would take three months to be resolved. Meanwhile the debt collector refused to put the matter on hold.

5.23 FSA rules on claims handling place insurers under a general duty to deal with claims promptly and fairly and not to unreasonably turn claims down. But too many CAB clients find that the administration and adjudication of PPI claims is unduly bureaucratic, insensitive to the position of people in financial difficulties and paradoxically responsible for increased indebtedness.

5.24 Citizens Advice believes that good practice in arrears management should start from the premise that lenders and their agents should do nothing that unnecessarily increases the size of a person's indebtedness. However this evidence suggests that default charges and collection action can be triggered by seemingly petty delays in PPI payments. **Citizens Advice recommends that the Banking, Finance and Leasing Association and Mail Order Trade Association codes of practice should commit their members to refrain from making any additional default charges or taking recovery action whilst a PPI claim is either pending or in payment. The codes should**

also specify these requirements should also apply where the debt has been passed to an external debt collection agency. In this case we would expect the Credit Service Association, the trade association for third party debt collection agencies makes similar amendments to its code of practice.

Conclusions

5.25 In this chapter we have looked at barriers to claiming on payment protection insurance policies, including unreasonable and costly requests for medical evidence, and delays in making payments under the policy.

5.26 PPI could and should provide an effective and accessible safety net against indebtedness; however for too many CAB clients this is currently not the case. The failure of PPI to provide this safety net for too many CAB raises wider competition and responsible lending questions that we believe require further investigation. This will be taken up in the final chapter.

6. Closing the gaps

6.1 This report has argued that PPI is failing as a safety net for CAB clients facing financial difficulties in four main respects.

- The price that borrowers pay for PPI is often equivalent to a large proportion of the credit advanced and lenders will often charge additional interest on this as well
- The design of many PPI products excludes important and common life events and provides insufficient cover when borrowers encounter the most severe problems
- The sales process of PPI products means too many people have policies that are unsuitable for their needs, and
- It appears that the cost of PPI gives poor value for money for many borrowers.

6.2 Some of these points have been raised before by a variety of commentators; not least by Citizens Advice in a 1995 evidence report on the effectiveness of mortgage payment protection policies as a safety net for borrowers.[40] It is of great concern to us that, ten years later, borrowers are still experiencing similar problems. The persistence of similar problems over time suggests that not enough has been done to address failures in the broader PPI market in the intervening period. We believe that this points towards gaps in the way that PPI is regulated.

The regulatory gap

6.3 The current system of regulating PPI has not led to consistency. PPI policies of all different standards are offered to borrowers and practices vary tremendously. The problem is that lenders who treat their customers fairly can be undermined by the practices of others:

> A specialist CAB debt advice service in Yorkshire reported that a couple had taken out payment protection insurance in respect of a secured loan and their first mortgage. Payments with the secured loan company were up to date when the husband suffered a heart attack in April 2005. The wife phoned both the first mortgage lender and the secured mortgage company to request insurance claim forms. The first mortgage lender sorted out her claim quickly. However, she did not receive a claim form from the secured loan company and, despite repeated telephone calls to request this, she still did not receive it. Meanwhile, the secured loan company issued possession proceedings and their claim was heard, and adjourned.

6.4 This suggests that good practice cannot just be left to the market. There is a clear co-ordination role for regulators.

[40] *Security at risk – CAB evidence on payment protection insurance and implications for public policy,* National Association of Citizens Advice Bureaux (now Citizens Advice), June 1995

6.5 But, because of the way that PPI straddles the jurisdiction of several regulatory regimes covering insurance, consumer credit and competition issues respectively, no single regulator has their eye on the whole ball.

