



## **Association of Mortgage Intermediaries response to FSA consultation on the assessment and redress of payment protection insurance complaints – CP09/23**

### **Introduction**

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI). AMI is the trade association representing over 75% of UK mortgage intermediaries. Approximately 60% of all mortgage transactions are originated by the mortgage intermediary community, including 50% of regulated contracts.

Intermediaries active in this market act on behalf of the consumer in selecting an appropriate lender and product from within their panel to meet the individual consumer's mortgage requirements. Our members also provide access to associated protection products.

Our members are authorised by the Financial Services Authority (FSA) to carry out mortgage and insurance mediation activities. Firms range from sole-traders through to national firms and networks with thousands of advisers.

### **General Principles**

It is a matter of public law and good regulatory practice that regulators should not intervene in a market except where there is evidence of market failure. As Verena Ross pointed out in *Managing risk in government and business*, A Speech by to The Foundation of Science and Technology 9 May 2007:

“Being risk-based means that we need to prioritise our efforts and focus on the most significant risks. So, when deciding on new policy initiatives we take an evidence-based approach - we consider first and foremost whether there is a market failure that needs to be addressed and, if so, whether regulation is the best way to deal with it.”

Similarly, Hector Sants said in “Judgements on judgements - Retail firms and principles-based regulation” A Speech to the FSA Retail Firms Conference, 27 February 2008:

“We are an evidence-based regulator. We seek only to intervene, and intervene in a cost-effective way, where there is evidence of market failure and where the market itself cannot provide the necessary solutions.”

See also the comments of Dan Waters in FSA/PN/068/2007 31 May 2007. In this area, there is no such evidence either as regards sales or complaint handling standards by the intermediary community.

It will be noted that the Common Point of Sale Failings for PPI Sales letter accompanying the CP does not mention mortgages at all. This is consistent with the long-expressed view of the FSA that sales of mortgage protection insurance outside the sub-prime market have been conducted acceptably and that complaints have also been handled in an acceptable fashion.

In “The sale of payment protection insurance – results of thematic work”, November 2005, FSA commented in the executive summary:

“5. Our visit findings suggest that the 15 firms in our sample selling regular premium PPI in the prime mortgage sector generally had better levels of compliance in this aspect of their business compared to the other sectors (revolving credit, unsecured lending and sub-prime mortgages/secured loans) and so they posed a lower risk. Because of this, the majority of the visit findings in this report relate to the 30 firms operating in these other sectors.”

In the main text, the regulator went further. It noted that not only did the sale of regular premium PPI with prime mortgages stand out as compliant but it actually was the case that those firms selling prime mortgage regular premium PPI carried over the same standards to their sub-prime book. It says:

2.1 From our visits, the sale of regular premium PPI with prime mortgages stands out as different from the other sectors. In general, we found that compliance tended to be better in this sector compared to the other sectors. From this, we have concluded that PPI selling practices in this sector do not represent a high risk to our regulatory objectives.

2.2 As already mentioned, we generally focused on the activities of individual firms in one particular area of their business. As such, it cannot be assumed that the relatively good level of compliance in a firm’s prime mortgage business permeated that firm’s PPI business in other sectors (i.e. with unsecured loans or credit/store cards). The exception to this is a few firms in our sample who were predominantly selling prime mortgages but also doing sub-prime business. For these, we found the good levels of compliance for their prime business also applied to their sub-prime business.

2.3 The 15 firms selling regular premium policies in the prime mortgage sector (which included a bank, a building society and 13 mortgage brokers) shared a number of common characteristics:

- where they operated on an advised basis (which most of these firms did) they completed a full fact find on the mortgage and the customer’s protection arrangements;
- staff were generally more familiar with FSA regulation compared to the other sectors;

- they had good training and competence schemes in place (with a couple of exceptions);
- most offered a range of protection products, in addition to PPI, such as term assurance, critical illness cover and income protection and they generally demonstrated a reasonable understanding of the role of these different types of product;
- all of the brokers (as opposed to the two lenders) selected the PPI provider themselves rather than selling PPI provided by a particular lender and most stated that they selected their chosen provider on the basis of value for money for the customer and the quality of administration the provider offered;
- their PPI penetration rates were generally much lower compared to the other sectors; and
- they generally demonstrated good levels of compliance with our rules, with a few exceptions.”

