



Financial Services Authority

The Sale of Payment Protection Insurance – results of follow-up thematic work

October 2006

Contents

1	Introduction	2
2	Key messages	2
3	Our approach	3
4	Findings	4
	• Significant concerns remaining	5
	• What we want to see	6
	• Good and poor practice	11
5	Regulation	15
6	Wider work on PPI	15
	• Competition authorities	15
	• Trade associations	16
	• Unfair contract terms	16
7	Next steps	18
8	Other information	18

Introduction

This review of the sales processes and systems and controls relating to the sale of payment protection insurance (PPI) policies follows up the work undertaken during 2005 and published in November 2005¹. As part of that earlier work we issued a Dear CEO letter to medium and large firms², a factsheet for small firms³, and made a commitment to carry out further work in 2006. This report contains the key results of that further work.

Key Messages

A number of firms have taken steps over the past year to improve their PPI sales standards, but visits to 40 firms reveal that there remain three key areas of widespread concern which result in customers being unable to make an informed decision:

- Many firms are still not giving customers clear information during the sales conversation: some are not making it clear that PPI is optional and customers are not receiving full information about how much the cover costs.
- Customers are still not being made fully aware that there may be parts of the policy under which they cannot claim. Furthermore, some firms are still failing to establish that the PPI policies they recommend are suitable because they are not collecting sufficient information from the customer – for example, about any existing cover they possess.
- Where customers are sold single premium policies, this is not always done with the best interests of the customer in mind – for example, where a choice between regular and single premium is available, the sales conversation may be biased towards a single premium policy when the customer's circumstances suggest this is not suitable.

1 www.fsa.gov.uk/pubs/other/ppi_thematic_report.pdf

2 www.fsa.gov.uk/pubs/ceo/ppi.pdf

3 www.fsa.gov.uk/pages/Doing/small_firms/insurance/pdf/paypro.pdf

In addition to these general findings, our work identified particularly poor standards among firms, such as motor dealers and retailers, for whom the sale of PPI is a minor activity relative to their main business.

As a result of these findings, we will:

- continue to work closely with the competition authorities recognising the more fundamental problems in this market (see Office of Fair Trading (OFT): Payment Protection Insurance – the market study report October 2006);
- follow through the detailed programmes of urgent remedial action which a number of firms are implementing to improve their sales standards;
- pursue formal disciplinary action against firms who fall below the required standards;
- conduct further work next year to ensure that senior management are addressing the areas of concern and embedding the behaviours and standards we expect;
- continue to work with industry trade associations to help improve overall standards
- consider, as part of the existing wider review of the effectiveness of the regulatory regime for general insurance products, whether there is a case for new rules in the area of PPI sales.

We have also secured undertakings from firms and the agreement of trade associations to make the practice of refunds on single premium PPI policies fairer and more transparent to customers.

Our Approach

As we have made clear before, when sold properly PPI can provide valuable protection against changes in personal circumstances.

The outcome we are seeking from our work is that customers who buy PPI are in a position to make an informed choice at the point of sale about why they are buying the product, what it will cover, what it will cost and – in an advised sale – why this product in particular meets their demands and needs.

In dealing with their customers, we expect firms to treat their customers fairly (TCF) and pay due regard to customers' information needs and communicate information to them in a way that is clear, fair and not misleading.

We have followed up the issues identified in our first round of work (Phase 1). All firms who received the Dear CEO letter in November 2005 were asked to set out the action they intended to take as a result. We closely monitored these responses and factored this in to the planning and scope of the latest visits (Phase 2).

The results of our Phase 2 work are based on supervision visits to 40 firms conducted between April and June this year. These firms came from a wide range of sectors – banks, mortgage brokers, credit brokers, car dealers and retailers. In selecting our sample we sought a good spread of firms across the sectors. We also wanted to ensure that our sample had a good mix of penetration rates⁴, a good mix of firms that sold single premium and regular premium PPI and sales on an advised and non-advised basis. We included some firms that sold PPI on a stand-alone basis too.

