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The Financial Services Authority (FSA) has made it clear that it will take enforcement action against those firms failing to treat their customers fairly in selling payment protection insurance (PPI). It has referred a number of firms to its Enforcement Division for further investigation and, to date, three businesses have been fined a total of £781,000. A recent online report from the BBC (22.1.07) indicated that up to 10 banks and lenders could be fined up to £1 million each for mis-selling PPI in the coming weeks - and the FSA announced the first enforcement action against a bank at the end of January.

The regulator is clearly getting tough on any evidence of mis-selling. Will it go one step further and enforce a strictly governed advised sales process? If so, what does this mean for the new entrants to the PPI market who are predominantly selling online in a non-advised environment but who are arguably offering better value to consumers in terms of price, product flexibility and features? How can this emerging new channel continue to provide an alternative source of insurance cover for consumers?

In its report *'The Sale of Payment Protection Insurance - results of follow-up thematic work'* (October 2006), the FSA made clear the outcome it is seeking from its work. Put simply, the regulator wants to ensure that customers who buy PPI are provided with more relevant and clear information at the point of sale so they are in a position to make an informed choice. Customers need to understand that PPI is optional, why they are buying the product, what it will cover, what it will cost and - in an advised sale - why the recommended product meets their demands and needs.

The report highlighted three key areas where some firms are continuing to fail to treat their customers fairly and, as a result, the customer is unable to make an informed decision:

1. In the sales conversation, customers are not always provided with timely, clear, fair and not misleading information
2. Some firms are failing to establish whether a recommended policy is suitable for the customer as they are failing to collect sufficient information from the customer

3. Some firms have biased the sales conversation towards a single premium policy when the customer's own circumstances might suggest a monthly premium would be more appropriate

The consumer survey conducted by the OFT revealed that overall 88 per cent of PPI holders took out PPI at the same time as their credit product. This was reinforced by the separate business survey carried out by the OFT, that indicated over 90 per cent of PPI policies were sold at the point of sale of the credit product being insured.

While the OFT did find that point of sale advantage is slightly weaker in the mortgage payment protection (MPPI) sector, it is likely this will be a key feature of any PPI market investigation and so it will also be interesting to see the outcome of the FSA's review of ICOB. Dan Waters, Director Retail Policy Division, warned that firms should expect radical changes. With that in mind and the outcomes the FSA wishes to see, are we one step away from the death of non-advised and the enforcement of a fully advised sales process for PPI?

Whether due to consumer apathy or a failure by Government and industry to educate, it is clear that most purchasers of PPI do not shop around. Research by Harris International for the Finance and Leasing Authority (FLA) showed that web searches on PPI are low.

Yet we have seen several new entrants to the market operating online, concentrating on MPPI, unsecured loan PPI and credit card PPI. While there is currently no firm data to confirm how much of the market they account for, anecdotal evidence suggests between 1 and 7 per cent, and latest Datamonitor figures estimate that 5 per cent of loan PPI is sold online. This is a relatively low figure and not a number that traditional providers might view as a real threat. However, these providers arguably operate a lower risk based model in that they don't provide advice and so have less exposure to accusations of mis-selling. Given that the fines imposed by the FSA to date have all related to an advised sales process, this is not a fact for lenders and brokers to ignore.

There is no doubt that consumers are increasing in confidence when it comes to shopping online. You only have to look at the retail figures that have been released following the Christmas period. UK consumers spent a staggering £7.66 billion shopping online in the run-up to Christmas, a 54 per cent rise from last year's total according to a report by e-commerce analyst IMRG. This is a marked contrast to the figures released by Footfall that found the number of shoppers visiting the High Street in the week before Christmas was down 8 per cent. IMRG figures indicate that total online sales for 2006 reached £30.2 billion, a figure which surpassed its original estimate of just under £30 billion.

Buying a DVD, book, or even electrical equipment online is one thing, but buying an insurance product is another. However, even here there is evidence of a steady increase in consumer confidence. Datamonitor figures indicate that while Internet-based sales account for 6 per cent of

the household insurance sector and 13 per cent of all motor insurance sold, these percentages have been gradually increasing year on year since the beginning of the millennium at the expense of face-to-face sales whilst telesales have remained relatively static.

So are we likely to see an increasing appetite amongst consumers to buy protection insurance online, particularly if the FSA's recently launched consumer education programme hits home and they are encouraged to shop around for cover? This depends on both the financial awareness of the customer as well as their technical sophistication.