6.6 After taking responsibility for regulating general insurance in January 2005, the FSA announced its intention to investigate aspects of the PPI market. However this will not extend to competition issues which the FSA clearly state as outside its remit. It is also not clear whether this investigation will probe into the content of policies, although this is clearly a key factor in determining the effectiveness of PPI as a safety for borrowers. The adequacy of product content and design certainly is within the remit of the FSA as shown by the emerging *treating customers fairly* initiative.[41] **While Citizens Advice warmly welcomes this investigation into the PPI market, we recommend that the FSA investigates whether PPI policies are treating their customers fairly in respect of the product design, price, the extent of risks covered and in particular the operation of exclusion clauses.** This would be a necessary first step in establishing the content of a regulated baseline product that we have argued for in this report.

6.7 In respect of the competition issues raised by the way PPI is sold, the OFT has a specific power under section 131 of the Enterprise Act 2002 to make a market investigation reference to the Competition Commission if it "…has reasonable grounds for suspecting that any feature, or combination of features, of a market in the United Kingdom for goods or services prevents, restricts or distorts competition". The OFT has already made one such reference to the Competition Commission in respect of PPI in the amended terms of reference of the ongoing store cards market enquiry [42]. **We believe that the evidence from CAB casework presented in this report makes a strong case for the OFT to undertake a market investigation into the sale of PPI with credit products more generally.** If the Competition Commission finds that features of PPI sales in the store card sector do distort competition then the argument for a market investigation of PPI more generally will become compelling.

6.8 It is also the case that much of the evidence of bad practice with PPI sales reported by CAB clients relates not to insurers but to lenders. Mortgage lenders are generally covered by the FSA *Mortgage Conduct of Business Rules* while other secured and unsecured lenders are regulated by the OFT under the provisions of the Consumer Credit Act 1974. While the broad regulatory powers to deal with many of the problems CAB clients experience with PPI are either in place or on their way[43], at present neither jurisdiction states clear standards of conduct for lenders in respect of their handling of PPI products. We believe that there is also a danger that the division of responsibility between regulators creates a gap for consumers to fall into; the

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[41] *Treating Customers Fairly – progress and next steps*: Financial Services Authority 2004
[42] The amended reference is available on the Competition Commission website at: http://www.competition-commission.org.uk/inquiries/current/storecard/index.htm
[43] At the time of writing the Consumer Credit Bill going through parliament proposes to give the OFT a better system of licensing backed up with the sanction of civil penalties. The Bill also proposes to empower courts to deal with unfair credit relationships. This could include sales of PPI.

evidence relating to consumer termination of hire purchase agreements and problems with PPI being a case in point. **We recommend the FSA and OFT work closely together in developing guidance on standards of conduct for all lenders promoting and selling PPI along with a joint regulatory strategy ensure that the content of the policies offered by lenders are fair to all of their customers.**

6.9 A concerted focus on PPI by consumer regulators might also yield some additional benefits over the longer term. There is widespread support for measures to improve consumer understanding of financial matters from levels that the FSA describe as 'worryingly low'.[44] PPI is a financial product commonly purchased by people who might not otherwise come into contact with financial products. The act of choosing whether to buy PPI involves considering risk, planning into the future and understanding how financial products relate to personal circumstances. These are all central themes of the financial capability agenda which makes the relative silence of consumer regulators on PPI issues all the more difficult to understand.

6.10 This silence is perhaps indicative of a broader failure to recognise the importance of PPI in the context of responsible lending. As the consumer credit markets have grown in size and economic importance, credit products have arguably become more important in maintaining standards of living. For instance, research into credit use by low income households shows the importance of borrowing to buy necessary items and make up short falls in incomes.[45] Likewise increased levels of home ownership bring more people into contact with the market for mortgages and other secured credit products. This aspect of credit has been both recognised by government and encouraged to develop further in two recent policy initiatives. Firstly the Financial Inclusion Fund aims to extend access to affordable credit for low income households by supporting third sector lenders such as credit unions and secondly the Homebuy initiative aims to make buying a home easier for people on lower incomes.

6.11 While increased use of credit can improve our lives, the key question that this report asks is what happens when things go wrong. We do not believe that is it right to leave borrowers to shoulder the risk of income shocks in their own way as both lenders and government benefit from increased credit use, albeit in different ways.