2.4 The practices of most of the 30 other firms posed a risk to our consumer protection objective because of various aspects of their selling practices and/or their lack of proper compliance controls. Given this difference between the prime mortgage sector and the other sectors, all the remaining findings in this report relating to our visits refer to the 30 firms outside the prime mortgage sector.

In “The Sale of Payment Protection Insurance – results of follow-up thematic work”, October 2006 at p. 3, the FSA commented:

“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.”

In fact, there is no discussion of MPPI at all in the 2006 work suggesting strongly the point that firms recommending PPI in the prime mortgage sector had acceptable standards when doing sub-prime work and also suggesting that sub-prime mortgage intermediaries did not constitute as great a problem as the other firms subject to CP 09/23.

Just to prove that this was not a flash in the pan, the FSA revisited the issue again in 2007 in “The Sale of Payment Protection Insurance Thematic update”, September 2007. It said in the Executive Summary:

“Our latest work has confirmed our earlier findings that sales of regular premium prime mortgage PPI, on an advised basis, are most likely to meet our requirements. We found that the processes and controls around the selling of this specific product are likely to result in a more thorough assessment of the customer’s demands and needs when arranging protection insurance.”

All reference to mortgages were omitted from the thematic update of 30 September 2008.

This analysis strongly suggests that the inclusion of prime mortgage intermediaries within the scope of CP 09/23 is just a mistake. This is

reinforced by CP 09/23 itself. It only mentions mortgages in one place and this reference only relates to second charge mortgages which are currently not regulated even though PPI sold with them is:

“1.6 Our proposals on complaints handling are not the only action we are taking to ensure fair outcomes for consumers and that firms’ conduct adheres to our principles and rules. We are also taking targeted and intrusive supervisory action in areas of the PPI market where we have specific concerns about sales practices. We have taken 22 enforcement actions against the mis-selling of PPI, which have imposed fines totalling £11.8m and required the redress of consumers who suffered detriment. And recently we have:

- encouraged firms to stop selling single premium PPI with unsecured loans, which they have now agreed to do;
- obtained agreements from firms representing over 40% of face to face sales in the Single Premium Unsecured Personal Loan PPI market to review these sales and redress those consumers identified as mis-sold;
- begun targeted reviews of sales of single premium PPI on *secured* loans (second charge mortgages), which will be extended to sales of PPI on credit cards in due course”.

The rationale for CP 09/23 as set out in that document does not include the prime mortgage market at all and, additionally, not even the sub-prime market.

The recent DP 09/3 barely mentions insurance at all as part of the Mortgage Market Review. Even then, its references suggest that mortgages should be excluded from CP 09/23, notably:

6.18 The financial crisis has been the cause of major economic distress for many people. Many are in arrears and facing real problems servicing their debts. Consumers were unprepared going into the financial crisis and a cautious attitude to risk amongst most of the population was not matched by behaviour. One study estimated that **only one-fifth were ‘relatively secure’ with appropriate insurance cover** and adequate savings, without being highly exposed to stock market changes or risky borrowing. **A further fifth were ‘highly exposed’ or ‘inherently at risk’, either through high levels of debt, or inadequate protection against income shocks.”**

One cannot encourage intermediaries to sell the insurance cover and provide adequate protection against income shocks while imposing past reviews of rarely received complaints.

Looking outside FSA research, the Financial Ombudsman Service (FOS) which has if anything been more vocal than the FSA about PPI mis-selling and complaint handling problems has not referred to mortgage PPI at all.