We excluded firms that sold regular premium PPI in the prime mortgage sector from our sample as they were found to generally meet our standards in Phase 1. Firms operating in this sector should nevertheless take into account the findings of our Phase 2 work.

Findings

Our findings in the PPI market support our more general view that there has been mixed progress complying fully with the requirements of ICOB and in implementing TCF. Some firms are making good progress, but others are lagging behind. The findings of this and other thematic work suggest that good intentions are not yet translating in all cases to good outcomes for consumers.

Over the past year, we have seen improvements in a number of areas. These include: training and competence arrangements (T&C); written disclosure material and policy documentation; compliance monitoring; and how firms establish and use management information. We have also seen some evidence of a more balanced approach to the remuneration of sales staff. However, the overall picture here was still very mixed with some quite poor firms, some quite good firms and a variety in between.

Firms who fall well below the required standards have been referred to our Enforcement Division for further investigation. Our Enforcement Division has concluded one of the cases referred as a result of Phase 1 (www.fsa.gov.uk/pubs/final/regency.pdf) and is still investigating other firms referred at the time. Further firms have been referred on PPI matters as a result of Phase 2. Two firms have withdrawn their permission to carry on regulated activities as a result of our visits.

One clear trend was the generally poor compliance seen among firms that do not have financial services as their main line of business and sell PPI as a tertiary product – for instance, after a motor dealer sells a car and sells the finance to pay for the car, it sells PPI to protect the payments on the finance. For such firms, selling insurance is a small part of their overall business. We will be working closely with relevant trade associations in this sector to help these firms address the shortfalls we have identified.

4 Percentage of loans/credit sold with PPI

With the exception of the tertiary firms mentioned above, there were no clear trends between sectors, or sizes of firm within a sector, in terms of overall performance, with good and poor practices seen within all sectors.

All of the largest firms sampled – as explained in their Dear CEO letter responses – have comprehensive projects in place which are delivering change to their internal processes and will deliver more in future. But, the commitment and speed of progress did vary across the sample. Many of the smaller and medium-sized firms have also spent time and money assessing and adjusting their PPI processes.

Significant Concerns Remaining

As noted above, while we are able to report improved compliance standards across most sectors of the PPI industry, there are three key areas where some firms are continuing to fail to treat their customers fairly and, as a result, customers are failing to make informed decisions:

- When firms have the sales conversation with customers they are not always giving them timely, clear, fair and not misleading information. For instance some firms are still not making it clear that PPI is optional and not giving full information about how much the PPI costs. These findings are backed up by OFT research⁵ in their consumer survey.
- Customers are still not being made fully aware that there may be parts of the policy under which they cannot claim. Also, some firms are failing to establish that the PPI policies they recommend are suitable for the customer because they are not collecting sufficient information from the customer to be able to make that judgement – for instance, not taking into account existing cover.
- Where customers are sold single premium policies this is not always done with the best interests of the customer in mind. For instance, we found that where a choice between regular and single premium is available, some firms biased the sales conversation towards a single premium policy when the customer's circumstances might suggest that this is not suitable.

We set out below what needs to change to bring about improvements. None of this is new; much of it was discussed in our November 2005 report and the Dear CEO letter/small firms' factsheet.

For many firms, we are looking for a significant cultural and behavioural shift around the sales process, to one that promotes the fair treatment of customers. Many of the firms visited have received detailed action plans which set out what we expect them to do. We will closely monitor the situation to confirm that progress is being delivered.

5 Payment Protection Insurance; market study report October 2006 – Summary of consumer survey

What we want to see

We recognise that different firms have different processes and different ways of organising themselves to achieve their regulatory responsibilities. It remains up to firms' senior management to decide how best they deliver the appropriate standards. We set out below the outcomes we wish to see and some of the issues firms need to consider and act upon in determining how to satisfy themselves that they are treating their customers fairly and providing clear, fair and not misleading information. In considering what action to take, firms must, of course, take into account the relevant ICOB rules and principles.