6.12 The core problem of over-indebtedness is striking a balance between easy access to affordable credit and the costs of unmanageable debt to both the individual and society as a whole. This is a question of responsible lending, not merely a technical question relating to data sharing and transparency but to the wider settlement between lenders, consumers and indeed government as to how these costs should be shared.

[44] *Restoring confidence in long term savings,* Treasury Select Committee 2004

[45] See for instance, *Access to credit on a low income*, Paul Jones (2001), *Would you credit it?* Paul Jones and Tina Barnes (2005) and *Affordable credit: the way forward*, Elaine Kempson and Sharon Collard (2005) for research on income use by lower income households

6.13 We believe that PPI is under-regulated because it does not sufficiently internalise the costs of debt and in too many cases it leaves borrowers shouldering too much of the risk while paying a premium for cover. PPI is a private, market response to debt. While regulators can deal with problems of practice, iron out distortions in competition or produce a perfect baseline product from a borrower's point of view, they cannot force any insurer to underwrite it or indeed any lender to sell it. This requires the co-operation of insurers and more particularly the credit industry that may have to forgo revenues to produce a better value PPI product for borrowers.

6.14 Therefore the success or failure of PPI as a remedy against indebtedness will be closely related to the question of incentives for both lenders and borrowers to make PPI work. As the scope of such an investigation is outside the remit of any individual regulator we believe that Parliament should inquire into this most important welfare issue. **Citizens Advice would like to recommend that the Treasury Select Committee investigate PPI as a pressing matter in its own right.**

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Appendix 1: The Citizens Advice PPI product baseline

In this report we have argued that the content of many PPI policies we have seen provides borrowers with insufficient cover against even the most common risks of credit default. This Citizens Advice baseline is intended to provoke discussion of the degree of cover that we believe an effective product baseline should contain. It is not comprehensive in the manner of a key facts document, rather stating some of the main points where we believe PPI polices currently provide borrowers with too little protection.

General principles

This product baseline sets the minimum standard of cover required for PPI policies offered to borrowers in the course of the sale of a credit product. Lenders may offer PPI products that exceed this standard if they wish.

As a minimum standard the baseline should provide effective cover against the risk of credit default arising from adverse life events that lenders could reasonably foresee at the time that the credit product subject to cover was sold.

A credit risk should only be excluded from cover where it is genuinely considered to be uninsurable. There should be no blanket exclusions where this is not the case.

Effective cover means that borrowers who have bought PPI should not find themselves exposed to debt if an insured risk arises. Payments in respect of an adverse event should continue for as long as the event has an adverse effect on the borrower subject to reasonable requirements for borrowers to mitigate.

Lenders should not take any action to recover overdue repayments nor add additional default charges to credit agreements in respect of which the lender has sold PPI while the premiums are up to date.

Borrowers claiming on a PPI policy should not be subject to unwelcome surprises. Policies must not include unreasonable requests for evidence and where further evidence (particularly medical evidence) is required to decide a claim the insurer should meet the cost of its production.

The content and administration of PPI should treat customers fairly in all respects.

People whose risks are covered

The base line product should cover any borrower named on the loan agreement.

Risks covered

Life cover
The loan balance should be cleared should the borrower or other relevant person die.

Involuntary unemployment
- Redundancy

- Self-employment where the business has ceased trading
- Self-employment for periods where the business produces insufficient returns for the borrower to meet their credit commitment and reasonable living standards. *Evidence of deterioration in business conditions since the loan was granted in addition to evidence of actively seeking work would be required. Evidence from Jobcentre Plus or Pensions Service that the borrower meets the conditions of entitlement to jobseekers allowance, income support or pension credit should be accepted as proof of this.*
- People employed on temporary contracts will be covered where their contract lasts for more than 12 months and has been renewed once previously. In other cases, people on temporary contracts whose contracts are terminated early will be covered from this date until the date on which the contact would otherwise have ended.
- There should be no upper age barrier to cover against the risks of unemployment as long as the borrower is employed.

