

Case Study: If we had the chance to do it all again, would we?

Lessons from the great British PPI truth and reconciliation scandal

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Summary

- A failure of ethics drove the mis-selling of a product that, sold properly, had a benefit to consumers.
- Some form of replacement for PPI might be possible in the future but this must be a fair, simple to understand and transparent product offering.
- The customer must come first and that focus starts with business leaders.

About 16 million payment protection insurance (PPI) policies have been sold since 2005. In terms of the number of policies held, and theoretical coverage of risk, PPI was a very successful product. To a nation exhibiting a huge appetite for consumer credit during the last decade, PPI understandably had wide appeal. Consumers taking on this insurance were acting responsibly, to protect themselves and the lender, and other consumers, from downside risk. Peace of mind for all concerned. But it is now widely accepted that, for the customers who bought them, these products were just not going to do what they seemed to say on the tin, or they were positively mis-sold.

The financial services industry is now paying the price of those errors. In November 2012, the amount set aside by 14 banks, building societies and credit card firms for dealing with this issue, including paying compensation, stood at just under £13bn. And in February 2013, Lloyds Banking Group announced it had set aside a further £1bn, bringing its PPI bill to £5.2bn so far.

With the number of complaints rising, and potentially more to come, banks are now calling for a cut off point for claims. In January 2013, the Financial Ombudsman Service (FOS) reported a record quarter in the number of complaints received, with complaints overall up 75% and most of those (80%) being about PPI. The FOS received more complaints in the first three months of 2013 than in any whole year up to 2010. The FOS has now received half a million PPI complaints, a rate of 400 every hour.

What's worse is that, while these cases are the ones rejected by the banks and other lenders, the FOS upholds the vast majority of complaints: about 70%, on average – in favour of the customer. Some customer uphold rates are in excess of a shocking 90%. These are all cases where the customer was right and in which the financial institution could have resolved the issue more quickly and cheaply.

Moreover, Citizens Advice, which made the “SuperComplaint” about PPI in 2005, has now thrown the spotlight on the burgeoning claims management market offering to help consumers with their claims. In a report last year, it reported that nine out of ten people surveyed had been pestered by calls, emails and spam texts from these firms within a period of 12 months – with 72% of those contacts about making a claim for PPI.¹²

¹² Claims Pests, Citizens Advice, 2012

Citizens Advice has found that people are spending, on average, over £1,100 in fees for something they can do themselves, free of charge. One Citizens Advice Bureau (CAB) even saw a client who paid over £4,000 in charges to a claims manager. Some claims firms are charging upfront costs of £600 – without being clear if the consumer will get any sort of payout. One in five CAB clients was lead to believe they can make a claim for PPI without ever having, or being mis-sold, a policy. Many other problems, including misleading information and poor service, abound.

So it is perhaps timely to reflect on what has brought us to this point, whether there are any lessons for the future, and whether there is any possibility at all of rehabilitating PPI.

When did it start?

Citizens Advice Bureaux help people resolve problems with debts they cannot afford to repay. Every year for the last decade, around two million debt problems have arrived at the door of the bureaux, and most of those have concerned consumer credit debt. People usually need help with debts when they have experienced an unexpected financial shock and just cannot make ends meet – a loss of job, relationship breakdown, or bereavement are very common factors. So too is the simple fact of low income and the cost of living – coupled with a burden of servicing borrowing. Where a consumer has any insurance that might replace lost income, or pay off any debts, it is, in theory at least, really helpful. So the CABs always look to see if that is a possible solution. We also advocate that people borrowing money should not take on more than they can afford, and that they should be clear about how they could afford to repay, including if something goes wrong.

We first started to highlight concerns about weaknesses with payment protection products in 1995. At that time, the key concern was with mortgage payment protection insurance (MPPI). There had been record levels of mortgage repossessions, set against a period of high unemployment and high interest rates. Government was about to cut the social security benefits to help with mortgage interest, on the basis that the private sector (in the form of MPPI) should cover part of the cost. We were concerned that private cover could not be relied upon, because of our evidence on:

- mis-selling
- exclusion clauses
- products that might have been suitable when originally taken out no longer were, due to a change of circumstances, or because the insurance company changed the terms at short notice
- poor administration and standards of service by insurance companies

We recommended that the Government should implement statutory regulation of general insurance, but failing that, the Association of British Insurers (ABI) could develop better self-regulation of PPI, and there should be a minimum standard, or baseline set of product features, which all MPPI policies should meet.