Sales Conversations and Oral Disclosures

The outcomes we want to see:	Actions for firms:
<p>Customers are in no doubt at the point of sale that PPI is optional, where this is the case.</p> <p>ICOB 5.5.14R(5)(b)</p>	<p>Do firms have the necessary disclosure in place to comply with ICOB?</p> <p>For example, do scripts used in telesales and branch sales processes make it clear whether PPI is optional?</p> <p>Are processes that do not involve a sales conversation similarly clear?</p> <p>Are firms confident that sales scripts are adhered to? And is monitoring undertaken to confirm this?</p>
<p>Customers are not led to believe that taking out PPI will improve their chances of being accepted for the underlying credit. From the OFT Consumer Survey⁶ : <i>'A particularly worrying finding was that nearly a third (30%) of consumers in our survey who went on to buy PPI either assumed – or were told or given the impression by the distributor – that taking out the PPI would help the application for credit.'</i></p> <p>Principles 6 & 7</p>	<p>Is it made clear that the underlying credit and the PPI are separate products and separate transactions?</p> <p>Where this is the case, is it clear that the application for the underlying credit is not affected if the customer chooses not to buy PPI?</p>
<p>Customers receive two distinct quotations for credit at the point of sale, one without PPI and one including PPI. So customers do not have to ask for a quote without PPI and should not have to rely on written disclosure to find this out.</p> <p>Principles 6 & 7</p>	<p>Are all credit quotations given on a without-PPI and a with-PPI basis? (Provided that the customer has not already indicated that they do not want PPI.)</p>

6 Payment Protection Insurance; market study report October 2006 – Summary of Consumer Survey

The outcomes we want to see:	Actions for firms:
<p>Customers understand the true cost of the product before they buy. They know the monthly and total cost of the PPI and where a single premium is included within the credit, how much interest they are paying. Firms do not just rely on the written Statement of Price.</p> <p>(ICOB 5.5.14R and Principles 6 & 7)</p> <p>OFT research⁷ notes the importance of disclosing the total price of PPI and how this influences consumer behaviour.</p>	<p>Firms must disclose the monthly premium and total cost of the PPI at the point in the sales process where the customer has the best chance of taking it in and using it to make an informed decision.</p> <p>Where the insurance is discussed over the telephone, and the firm sends full information to the customer with the loan documentation, the firm should ask itself whether only providing full information at this stage complies with 'in good time before conclusion' and Principles 6 & 7. This is especially important where a decision not to take out insurance at this stage might mean a delay in the customer receiving the loan.</p>
<p>Customers are clear about whether they have been given advice.</p> <p>ICOB 4.2.8R(6) and 4.4.1R(1)(b)</p>	<p>Firms should indicate clearly whether advice is being given. The statement of demands and needs says whether advice has been given.</p>
<p>Customers understand the significant limitations of the policy as well as the significant benefits.</p> <p>Principles 6 & 7</p>	<p>Is the conversation about the policy carried out in a balanced way? Does it feature the limitations as well as the benefits of the policy?</p>
<p>Customers are clear on all of the above before making a decision. Information gained from the sales conversations is augmented by the customer reading the written disclosure material. The firm tells the customer that it is important to read it.</p>	<p>Is explicit reference made to the important parts of the disclosure documentation? Are these flagged to the customer so they know where to find the key information?</p>