Unemployment through caring responsibilities
A need to provide substantial care for a sick or disabled relative where there is no other reasonable alternative. Reasonable evidence of the need for care can be required.

Relationship breakdown
To cover the borrower against a drop in income resulting from the breakdown of a relationship where the borrower's ability to meet credit repayments is wholly or mainly dependant on the income of a partner and this was known to the lender when the loan agreement was made.

Accident and illness/disability
This should cover a borrower against the risk of being unable to work because of accident, illness or disability. There should be no unreasonable exclusion from this cover of particular categories of illness of disability. Bad backs and mental health problems should be specifically included without requirements to provide unreasonable levels of medical evidence.

There should be no upper age barrier to cover loss of earnings through illness or disability as long as the borrower was in employment at the time the policy was taken out.

Insurers should meet the cost of obtaining medical evidence required to make a decision on the claim.

Significant reduction in income
Covering a borrower where they, or the other relevant person, experience an unforeseen reduction of earned income greater or equal than the monthly credit repayment.

Benefits

- Benefits for unemployment, caring responsibilities, relationship breakdown, accident and illness/disability and significant reduction in income should accrue on a daily basis and be paid monthly.

- Benefits for accident/illness/disability should continue to be paid until the loan balance clears or the borrower is capable of working.

- Benefits for caring responsibilities should continue to be paid until the loan balance clears or the borrower ceases to be a carer.

- Benefits for unemployment should continue to be paid until the loan balance clears or the borrower enters employment as long as the borrower continues to prove that they are actively seeking work.

- Benefits for relationship breakdown and significant reductions in income should be payable for a reasonable period of adjustment of six months.

Appendix 2 – comparison of CML and FLA baselines for payment protection insurance

Issue	CML baseline[46]	FLA baseline
Risks covered	The benefit is paid if the person insured is unable to work due to: • accident or • sickness or • unemployment (which is involuntary)	An FLA creditor product will offer at least one of the following covers: Life, Accident and Sickness and Redundancy Where any of the above covers are provided, the following minimum standards will apply.
Eligibility to apply	The applicant must: • be aged between 18 and 64 (unless otherwise stated); • live in the United Kingdom, the Channel Islands or the Isle of Man; • be working in the United Kingdom, the Channel Islands or the Isle of Man; • either be applying for a residential mortgage or have a residential mortgage that is not in arrears; • be in paid full time employment (including self employment and contract work) and • have been continuously employed for at least the previous six months at the date of application.	The applicant must be: • A minimum of 18 years of age at the commencement of the agreement and cover could terminate as early as 65 years of age. • A UK resident, although cover will be extended to those working for the armed forces or as civil servants in British embassies or consulates. In addition, if the cover provided is Accident and Sickness or Redundancy the customer must be in work for a pre-determined amount of time before the cover is taken out.[47]
Initial qualifying period	**For unemployment only** • 60 days from the date of completion on a residential property (for cover arranged at the same time as the mortgage)	90 days initial exclusion period (from policy inception)

[46] The CML baseline also sets out requirements in relation to linked claims, re-qualification periods and minimum periods of notice for changes to the policy which have not been reproduced here
[47] The market definition of 'in work' varies between providers. The ABI's Statement of Principles on Creditor Consistent Policy Interpretations provides guidance.

Issue	CML baseline[46]	FLA baseline
	• 120 days from the date of application for cover (for cover arranged after the mortgage)	
Excess period (for each claim)	60 days	*No specification*
Benefit payment basis	Daily benefit, payable monthly in arrears	*No specification*
Benefit period	12 months for any one claim, subject to the length of individual claims	Cover will usually match the term of the loan but where it does not, the FLA member will write to the customer when cover is coming to an end.
Insured person	Any named mortgage applicant or existing borrower	To be eligible for cover, a customer must be at least the first named party on the credit agreement
Monthly benefit	Not less than the full monthly commitment to the lender at the start of the mortgage. The monthly benefit will be adequate to cover the monthly mortgage payment at the start of the mortgage	No guidance to be provided within these minimum standards
Claims eligibility (contract workers)	1. regularly renewable 2. individually negotiated Covered if: • on a yearly contract which has been renewed at least once, or • under contract with the same employer for a period of at least 24 months. Covered if at least 6 months with the same employer and the contract has been renewed at least twice • unemployment benefit paid only if contract terminated early • unemployment benefit ceases at the end of the contract term.	Customers employed on seasonal, fixed term contracts, casual or temporary employment will be excluded from cover

