FINAL DECISION

complaint by:	Mr and Mrs B
complaint about:	the firm
complaint reference:	
date of decision:	November 2008

summary of complaint

This final decision is issued by me, Tony Boorman, an ombudsman with the Financial Ombudsman Service. It sets out my conclusions on the dispute between Mr and Mrs B and the firm. Under the rules of the Financial Ombudsman Service, I am required to ask Mr and Mrs B either to accept or to reject my conclusions in writing.

The dispute is about the sale of a single-premium payment protection insurance (PPI) policy, recommended by the firm in connection with a secured personal loan. The recommendation was made in February 2006 (after the introduction of regulation of such sales by the Financial Services Authority) during a phone conversation.

I have considered all the available evidence and arguments from the outset, in order to decide what is fair and reasonable in the circumstances of this complaint. For the reasons I set out below, I have determined the complaint in favour of Mr and Mrs B and have made an award against the firm.

background to complaint

a) events leading up to the complaint

Mr and Mrs B faced significant financial difficulties. They had various credit-card and other debts from a number of providers. In total these debts amounted to around £89,000. Mr and Mrs B faced significant difficulties in meeting the minimum monthly payments required to service these debts (around £2,500). Mr B was self-employed and his wife was employed and training as an accountant.

Mr B approached the firm to help him resolve his difficulties. The issue was discussed in two phone conversations (recordings of which have been made available to me). In February 2006 the firm agreed to provide a secured loan (a second-charge mortgage) of £95,000 that was to be repaid over twenty five years.

This money was to be used to consolidate the previous debts (including over £30,000 with businesses in the same group as the firm). The firm (acting as an authorised insurance intermediary for this purpose) also recommended that Mr and Mrs B should purchase its branded “loan protection insurance” (PPI) policy – the greater part of which was underwritten by a general insurer within the same group of companies as the firm. This PPI policy had a duration of five years and was paid for with a single premium of £23,265.50 which was added to the loan of £95,000 – making the total amount advanced to Mr and Mrs B £118,236.50. In this way, the cost of the premium *plus* the interest on that aspect of the loan was set to be recovered over the 25 year term of the loan. The premium for the PPI policy (but *not* the interest paid on that premium) was refundable in full at the end of the five year period, subject to certain conditions, including no claims being made on the policy.

b) Mr and Mrs B's complaint and the firm's response

Mr and Mrs B considered that the firm had acted unfairly in respect of the sale of the PPI policy. They said that they strongly believe the sale was not carried out correctly. They were sold a product they *"did not have a full understanding of, and which costs far outweighed its benefits."* They say this has caused them "*considerable financial and emotional heartbreak.*" They conclude that they have not been treated fairly by the firm.

The firm responded promptly to Mr and Mrs B's complaint. It reiterated the terms of the loan and PPI policy. It said these matters were explained adequately at the time of the sale. In particular, it said that during the substantive phone call to arrange the loan, the firm *"went through a series of questions with you to ascertain if you had any existing cover in place to cover this loan and whether the policy was suitable for you, based on the answers given it was recommended to you."* The firm did not uphold the complaint.

However, following further correspondence with Mr and Mrs B, the firm said in January 2008 that it was "*satisfied that you were provided with enough information as to the suitability of the policy.*" Nonetheless, it offered "*with no admission of liability" "an enhanced rebate of £8,190.97 in addition to the £3,302.18 that will be applied to your loan account on cancellation of the policy."*

Mr and Mrs B felt that this response was inadequate and they referred the matter to the Financial Ombudsman Service. My adjudicator considered the matter. In her assessment of the case, she concluded that the policy had indeed been mis-sold and that the firm should compensate Mr and Mrs B by returning them to the position they would have been in, had they proceeded with the loan but *without* the PPI policy (in effect, to return to Mr and Mrs B the payments they have made in relation to the PPI policy *plus* interest). The firm did not accept this assessment. It asked for a delay in resolving matters, but I do not believe a delay is necessary – nor would it be fair to Mr and Mrs B. So as agreement cannot be reached, the matter falls to me to determine.

my findings

I have considered all the evidence and arguments very carefully from the outset – including the firm's response to the adjudicator's conclusions and the recordings of the two relevant phone conversations – in order to decide what is fair and reasonable in all the circumstances of this case. Having done so, I have come to the same overall conclusions as the adjudicator, and for broadly the same reasons.

a) relevant considerations

This sale was made after the introduction of FSA regulation of insurance mediation. Whilst the general principles that I need to consider in assessing cases such as this are, in large part, similar both before and after regulation by the FSA, it is important to note the relevant regulatory regime that applied at the time. The FSA Principles apply to all authorised firms including the firm (acting as an insurance intermediary). Of particular relevance to this dispute are:

- Principle 1 (integrity):
  “A firm must conduct its business with integrity”

- Principle 6 (customers’ interests):
  "A firm must pay due regard to the interests of its customers and treat them fairly"

- Principle 7 (communications with clients):
  "A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading"

- Principle 8 (conflicts of interest):
  “A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client”

- Principle 9 (customers: relationships of trust):
  “A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment”

In addition, it is relevant to take into account the more detailed rules set out in “ICOB” (the insurance conduct of business rules), especially the provisions of ICOB 4.3 (suitability), ICOB 4.4 (statements of demands and needs) and ICOB 5.3 (provision of information to retail customers). In particular, ICOB 4.3.1R requires that:

> *“An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal recommendation to a customer to buy or sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made.”*

I also need to take into account the law (and especially the provisions of insurance law), industry codes and good industry practice.