7 Payment Protection Insurance: market study report October 2006 – Summary of Dr Rob Ranyard's work

Eligibility and Suitability

The outcomes we want to see:	Actions for firms:
<p>For all sales (advised and non-advised) customers' eligibility is checked.</p> <p>Principle 6</p>	<p>Are reasonable steps taken to ensure that the firm always checks eligibility so customers do not buy policies they cannot claim under?</p> <p>If it is not possible to check eligibility in a particular case, does the firm still give the customer clear and balanced information they can use to make an informed decision?</p> <p>Eligibility is about checking whether parts of the policy apply at all – for instance, as a result of employment status, residency or age.</p>
<p>For all sales (advised and non-advised) customers are made fully aware of any parts of the policy that they may not be able to claim under.</p> <p>ICOB 4.3.1R(3)(b) –advised</p> <p>Principle 6 – all sales</p>	<p>Firms might like to consider whether the policies sold could be simplified – for instance by having fewer exclusions? Can the policy be split into its component parts to enable the customer to only buy those parts of cover they are eligible to claim under?</p> <p>Some firms we visited are discussing this with their PPI providers and others have already split, or are looking to split, PPI policies.</p> <p>It is not acceptable for the firm to put the onus on the customer, after buying the policy, to read the policy exclusions and then have to cancel it if they are not happy with the cover it provides.</p>
<p>For advised sales, firms recommend suitable policies that meet customers' demands and needs.</p> <p>ICOB 4.3.1R</p>	<p>Firms need to ensure that suitability is assessed when making a personal recommendation. This involves assessing the customer's demands and needs, based on information the salesperson must actively seek from the customer - rather than simply relying on what the customer tells them. In doing this the salesperson must take into account existing cover.</p>

The outcomes we want to see:	Actions for firms:
<p>For advised sales the firm retains a statement of demands and needs, tailored to the individuals' circumstances, on file to act as a record of that recommendation and gives a copy to the customer.</p> <p>ICOB 4.4.7R</p>	<p>The firm needs to demonstrate that it has sought information from the customer and this should be reflected in the statement of demands and needs which is therefore a tailored document – not generic. Such an assessment should also take into account the relevance of any exclusions and limitations. Firms must take the cost of the contract into account where relevant, based on the customers' circumstances and their demands and needs in this regard.</p>
<p>For advised sales, firms ask customers whether they have existing cover.</p> <p>ICOB 4.3.2R</p>	<p>The response should be assessed and factored into the recommendation.</p>
<p>In all sales customers are aware of the significant and unusual limitations and exclusions, and know where to look for more information.</p> <p>ICOB 5.3.1R(2) and ICOB 5.3.6R(1)(a), (2)(a)(iv) and (2)(b)(iv)</p>	<p>In telesales, is simple and clear disclosure made of the significant and unusual exclusions?</p> <p>Is the customer told where to look for more detail and the importance of doing so?</p>
<p>In all sales customers understand what constitutes a pre-existing medical condition and the importance of disclosing such.</p> <p>ICOB 4.3.2R(3) – advised sales</p> <p>Principle 6 – all sales</p>	<p>Does the customer know what a pre-existing condition is and where to look for more information in order to make an informed choice about the cover?</p> <p>There is no expectation that a detailed discussion of the customer's medical history takes place between the customer and the firm.</p>

Single-Premium Policies – Firms need to act with particular diligence when selling single-premium policies. The delivery of information must be clear, fair and not misleading.

The outcomes we want to see:	Actions for firms:
Customers come away from the sale having been given the best possible chance of understanding: – How a single-premium policy works; ICOB 5.5.14R and Principle 6	Firms should ask themselves whether it is always fair to only offer customers single premium policies. If a firm only offers a single premium option and the customer's circumstances show that this is not suitable, then it must not recommend it to that customer.
– How it differs from a regular premium policy; Principles 6 & 7	Where firms offer a choice between single and regular premium, does the sales discussion avoid any bias in favour of single premium if an alternative policy is more suitable? In advised sales, the firm should detail the reason for recommending a single-premium policy (as with all recommendations) in the statement of demands and needs.
– How much it costs, in monthly repayments, and total repayable (see also under Oral disclosures on Page 7); ICOB 5.5.14R and ICOB 5.3.6R(2)(a)	When comparing the costs of single-premium against regular-premium, does the firm do this in such a way that the comparison is not misleading (eg. on a like for like basis)?
– How long it lasts; ICOB 5.5.5R(7) and Principle 6	Is the term of the policy made clear to the customer so they understand whether it covers them for the term of the loan or a shorter period? If it is for a shorter period does the customer understand it will need to be renewed?
– What they get back if they cancel – both within and outside the statutory cancellation period; ICOB 5.5.5R(9) and Principle 6	Are refund policies clear, fair and understandable?
– Why the product was recommended to them. ICOB 4.4.1R(1)(c)	Firms should ensure that every sale of a single-premium policy has been carried out with a view to treating the customer fairly so the customer is able to make a fully informed decision.