Issue	CML baseline[46]	FLA baseline
Claims eligibility (self employed)	The self employed will be covered if: • they have involuntarily ceased trading and declared this to the Inland Revenue and • they have registered for jobseekers allowance at the appropriate office in the United Kingdom (or equivalent in Channel Islands or Isle of Man)	Self-Employed customers – redundancy cover is not available to the self-employed. However, alternative benefits will be made available in place of the redundancy benefits.
Temporary earnings during a claim period	Will be allowed, in effect suspending claim payment for the period of temporary work.	*No specification*
Exclusions	***For accident, sickness and unemployment:*** • any pre-existing medical conditions for which treatment had been given or diagnosis had been made or investigations had commenced during the 12 month period before cover commences • pre-existing chronic or continuing disease • self-inflicted injuries • alcohol abuse • drug abuse • war, invasion etc. • radioactive contamination • pregnancy ***For unemployment:*** • casual or temporary work • when unemployment is a seasonal occurrence • known or impending unemployment • voluntary unemployment	***For life cover:*** • AID'S and HIV[48] • War, riots, invasion • Radioactive contamination • Suicide • Drug and alcohol abuse • Pre-existing medical conditions[49] ***For accident and sickness cover:*** • Events listed under life cover above; and • Back related conditions • Mental disorders • Normal pregnancy • Cosmetic surgery or resulting from cosmetic surgery ***Redundancy cover:*** • Events listed under life cover above; and in addition • Voluntary termination of

[48] Some providers have now removed their AIDS exclusion. For the purpose of the baseline AIDS can be excluded, as providers are free to improve on the baseline.
[49] Can be excluded. The ABI's Statement of Principles on Creditor Consistent Policy Interpretations provides guidance.

Issue	CML baseline[46]	FLA baseline
	• unemployment caused by misconduct • a period of unemployment for which pay in lieu of notice has been received	employment • Redundancy known about or impending at the start of cover • Where alternative employment has been refused • Overseas employment • Close companies • Periods of unemployment for which a payment in lieu of notice has been made.
Medical evidence	Normally the doctor's report is sufficient. The borrower pays for this at the commencement of the claim. If further specialist medical evidence is required by the insurer, the cost is met by the insurer in line with the standard fee structure as set out by the BMA.	*No specification*
Policy wording interpretations	No specification	ABI's Statement of Principles on Creditor Consistent Policy Interpretations provides guidance.

Appendix 3 – List of Citizens Advice Bureaux that submitted evidence between January 2004 and April 2005

EAST REGION
Bedford
Broxbourne
Bury St Edmunds
Bushey
Cambridge and District
Chelmsford
Colchester
Dereham
Diss and District
Elstree and Borehamwood
Ely
Felixstowe and District
Fenland
Harlow
Haverhill
Huntingdon
Ipswich and District
Leighton Linslade
Leiston and Saxmundham
Mid-Bedfordshire
Mid-Suffolk
North Hertfordshire and District
Peterborough
Southend-on-Sea
Stevenage
Tendring
Ware and District
Watford
Wickford

LONDON REGION
Beddington and Wallington
Beckenham and Penge
Bow
Camden HIV Housebound Project
Enfield Town
Finchley
Greenwich MAS
Hillingdon
Holborn
Kensington
Kingston and Surbiton
Merton and Lambeth
Morden
North Paddington
Palmers Green
Peckham
Pimlico
Richmond
Roehampton
Tottenham
Sheen
Sydenham
Thornton Heath
Wandsworth MAS
Whitechapel