According to research from the Communities and Local Government department (formerly the Office of the Deputy Prime Minister) and our own analysis, the typical profile of someone buying MPPI falls into two distinct categories:

Profile 1: Couple aged between 30 and 39, employed in an intermediate managerial, administrative, or professional role, and living in Greater London. They have one or two young children, and have a mortgage commitment of over £1,000 a month. They bought the cover for peace of mind.

Profile 2: Couple aged between 40 and 49, employed in an intermediate managerial, administrative, or professional role, or in a supervisory, clerical, or junior administrative position. They live in the south east and have older children. Their mortgage commitment is around £800 per month, and they also bought cover for the peace of mind it brings.

Looking at these profiles, arguably they would be comfortable with using the Internet to source information and buy certain types of products. Given their desire for peace of mind, is it reasonable to assume that they would research the options available to them both online and in the personal finance pages, but probably seek advice when it came to the point of actually purchasing the cover? However, in a remortgage situation where they have previously had cover, would they buy direct from a stand-alone provider? Quite possibly, particularly if there is a drive from the regulator to educate the public as to what to consider when buying PPI.

Distributors of PPI products, whether selling face-to-face or via the Internet, have a multitude of factors to take into consideration, including an understanding of the different products available, the regulatory requirements placed on them, and capturing the individual needs and requirements of their customers - the latter being particularly important if advice is being given. So where does it go wrong? How are some firms currently falling down in treating their customers fairly?

For all sales, checking the eligibility of the customer and ensuring they understand the benefits and limitations of the policy is a key priority on the FSA's wish list.

- Eligibility is about checking whether the customer meets the criteria outlined in the terms and conditions of the policy - for instance, employment status or age - and that the product is right for the consumer. If it is not possible to check eligibility in a particular case, the firm must provide clear and balanced information for the customer to use and from which they can make an informed decision.
- Ensuring that the customer is fully aware of any parts of the policy that they may not be able to claim under is essential. Simply telling the customer to read policy exclusions and then cancel if they don't think it is providing the level of cover they want is not good enough. Significant and unusual exclusions must be made clear, and the customer should know where to look for more information in written material.
- Customers must understand what a pre-existing medical condition is and the importance of disclosing this type of information.

It becomes more complicated in an advised sale and firms must ensure they complete and retain an accurate statement of demands and needs:

- Suitability must be assessed when making a personal recommendation. This involves actively seeking information, rather than relying on the customer to provide it and the customer must be clear about whether they have received advice.
- Existing covers must be taken into account and factored into the recommendation.
- Customers must be in no doubt that PPI is optional, where this is the case, and that the credit agreement and the PPI cover are separate products and separate transactions.
- They must receive two separate quotations - one for the credit at point of sale with PPI, and one without the insurance cover.
- Customers must receive clear information about the cover, how much it costs, and - where a single premium is included within the credit - how much interest they are paying.

So will the ICOB effectiveness review currently being undertaken by the FSA apply more stringent rules and principles in its bid to ensure that PPI delivers the protection that the customer deserves? Will it determine that non-advised sales fail to provide enough checks and balances to ensure the consumer has enough information to make a decision without the benefit of the expertise and knowledge of a competent adviser?

Such a decision would fly in the face of the findings of OFT in its market study, which believes there should be more competition in the PPI market to deliver choice and value to consumers. It has clearly stated that the point of sale advantage experienced by some distributors means that there is little competitive pressure at the point at which consumers tend to buy the insurance and that stand alone providers therefore have difficulty in accessing these consumers, relying on those

who shop around. It would seem likely that this is a key area for the Competition Commission to review if indeed the OFT does make a market investigation reference.

With an emphasis on treating customers fairly, it is highly unlikely that the FSA would make the drastic move of 'outlawing' non-advised sales as in doing so it would remove a distribution channel of increasing interest and choice amongst consumers. Stand alone providers are equally regulated by the FSA and you can be sure that if any fall foul of the regulatory requirements now or in the future, the regulator will not hesitate to show that it means business as it has done with its enforcement actions over recent months.

Different consumers have different needs, not only when it comes to the type and level of cover required but also in how they make their decision to purchase PPI. Non-advised sales have an equally important role to play in the future of the market as does the more traditional advised sales route. What will be the determining factor in the success of either method is ensuring that the customer has access to quality cover that can be tailored to their individual needs, but that they are provided with clear and accurate information to help them make the right decision for their own particular circumstance.

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