Example: One firm we visited offered loans from one provider and that provider offered one type of single-premium PPI policy to accompany the loan. The firm did not feel that it was in the best interests of its customers to restrict their choice in this way, so it sourced a regular-premium policy from elsewhere. It is now able to offer customers a choice and makes it clear to them how the products differ.

Good and poor practice

While the earlier sections of this report focused on those areas where we still have concerns, we now focus on areas where we have seen improvements and to illustrate this we use a combination of good and poor practice. Where re-stating poor practice is less helpful – such as with management information and T&C – we concentrate on good practice and examples.

The good and poor practice we report below is to help the firms' senior management decide what TCF means for their particular firm. We think the good practice is likely to help a firm meet our regulatory standards and in doing so treat its customers fairly and the poor practice is likely to either get in the way of a firm doing so or create the risk of the firm not doing so if not appropriately managed. However, some of the practice we report concerns compliance with or breaches of detailed rules which we think have a significant impact on fair outcomes for customers; where this is so, firms must of course comply with those detailed rules.

Inducements (ICOB 2.3)

Our work on inducements concentrated on internal systems to remunerate sales staff rather than the financial incentives offered by providers to distributors. We found encouraging signs that firms are moving away from purely quantitative measures of sales performance and linking financial rewards more closely with the quality and/or persistency of sales. However, some firms still have work to do to remove the culture of 'PPI sales at all costs'.

Example of good practice

Reward structures are based on a mixture of inputs which are not restricted to the number of policies sold by the individual, but also include reference to other factors such as:

- the compliance quality of those sales
- cancellation rates
- failed claims data
- complaints data
- sales across the whole product range, with no undue bias towards PPI; and
- paying bonuses a few months in arrears so they take account of cancellations.

Examples of poor practice

The firms' attitude towards PPI is focussed on selling as many policies as possible.



There are no claw-back arrangements in place for commissions earned on policies that do not persist.

Written Disclosure

Reference should be made to our relevant publication on the responsibilities of providers and distributors⁸

Good Practice

Specialist agencies are employed to re-design customer-facing material, making it more attractive and easier to read.

Some policy summaries contain an icon  to highlight exclusions and limitations and an icon  to help cross-reference between the policy summary and the policy document.

Poor Practice

Some policy summaries are too detailed.

A number of policy documents contain too much small print or a confusing layout. And some policy documents don't make the refund policy clear.

Systems and Controls

Example of good practice

- Taking a risk-based approach to monitoring sales staff. 100% of the business is checked for new advisers until their general attitude, business levels and files indicate that they are competent. All advisers are graded so that pre-determined volumes of their business are checked on a sample basis. Unusual variations in sales volumes for a particular sales person will also trigger increased monitoring.
- Compliance review and sign-off all sales staff incentive schemes (financial and non-financial).
- A zero-tolerance view of non-compliant sales is taken; non-compliant sales will affect the individual's remuneration package.

Example of poor practice

- Monitoring is not risk-based; for instance only one sales call is listened to per month for each adviser regardless of the risk that advisers with different levels of experience may pose.
- Some firms are unable to demonstrate that they have controls around non-advised sales and simply 'trust advisers' not to advise.
- Inadequate controls in place to monitor the standard of service provided by outsourced call centres. The regulated firm relies on checks carried out by the call centre audit without independently verifying performance standards itself.