MIDLANDS REGION
Ashfield
Bedworth and District
Beeston
Biddulph
Birmingham City Centre
Birmingham North District Health Unit
Burton-upon-Trent
Charnwood
Chesterfield
Cradley Heath
Daventry and District
East Lindsey
Erewash
Grantham and District
High Peak
Kingstanding
Lichfield
Lincoln and District
Lutterworth
Malvern Hills District
Mansfield
Melton Mowbray
Newcastle-under-Lyme
Northfield
Northampton
North Warwickshire
Oswestry and Border
Redditch
Rugby
Rugeley
Rutland
Shirley
Shrewsbury
South Shropshire
Sleaford
Solihull
South Holland
Stamford and District
Stoke on Trent
Stone
Stourbridge
Stratford Upon Avon
Tamworth
Walsall
Warwick District
Wellingborough
Worcester
Wychavon District
Wyre Forest

NORTH REGION
Barnsley
Batley
Bradford
Blyth Valley
Calderdale
Darlington
Derwentside
Doncaster
Gateshead
Hambleton
Hartlepool
Hull City Centre
Leeds
Newcastle City
North Tyneside
Redcar and Cleveland
Rotherham
Ryedale
Scarborough and District
Scunthorpe and District
Selby District
Sheffield DSU
Shipley

Stockton and District Information and Advice Service
South Elmsall
Tynedale
Wansbeck
Washington
Wear Valley
York

NORTH WEST REGION
Atherton
Barrow-in-Furness
Birchwood
Birkenhead
Blackpool
Bolton and District
Burnley
Carlisle
Chester
Chorley and District
Crewe and Nantwich
Crosby
Cumbria Rural
Eden
Harpurhey
Lymm
Macclesfield and Wilmslow District
Manchester Central
Manchester District Projects Team
Marple and District
Middleton
Morecambe and Heysham
Northwich
Old Trafford
Prestwich
Rochdale
Rossendale
Salford
Skelmersdale
South Lakeland
Southport
Tameside
Toxteth
Warrington
Wallasey
Wigan

NORTHERN IRELAND
Central Belfast
Downpatrick
Shankhill

SOUTH EAST REGION
Addington
Aldershot
Andover
Ash
Basingstoke
Bexhill and Rother
Bicester
Bishop's Waltham
Bognor Regis
Bracknell
Brighton and Hove
Camberley
Caterham and Warlingham
Crawley
Chiltern
Dartford
Didcot and District
Dorking
Eastbourne
Esher and District
Farnborough
Faversham and District
Fleet and District
Godalming
Gosport
Guildford
Haslemere
Hastings and Rother
Havant and District
Haywards Heath
Heathlands
Henley and District
Littlehampton
Lymington
Maidenhead
Medway
Milton Keynes
Oxford
Oxted
Reading
Reading Community WRU
Romsey and District
Runnymede
Seaford
Sevenoaks
Southampton
Thanet
Tunbridge Wells
Uckfield
West Berkshire
Winchester
Woking
Worthing and District

SOUTH WEST REGION
Bath and District
Bristol
Bude, Holsworthy and District
Cheltenham and District
Christchurch
Cirencester
Dorchester and District
Exeter
Frome and District
Kennet
Mid Devon
North Cornwall
North Somerset
North Wiltshire
Okehampton
Plymouth City Centre
Purbeck
Salisbury and District
Saltash
South Gloucestershire
South Somerset
Stroud
Swindon and District
Taunton and District
Tavistock
Teignbridge
Torbay
West Oxfordshire

WALES
Abertillery

Ammanford	Haverfordwest	Powys
Carmarthen	Llandudno	Swansea
Chepstow	Neath	Torfaen
Colwyn Bay	Newport	Vale of Glamorgan
Gwynedd	Port Talbot	Ynys Mon