The FOS Annual Review 2008/2009 comments:

“The PPI complaints we see mostly concern policies that were paid for with a single premium, where the up-front cost was added to an unsecured or second-charge loan. We also see a significant number of cases relating to payment-protection insurance sold alongside credit cards. However, **mortgage payment-protection insurance (MPPI)** and other forms of payment protection **have not given rise to significant volumes of complaints to the ombudsman service.**”

The case studies in Ombudsman News Issue 62 do not mention intermediaries or mortgages. Issue 71 only refers to second mortgages and not to intermediaries. The online PPI resource on the FOS website does not mention mortgages.

By sector, FOS found that mortgage and insurance intermediaries and IFAs only were complained about in 10% of its new cases. It found only a small increase in complaints against mortgage and general insurance intermediaries. One has to bear in mind that PPI represents a tiny proportion of these firms' activities. The 3% for IFAs shows this sector to be one of the least complained against, considering the volume of business it generates through the vulnerable advice sector. Of complaints about PPI insurance, mortgage intermediaries and IFAs represent less than 3 % being included with Building Societies in this category.

If one looks at the FOS statistics for complaint volumes, only Homes.co.uk of the mortgage intermediaries which is not owned by a major bank has more than 60 cases. Of an IFA group, only Sesame appears in the statistics with 9 general insurance cases. Incidentally, Sesame's uphold rate of 32% across all its business areas compares very favourably with the FOS average of 57%.

The FSA has found further evidence that IFAs, many of whom are also mortgage intermediaries handle complaints well even in highly controversial areas. On 9 December 2005, the FSA reported in “[Mortgage endowment complaints handling within small investment firms](#)” to quote the accompanying press release, FSA PN/134/2005:

“Based on a sample of 51 firms and 412 files reviewed, the FSA's findings identified that in the majority of cases the decisions being made by small firms we visited to reject or uphold a complaint are appropriate.”

Overall, there is simply no evidence to support any suggestion that mortgage brokers or intermediaries who have sold PPI with prime mortgage loans have mis-sold the policies or mishandled complaints relating to them. Indeed all the evidence points in the other direction. Their inclusion within the CP 09/23 review runs counter to all of the FSA's evidence and that of the external body best able to judge: the FOS. To include such intermediaries would be arbitrary and contrary to all the available evidence and thus beyond the FSA's legal powers.

For the sub-prime market, one can say the same in relation to intermediaries operating in both the prime and sub-prime markets. The FSA has consistently reported the absence of any selling problems in this sector and there is no evidence of problems at FOS if anything quite the opposite.

The mortgage intermediary market engaged entirely in the sub-prime market is in a different category. It is noticeable, however, that the FOS has expressed no concerns in this area, suggesting that while some firms have mis-selling issues, the vast majority do not appear to be mishandling complaints even if they do have such issues. Where an individual firm is found to have mis-sold policies, it would be more appropriate for this to be handled on a firm-by-firm basis rather than tarring all the intermediaries in the same sector with one brush.

There is in any event no evidence of regular premium mortgage PPI mis-sold or indeed regular PPI of any type having been discovered as being mis-sold by either the FSA or the FOS.

### **Consultation questions**

**Question 1: Do you agree the proposed approach to the assessment and redress of PPI complaints is fair and balanced and will provide fairer outcomes for more consumers?**

There are a number of features of the proposed compensation approach which are unclear and which appear to be over-generous to complainants.

Members are concerned that they will be unable to carry out the regular premium calculation. There is in any case a good argument for limiting it to the situation where the customer is likely to be able to claim and wishes to retain the policy but in regular premium form. We would ask the FSA to ensure that the provider located offering this policy be persuaded to make it available for appropriate payment to provide the necessary benefits. Otherwise, there is likely to be a muddle. In truth, the one policy would almost certainly never have been recommended by mortgage intermediaries..