8 www.fsa.gov.uk/pubs/discussion/dp06_04.pdf

- Compliance regularly review items such as sales scripts and statements of demands and needs to ensure they continue to meet regulatory standards.
- Controls around sales conversations – some firms selectively record their sales advisers during visits to the customer's home to ensure that a compliant process is being followed.
- Ideally telesales calls are recorded. These calls are monitored to ensure that advisers are not straying away from scripts or guidance.
- Firms only rely on their ability to listen to live calls.
- Firms do not monitor 'home' visits in any way.

Management Information

Good Practice

Customer contact exercises are used to establish what facts the customer was made aware of at the time of the PPI sale - for instance, did the customer think they received advice? Did the customer think that PPI was compulsory? How much did the PPI cost? Did they feel under pressure to take out PPI? Were the limitations of the policy discussed and did they understand them?

MI is collected on sales and broken down according to which adviser sold the policy. Information includes details of individual penetration rates, claims data (including rejected claims), cancellations inside and outside the statutory cancellation period, and complaints. These are collected in one document and passed to senior management regularly with the frequency depending upon sales volumes.

MI is acted on in assessing the quality of the sales of individual advisers. The firm also takes a holistic view to determine whether the sales process is delivering compliant sales where customers are treated fairly.

Cancellation rates are broken down into specific timeframes for instance within 30 days, 30 days to one year, and over a year - to better understand the persistency of PPI sales.

Senior management ensure that useful MI is communicated down through the firm to the relevant staff in Compliance, Sales, Audit and Training.

Providers and distributors have systems and controls in place to share key MI in a timely way.

Training & Competence

On the whole, especially among the medium to large financial services firms we visited, improvements have been made to T&C where necessary in line with our comments from Phase 1 of our PPI work.

It is among some smaller firms, and in particular those whose main business is not financial services, that T&C arrangements continue to fall short of our expectations. So this is where the risk of customer detriment remains, owing to poorly trained sales staff and lack of supervision of their activities.

Example

In a typical scenario the firm may have set up initial training, a system of probationary coaching/mentoring, ongoing training and observation. Inductees are given comprehensive training on product knowledge and sales technique before being allowed to talk to customers. This may take the form of classroom-based training (covering the loan product, FSA regulations and credit insurance products), role-playing and time spent among the sales team.

This may be followed by a comprehensive test. Effective ongoing support is provided even when the member of staff has completed the initial training successfully.

An assessment of competence is not made until the inductee has been observed over a period of time and their supervisor/mentor is content with their ability. Ongoing assessment will then be made with the Compliance department operating on a risk-based approach to listening to call records – the less experienced the member of staff, or where there have been previous issues with a salesperson's compliance, the more calls are listened to.

Regular and frequent observations are made of sales staff and the firm deals with non-compliant practices by preventing the individual from selling and then re-training them in some form. Over and above re-training, we would expect the firm to check the staff member's previous sales and take steps to rectify the breaches found.

The firm may give frequent, regular training for all sales staff and this enables its supervisors and compliance staff to update the sales team with technical and regulatory changes that will affect the process. Formal refresher training is given periodically too.

The firm might ask product providers to come to the firm and give training on their particular products. Ideally this should be a balanced picture of the product including descriptions of the limitations and exclusions rather than just a session on 'how to sell our PPI policy'.

Regulation

In the light of the continuing problems with the sale of PPI, as evidenced by our thematic work and the OFT's market study, we are looking at the case for further regulation of the PPI market. Subject to the further work we are carrying out, including cost benefit analysis, we propose to consult on rule changes to enhance the protection provided to consumers taking out PPI. This work will be carried out as part of our review of the Insurance: Conduct of Business sourcebook. We intend to publish a report on the results of this review in the first quarter of 2007, to consult on any rule changes that arise from the review in the second quarter of 2007, and to make any rule changes in the fourth quarter of 2007. We will, of course, take into account any improvements made by the industry in this work.