By 2003, we were reporting on a tidal wave of consumer credit debt problems. In our report *“In too deep”*, we examined our clients’ debt problems, including whether they had any insurance. While the majority of our clients, 60%, cited a change of circumstance as responsible for their debt problem, only 11% of the debts in the survey actually had PPI associated. And where they did, the limitations of the policy meant that clients could only make claims in a quarter of these cases. Even fewer were successful – 1.7% of all the debts in the survey. Reasons for rejecting the claim included common exclusion clauses. As the FSA was about to take on the regulation of general insurance, we recommended that, it should take into account the findings of our report when formulating PPI regulation.

Almost concurrently to this, in September 2005 we published an in-depth report on PPI, which we submitted to the Office of Fair Trading (OFT) as a “SuperComplaint” under our then-recently conferred special powers.¹³ We were continuing to see a substantial and growing number of cases of mis-selling expensive and inappropriate PPI products to clients. While the FSA had started a ‘probe’ into PPI, we were unsure that its action would tackle the problems we were seeing, as it wouldn’t look at competition issues and it was unclear whether the probe would look at the content of policies. At this time, the FSA approach was predominantly about transparency and disclosure and we felt that a more interventionist response was needed.

We therefore decided to submit our evidence as a Supercomplaint, to raise the profile of the issue and demand a response from the regulatory community. The report outlined our evidence on mis-selling, the cost and cover provided by banks/insurers, exclusion clauses, and problems with claiming. We were particularly concerned about single premium policies sold with bank loans, where the customers we spoke to had borrowed the money to fund the premium as part of the loan. We were given the strong impression that taking the insurance was the key to being able to get the loan. We recommended a wide range of measures to improve consumer information and transparency, and the introduction of a baseline/standard product design for PPI.

The Supercomplaint had an immediate impact on the share prices of a number of banks, with the stock market rightly seeing this as a threat to profits from the sale of PPI. We received a lot of dismissive and aggressive responses from the industry, perhaps due to the scale of reliance upon this product for rewards, as revealed by the subsequent investigations by the OFT and Competition Commission (CC).

The issue trundled through the in-trays of the OFT, CC and FSA for almost a decade (see the timeline in Box 1). Meanwhile, more and more was uncovered from the frontline, which simply backed up our initial insight that consumers just were not getting a good deal.

Box 1: Key points in the timeline of shame

November 2005 – FSA ‘probe’ finds:

- poor disclosure of product and price details;
- the possibility that consumers may not be eligible to claim against their policies;
- that customers might not be aware they could receive little money back if they cancelled their policies early;
- advice given on buying PPI was likely to be poor, with a lack of proper monitoring and training meaning that staff in around half the firms in question were not competent;
- using sales commissions or bonuses to pay employees was encouraging some staff to mis-sell the policies; and
- product regulation would stifle competition.

December 2005 – the OFT issued its response to Citizens Advice Supercomplaint.

- It decided to undertake a market study on the selling and competition issues that our Supercomplaint highlighted.

January 2006 – FSA writes to companies asking them to improve sales practices.

- Confidential undertakings given.
- FSA working with the trade bodies to come up with a self-regulatory response.

13 Citizens Advice, Protection Racket, Sep 2005. Citizens Advice is one of eight designated consumer bodies conferred with powers under the Enterprise Act 2002 to submit to an appropriate authority “Supercomplaints” that describe “any feature, or combination of features, of a market in the UK for goods or services is or appears to be significantly harming the interests of consumers.” Under the Act, the authority receiving the report then has 90 calendar days to publish a reasoned response.

March 2006 – CC issues response to its store card inquiry, proposing:

- Un-bundling PPI from store cards because of sell-rather-than-buy implications; and
- The supply chain has no incentives to pay regard to the customer and their requirements.

October 2006 – FSA publishes results of second round of PPI probe. OFT market study:

- Shows that PPI is still failing customers, giving them a poor deal.
- Concludes that there is limited evidence that the industry is taking steps to improve the situation.
- Citizens Advice says it is disappointed by the length of time being taken.

February 2007 – OFT issues its reasons for referring PPI to Competition Commission (CC).

November 2007 – CC issues its emerging thinking

June 2008 – FSA's new rules on selling PPI come into force

CC publishes report on PPI:

- It agrees that there was a problem to address.
- People buying PPI are being overcharged by about £1.4bn a year.
- British Bankers' Association (BBA) response: 'I don't necessarily see that we have been overcharging at all' (Eric Leenders, BBA, 5 June 2008)

September 2008 – FSA publishes its third thematic review into PPI.

FOS issues wider implications letter to FSA about the increase in complaints about mis-sold PPI and the very high uphold rate.