The 8% interest rate is wildly in excess of anything that an investor could have obtained in the last decade. It should be reduced. It is the judgement rate and FOS is only required to have regard to the law. It is not required to apply the law only applicable to courts in a situation where a court might be embarrassed to apply such a rate. Indeed, in the Commercial Court, a more realistic approach is adopted providing interest in line with bank base rates and adoption of this approach was recommended by the Law Commission in 2004. See [www.lawcom.gov.uk/docs/lc287sum.pdf](http://www.lawcom.gov.uk/docs/lc287sum.pdf). This seems more appropriate. As the Commission said in its summary paper:

“ 1... The current system for awarding interest before judgment leads to widespread confusion and mistakes. Even when the rules are applied correctly, they bear little relationship to commercial reality. In short cases, debtors often pay too much – frequently paying 8% at a

time when base rate is 4% or less. In long-running cases the present ban on compound interest means that claimants may be undercompensated.

2. The Law Commission's proposals are designed to provide claimants with fair compensation for delays in payment, without penalising debtors. We make three main recommendations:

(1) The courts should normally award interest at a **specified rate**, set each year at 1% above the Bank of England base rate. This would provide a starting point, though the courts would have discretion to depart from the rate where there was good reason to do so. In particular, where claimants could show that they had been forced to borrow at higher rates, they would be able to apply for higher interest.

(2) The courts should have a power to award **compound interest** in appropriate circumstances. For debts or damages of £15,000 or more, if claimants asked for compound interest there would be a presumption that they should receive it (though the presumption could be rebutted for good reason). For cases involving less than £15,000 there would be a rebuttable presumption that interest should be simple."

There is also a concern about the deduction of tax from any interest payments. Essentially, the proposed approach breaches the Taxes Management Act in that tax needs to be deducted at basic rate.

Intermediaries will need access to the relevant certificates of deduction. See [http://www.financial-ombudsman.org/publications/guidance/comp\\_tax.htm](http://www.financial-ombudsman.org/publications/guidance/comp_tax.htm).

**Question 2: Do you agree that the regular premium referent price we propose to stipulate is a reasonable one?**

FSA has assumed an appropriate comparator regular premium policy price of £6 per £100 of benefit. However, the product that FSA identified as a comparator was from an internet only source and was only for unsecured loans. It would therefore seem inappropriate to compare it to a mortgage protection product. The short consultation period has not provided sufficient time for a more realistic price to have been calculated and then justified to FSA.

**Question 3: Do you consider that this alternative approach to paying for future regular premium cover would be fair to relevant consumers and practicable?**

We do not consider this question applies to mortgage intermediaries who will have predominantly sold regular premium MPPI.

**Question 4: Do you agree that the proposed guidance on the fair assessment of complaints and the evidence about them is relevant, helpful, reasonable and appropriate?**

We do not consider that these proposals should apply to mortgage intermediaries for the reason stated above.

**Question 5: Do you agree that requiring the re-assessment of rejected PPI complaints against the proposed guidance is a fair and proportionate requirement?**

We do not consider that these proposals should apply to mortgage intermediaries for the reason stated above.

**Question 6: Do you agree with the scope of the review rule?**

We do not consider that these proposals should apply to mortgage intermediaries for the reason stated above.

**Question 7: Do you agree that the immediate implementation of our proposals would be reasonable?**

No clear explanation is given in the CP as to why the consultation paper has been reduced to one month. In our experience, three months is the minimum required to ensure that the proposed rule changes do not need to be subsequently amended. The issue of PPI mis-selling goes back to 2005 at least when the FSA was aware of the nature of the problem. Consumer detriment will not be caused by any delay because the past review will incorporate any complaints rejected during the delay. A private pre-consultation is no basis for a shortened public consultation in which many experts who were not privy to the earlier discussions have been unable to contribute. A period of three months is likely to reduce the scope for errors due to the brief period for reflection.

**Conclusion**

Accordingly, AMI calls for the scope of the proposals included in CP09/23 to be limited. We request the FSA exclude all sales of both single and regular premium PPI where these are linked to a loan or mortgage linked to property from the scope of these proposals. This will avoid unnecessary activity amongst firms not currently in receipt of significant volumes of complaints and avoid consumers considering voiding insurance contracts which are valuable, particularly at this point in the economic cycle.

AMI  
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