Wider Work on PPI

This report needs to be read in the context of the PPI market as a whole and whilst it can only reflect in detail on those issues over which we have direct responsibility, there are other initiatives underway including:

- **Competition Authorities:** We have been working closely with the OFT on its recently released PPI market study which concluded that there are sufficient concerns within the PPI market to warrant a referral to the Competition Commission. For instance it found:
 - low claims ratios compared to other insurance products
 - high commission rates in comparison with other general insurance products
 - wide differentials in price for the same level of cover
 - possible cross-subsidisation to keep Annual Percentage Rates low
 - consumers that do not shop around or switch; and
 - lack of competitive pressure on prices.

Both phases of our work on PPI have done nothing to alter our own view that the market is flawed. For instance, some small loan brokers who sell PPI alongside the credit product claim it is difficult for them to offer PPI products other than those offered by the lender providing the credit. Furthermore, if they have concerns over the disclosure documentation that accompanies the product they meet resistance from the product providers when they attempt to get it changed. The nature of the market also makes it difficult for those firms who offer stand-alone PPI policies to increase their market share.

We will continue to help these agencies pursue a fair deal for consumers.

- **Trade Associations:** We challenged all of the trade associations with an interest in PPI⁹ to work with firms to consider what action the industry could take to address the compliance failings identified at Phase 1, as well as the wider competition issues in the market.

Work has progressed in several areas both collectively and individually and the following items will be finalised and available for member firms in due course:

- Creating consumer information designed for use before and during the sales process (being launched for consultation on 19th October 2006). The most effective methods for distribution are currently being considered.
- Considering scope for standardised terminology in price information and key product features issued by member firms.
- Reviewing the Consistent Interpretations Guidance for claims handling (completed June 2006) and promoting this code to non-signatories.
- Providing a management information model for firms to better enable them to gather and monitor sales, complaints and claims data in order to more effectively monitor their PPI sales process.
- Providing model elements for incorporation into member firms' sales procedures to improve the sales process.
- Issuing member firms with learning objectives for a generic PPI training course for benchmarking purposes; and
- Providing a minimum set of standards on Mortgage Payment Protection Insurance products.

We recognise the work, initiated by the industry, that is underway and also recognise that it will take time for the benefits to be realised. We will, of course, take into account the effectiveness of that work when we come to consider whether new rules are justified.

- **Unfair Contract Terms:**

We had concerns about terms in PPI contracts that prevented consumers from receiving any refund if they repay their loan early (but outside the statutory cancellation period). In June this year we published several agreements from firms who agreed to change their terms and practices. This was under the *Unfair Terms in Consumer Contracts Regulations 1999* (the Regulations).

⁹ The trade associations involved are: Association of British Insurers (ABI), British Bankers Association (BBA), Council for Mortgage Lenders (CML), Finance Leasing Association (FLA), Association of Independent Financial Advisers (AIFA), Association of Mortgage Intermediaries (AMI), Finance Industry Standards Association (FISA), Association of Payment and Clearing Services (APACS), Building Societies Association (BSA), British Insurance Brokers Association (BIBA), Consumer Credit Trade Association (CCTA) and Protect.

We also had concerns with:

- policy terms that provide no refund of the single insurance premium where the consumer wishes to cancel the PPI policy without early repayment of the loan; and
- the amount of the refund, which may not be fair and proportionate and which may not be clear from the terms of the policy how it is calculated.

We have discussed these concerns with the relevant trade associations. They have agreed in principle that firms should not include nil refund terms in their PPI policies where the consumer cancels the policy for any reason. This is unless a claim has already been paid under the insurance policy or if the consumer has instead chosen to take continuing PPI cover for another loan.

We have considered terms relating to the amount of the refund to be provided and the clarity of such terms. Due to the differing types of firms and commercial practices within the PPI industry, we do not intend to propose a single refund method for all firms to use. We believe refunds should be based on firms' reasonably incurred costs. Where methods used to calculate the amount of refund are not easy for the consumer to understand – for example methods which take into account the uneven spread of the risk the insurer is carrying – firms should make them clearer.

