

## **EIOPA Opinion on Payment Protection Insurance**

### **Legal Basis**

1. This opinion is issued under the provisions of Article 29(1)(a) of Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 (hereafter the 'Regulation'). As established in Article 29(1)(a) of the Regulation, EIOPA shall play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.
2. To this end, EIOPA has provided this opinion concerning consumer protection issues related to Payment Protection Insurance (PPI).
3. This opinion is addressed to the National Competent Authorities (NCAs) represented in EIOPA's Board of Supervisors.

### **Context and aim**

4. EIOPA is from a European perspective attentive to the effectiveness of the financial system and has identified consumer protection issues surrounding PPI to be a cause of concern. In this respect, in EIOPA's "Initial Overview of Key Consumer Trends in the EU", consumer protection issues related to PPI have been identified by some EIOPA Members in their jurisdiction.
5. In view of this, this opinion is aimed at drawing Member States' attention to consumer protection issues regarding PPI products. On the basis of analysing detailed information on existing national practises, EIOPA recommends NCAs to explore their national markets and report back to EIOPA with a view to deciding potential (further) investigation and any possible (further) supervisory and/or regulatory action at national level.
6. For this purpose, the detailed information on existing experience is made available in the form of a *background note*, listing the most important consumer protection issues regarding PPI and the ways some Member States chose to tackle them.

7. It is noted that differences in products, regulatory frameworks and the maturity of the market result in variations in the issues national authorities face, and as a result of this, any market intervention must be tailored to individual characteristics of the given market.

### **What is PPI?**

8. PPI is an insurance product designed to provide coverage for the consumer of a financial obligation (generally mortgage or consumer loan repayment) in case they are unable to fulfil a payment. The risks covered by PPI generally include accident, sickness and unemployment, and for certain products often life; however, it is worth noting that mortgages are sometimes sold together with insurance covering damage to the property as well.
9. EIOPA acknowledges that PPI products, when properly designed and sold, serve legitimate consumer needs. Yet, EIOPA also acknowledges that, in a number of jurisdictions, significant cases of misselling have occurred, to the detriment of consumers and negatively affecting the reputation of the insurance sector as a whole.
10. In a few countries, EIOPA has also become aware of some firms developing an alternative new generation of protection products. To the extent they share some of the same characteristics as PPI, these newer products could pose some of the same risks, unless undertakings take particular care with their product design and sales practices to ensure the problems with PPI are not repeated.

### **What types of consumer protection issues have been identified with PPI?**

11. PPI is on the agenda for many different reasons in various jurisdictions. Consumers are often not aware that they buy an insurance product or that they buy a product that offers a different coverage than expected. A further issue is that consumers are not always able to choose the product that best suits their needs in terms of price and coverage. Although several other causes have been identified in national jurisdictions that contribute to suboptimal outcomes in PPI markets, the current EIOPA analysis identifies five areas that are most relevant for consumer protection:
  - a) Mis-selling issues
  - b) Market imperfections
    - i. Cross-selling issues
    - ii. Potentially unfavourable effects of group insurance contracts
    - iii. Information asymmetry
    - iv. Failings in product design.