October 2008 – CC publishes its provisional findings on retail PPI

November 2008 – CC publishes its provisional remedies.

- Creditors not allowed to propose PPI sale within 14 days of credit sale, although consumers can pursue this;
- Ban on single issue premiums, notices, advert requirements and price metrics.

Autumn 2008 – BBA sets up group on improving complaints handling.

January 2009 – Final CC report on the inquiry and remedies:

- Single premium policies to be banned (a highly interventionist remedy from the CC), and
- A range of other remedies designed to stop vendor-bias in the sales process and encourage consumer shopping around.

April 2009

Barclays appeals to the Competition Appeal Tribunal (CAT) on the point of sale ban and the analysis that led to the CC's decision.

October 2009

The CAT orders the point of sale ban to be reviewed. The CC must reconsider this remedy and the background to it. FSA consults on the assessment and redress of PPI complaints.

October 2010 – BBA take FSA to judicial review on PPI policy.

May 2011

The High Court dismisses the BBA's application for judicial review. The banks agree not to appeal.

Where next?

Despite the problem of delayed payments to customers, such is the scale of compensation that the Office for Budget Responsibility said that its economic forecast of growth at a positive 0.5% over two years would be "mainly due to the effects of payment protection insurance (PPI) fee repayments".¹⁴ This constitutes a bigger impact than any government initiative, as Britons have used the refunds on home improvements and holidays, providing a boost to Britain's ailing economy.

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The improvement to growth aside, overall the PPI scandal has been a total tragedy. After a decade of damning indictments, timid regulators, prevarications and quarrels, the banks are now, slowly, paying back billions in compensation to consumers, but making too many of those customers seek independent redress.

The incident has spawned the new problem of a burgeoning claims management market and consumers remain no better protected for the downside risks if they are unable to afford to repay their debts. A product that still seems like a prudent concept is a toxic brand. As PPI includes the two magic words ‘protection’ and ‘insurance’, this will surely have had an impact on consumers’ views of other products using similar labels.

Would we still make the Supercomplaint? Yes, absolutely. Without that, the full scale of the issues that the OFT market study and Competition Commission investigation revealed may not have surfaced even as quickly as within four years.

Lessons learned

So are there any lessons for the future? Is there any possibility at all of rehabilitating PPI? Reviewing Citizens Advice involvement in this issue over the past 10 years, my view is that the two key lessons for businesses and regulators are:

Put the customer before the company

All the evidence on the PPI scandal shows us that companies have put themselves first all the way down the line, including even now, in the handling of complaints and the appeals for cut off dates for claims. The root of that is greed, intensified by firms becoming hugely dependent on the excess profits from one product line. Business leaders in financial services who have looked at the numbers down the years will have known, even from the figures alone, that they were taking advantage. Seeing those numbers will have told them the customer was not coming first. Fundamentally, it’s about ethics.

“*Fundamentally, it’s about ethics.*”

¹⁴ Office of Budget Responsibility, Economic & Fiscal Outlook, March 2012, p.57, para.3.59.

Listen to what consumer representatives are saying

Companies dismissed our SuperComplaint as anecdote – though the stock market response was telling. But even back in 2003, our modest recommendations for reforms – if adopted then – could have made a huge difference to the outcomes. Citizens Advice has two aims. One is to help people through advice and information, to ensure that they know their rights and their responsibilities. The other is to influence policy and practice, so that the problems we see are resolved on a wider scale and do not happen again.

Importantly, our aims are to act responsibly when influencing policy – we are not a knee-jerk, rent-a-quote campaign, but an authentic, evidence-based, responsible charity. We may not always have the whole picture about what is causing a problem in a market but, like the canary down the mine, we often get the first whiff that something smells wrong. If businesses and regulators had taken our insight more seriously, and acted more swiftly in response, some of the scale of this problem could have been reduced, and consumers might have got a better deal.

Is there any prospect of PPI being rehabilitated?

Right now, this may sound like an impossible prospect. But the fundamental idea that a consumer should have appropriate protection in place for risks, if they take on significant financial commitments, is a good one. That could include insurance. There is certainly an ongoing need for consumers to have protection, particularly as the level of support available from the welfare state seems set only to decline further, as we all live longer and the dependency ratio increases.

The challenge will be to engage consumers AND offer them simple and fair products and services that do what they say on the tin. There may not be a rush to market, and any firms that do wish to rehabilitate PPI will find consumers far more challenging and sceptical going forward. Getting the offer right will be key to restoring consumer trust and confidence, and product regulation is likely to be essential to achieve that.