The trade associations have committed to work with their members to improve the transparency of refunds. They have proposed that firms include in presale material and/or the policy documents explanations of whether the refund is based on a pro-rata calculation or not. We are also exploring with the trade associations how firms could include a table or example to illustrate the amount of refund consumers can expect to receive.

We have concerns that lack of competition at the point of sale, as identified by the OFT, may be an adverse factor in calculating the amount of the refund provided to consumers. This is because commission paid by an insurer to a distributor is sometimes deducted from the premium paid by the consumer before any refund is calculated. However many firms have other arrangements in place so that refunds are based on the amount of premium paid without taking account of commissions paid. We expect that with improved transparency of the amount of refunds and the work of the OFT on competition at the point of sale in the PPI market, consumers will benefit from better refund terms. So, we do not intend to take our concerns with commission any further at this stage.

We expect insurers and distributors to consider these proposals when drafting their contracts. Firms may find it useful to carry out a review of their refund terms to ensure they are fair under the Regulations. We will provide a further update on this work on refunds of PPI when the remaining issues have been resolved.

Next Steps

The following are either already underway or planned for the very near future:

- As the OFT report shows, the causes of the problems are complex and rooted in competition concerns and we intend to continue to work closely with the competition authorities in this area.
- We are examining the case for further regulation of PPI sales, subject to cost benefit analysis and consultation, as part of the ICOB effectiveness review.
- We have given feedback to all of the firms visited during this review. Many have received detailed action plans subject to tight timetables and we will follow up this remedial action with individual firms in forthcoming months.
- We anticipate that further work will be required during 2007 and will make a decision on the nature and scope of that in the first half of next year taking into account the plans of the competition authorities.
- Enforcement investigations into a number of firms are continuing and we have not ruled out Enforcement action against firms that fail to deliver on any remedial action plans arising from Phase 2.
- We recognise the work being carried out by the trade associations and the commitments made in several areas. We welcome these initiatives and accept that there will be a period of time before the benefits flow through to customers.
- We will keep in contact with consumer representatives on matters relating to PPI.
- We will tackle the problems found in the tertiary sector including engaging with the relevant trade associations to find ways of increasing compliance in this area. We will roll out a programme of work between now and the middle of next year.

Other Information

- Phase 1 report (November 2005)
www.fsa.gov.uk/pubs/other/ppi_thematic_report.pdf
- Mystery shopping report (November 2005)
www.fsa.gov.uk/pubs/consumer-research/crpr45.pdf
- Dear CEO letter (November 2005)
www.fsa.gov.uk/pubs/ceo/ppi.pdf

- Small Firms factsheet (December 2005)
www.fsa.gov.uk/pages/Doing/small_firms/insurance/pdf/paypro.pdf
- Consumer website Q&A
www.fsa.gov.uk/consumer/05_INSURANCE/types_insurance/payment_protection.html
- Regency Mortgage Enforcement case (September 2006)
www.fsa.gov.uk/pubs/final/regency.pdf
- The Responsibilities of Providers and Distributors for the Fair Treatment of Customers (September 2006)
www.fsa.gov.uk/pubs/discussion/dp06_04.pdf
- Treating Customers Fairly – towards fair outcomes for consumers (July 2006)
www.fsa.gov.uk/pubs/other/tcf_towards.pdf
- Treating Customers Fairly – General Insurance and Pure Protection Products (July 2006)
www.fsa.gov.uk/pages/Doing/Regulated/tcf/pdf/insurance.pdf
- The trade association PPI meeting notes on the FSA website
www.fsa.gov.uk/pages/Library/Other_publications/Miscellaneous/2006/ppi_310706.shtml
- Unfair Contract Terms Publications
www.fsa.gov.uk/Pages/Doing/Regulated/consumer/index.shtml



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