12. An issue that certainly has drawn a lot of public and media attention in several countries is *mis-selling* of PPI, where breaches of business conduct rules resulted in significant consumer detriment. The most frequently arising mis-selling issues are *eligibility/suitability* issues (where consumers are unable to claim benefits, because their individual situation is not covered by the policy or PPI is not in their best interest, although it is required by national law), and the provision of misleading information. *Misleading information* often includes hints that PPI is compulsory (although it is not true in the given case), or omits essential product characteristics.
13. Apart from mis-selling, *market imperfections* have extensively contributed to the fact that in many markets, consumers are (or have been) forced into distorted choices, which results in higher prices for them.
14. One of the major factors contributing to PPI problems is *cross-selling*, i.e. that payment protection products and loan products are often offered together (jointly), with the loan product being the primary product for the consumer. This market feature can sometimes take the form of a tying practice (meaning that insurance - often from the same company or group - is made mandatory to obtain a loan from a given provider), which is likely to result in very significant market power (economic strength) for distributors (mostly banks or other loan providers). This market power resulted in an upward pressure on the level of commissions and had an unfavourable effect on consumer prices.
15. Related to cross-selling, but raising additional issues in itself, *group insurance* may have an unfavourable effect on consumer choice and claims. With group insurance contracts, the insurance contract is originally signed by the loan provider, leaving the consumer with no choice of the insurance provider. Further, these group insurance contracts could result in some uncertainties around the beneficiary as well.
16. Apart from misleading information at the point of sale, *information asymmetry* also frequently contributes to unfavourable outcomes and consumer detriment. Lack of individualised information (personal quote) and comparable information, as well as limited consumer financial literacy all present impediments to informed consumer choice. In addition, consumers often focused on the loan products and less on PPI.
17. A further issue that often increases the likelihood of consumer detriment is *product design*. Limitations in coverage, mismatches in the duration of the loan product and insurance product or selling PPI with a single premium (paying premiums as a lump sum at the start of the contract) also make it more likely that consumers do not exactly get what they expect.

## Supervisory and regulatory actions in Member States

18. Consumer protection issues around PPI have resulted in supervisory and regulatory actions in some Member States. A detailed analysis of these actions and an overview of national experience are presented in the accompanying background note.
19. The actions undertaken by Member States are either supervisory actions or regulatory measures that address specifically consumer protection issues in PPI. These measures sometimes require legislative modifications at parliamentary level, in other cases they are addressed in the form of sector legislation or guidance issued by the competent authorities.
20. *Mis-selling issues* are often addressed by individual supervisory actions, such as on-site inspections or enforcement procedures based on evidence of poor selling practices or of poor handling of consumer complaints. Some authorities have taken steps to ensure that undertakings have a proper complaints-handling mechanism in place or requested firms to review their PPI sales for a given period from a compliance perspective. Aiming to avoid any misleading information, specific information requirements at the point-of-sale have been introduced, and a guidance paper on the proper assessment of consumer suitability has been issued.
21. The market power arising from *cross-selling* of PPI with loan products is often considered as a major factor contributing to distorted consumer choice. There have been significant measures to introduce comparability and competition at the point-of-sale for loans, requiring loan providers to present alternative offers, and that these offers are assessed equally should they provide the same coverage. There have also been rules that focus on avoiding conflicts of interest between the loan provider and the insurance underwriter, prohibiting the same entity from being beneficiary and distributor of the same policy.
22. When trying to empower consumers to make an informed choice, the availability of *comparable information* is another key element. This is sometimes targeted by requiring the timely provision of a personal quote, and prescribing a standardized format for disclosure of price, sometimes together with other product characteristics. The comparability of information is ensured by presenting a number of offers at the point of sale, or via online tools.
23. There have been some measures that influence *product design*; these can improve the outcome consumers receive and help comparability as well. For transparency reasons and to ensure proper refund in case of cancellation, the use of policies sold with a single premium have been prohibited or limited, and the refund process has been regulated. To avoid insufficient

coverage, and to help comparability, minimum information on content of the policy has been regulated in some Member States.

**Taking the above into consideration, EIOPA recommends the following next steps:**

24. This opinion is aimed at building a common Union supervisory culture and consistent supervisory practices. EIOPA recommends that NCAs should analyse their national markets and on this basis decide whether PPI merits (further) investigation and any possible (further) supervisory and/or regulatory action at national level, based on the findings of this opinion.
25. NCAs are requested to provide feedback on previous actions in this field if not yet covered in the background note, and on their decision whether they undertake any action on the basis of this opinion, including the details of any market investigations, regulatory or supervisory actions regarding PPI, within six months of its publication.

This opinion and the accompanying background note will be published on EIOPA's website.

Done at Frankfurt am Main, 28 June 2013

*[signed]*

Gabriel Bernardino

Chairperson

For the Board of Supervisors