In this respect, it is relevant to note that there has, for some time, been regulation or codes governing the sale of insurance products such as PPI. There is much in common between the present statutory regulatory regime and the non-statutory provisions that preceded it (and indeed the position at law). The non-statutory provisions no longer apply as specific requirements on those selling insurance. But I consider that they still represent a helpful guide to good industry practice.

For example, in the period immediately before statutory regulation in 2005, the General Insurance Standards Council (GISC) promised in its Code that its members would:

- “*act fairly and reasonably when we deal with you [the customer];*
- *make sure that all our general insurance services satisfy the requirements of this Private Customer Code;*
- *make sure all the information we give you is clear, fair and not misleading;*

- *avoid conflicts of interest or, if we cannot avoid this, explain the position fully to you;*
- *give you enough information and help so you can make an informed decision before you make a final commitment to buy your insurance policy."*

The GISC Code provisions included:

"3. We will give you enough information and help so you can make an informed decision before you make a final commitment to buy your insurance policy."

"3.2 We will make sure, as far as possible, that the products and services we offer you will match your requirements …

- *If it is practical, we will identify your needs by getting relevant information from you.*
- *We will offer you products and services to meet your needs, and match any requirements you have.*
- *If we cannot match your requirements, we will explain the differences in the product or service that we can offer you.*
- *If it is not practical to match all your requirements, we will give you enough information so you can make an informed decision about your insurance."*

"3.3 We will explain all the main features of the products and services that we offer, including …

- *any significant or unusual restrictions or exclusions;*
- *any significant conditions or obligations which you must meet."*

"3.4 We will give you full details of the costs of your insurance."

"3.5 If we give you any advice or recommendations, we will:

- *only discuss or advise on matters that we have knowledge of;*
- *make sure that any advice we give you or recommendations we make are aimed at meeting your interests; and*
- *not make any misleading claims for the products or services we offer or make any unfair criticisms about products and services that are offered by anyone else."*

The Association of British Insurers (ABI) codes (which pre-dated GISC) also set out relevant requirements. For example the ABI General Insurance Business Code of Practice for all Intermediaries (1989) (the ABI Code) said that it *"shall be an overriding obligation of an intermediary at all times to conduct business with utmost good faith and integrity."*

The ABI Code stated as one of its general sales principles that the intermediary shall *"ensure as far as possible that the policy proposed is suitable to the needs of the prospective policyholder."* It also included requirements about "*Explanation of the Contract*". It said the intermediary shall *"explain all the essential provisions of he cover afforded by the policy or policies he is recommending so as to ensure as far as is possible that the prospective policyholder understands what he is buying; [and] draw attention to any restrictions and exclusions applying to the policy."*

Taking the relevant considerations here into account, I conclude that the overarching question I need to consider in this case is whether the firm gave Mr and Mrs B information that was clear, fair and not misleading – in order to put them in a position where they could make an informed choice about the transaction they were entering into and the insurance that they were buying; and whether, in giving any advice or recommendation, the firm took adequate steps to ensure that the product it recommended was suitable for Mr and Mrs B's needs.

But overall, taking account of these factors, I must determine this dispute between the firm and Mr and Mrs B by reference to what is in my opinion fair and reasonable in all the circumstances of the case.

b) did the firm take adequate steps to ensure that its recommendation was suitable?

It is clear that the firm gave Mr and Mrs B "a recommendation". It was therefore under a duty to take all reasonable steps to ensure that recommendation was suitable.

I say this because the firm itself describes what it did as a recommendation. During the primary phone conversation, the firm's representative says: "*In that case ... I can recommend based on the information you provided that in the event of loss of income [the firm's] payment protection could assist you in paying your borrowing.*"

During the phone call in which the loan and policy were initially agreed, the firm asks a number of questions of Mr B of relevance to its assessment of the suitability of the PPI policy. This includes a question about loan-protection cover in relation to the first mortgage on the property (he confirms he has this). He also confirms he has an "accident critical illness and accident insurance" (also provided from the same group of companies as the firm). In addition, Mr B mentions life insurance for £455,000.

Mr B is self-employed. The firm's representative says *"... when I say redundancy, because you are self-employed okay, we cover self-employed. It's not an issue with us alright? When I say unemployment, if your business was to wind up you could no longer trade. Do you have any policies in place that would give you an income?"* Later she notes that Mr B would not get *"standard sick pay because you are self-employed."* (In fact, disability benefits for self-employed customers are restricted under the policy.)

It seems to me that the firm did not fully consider these points in making its recommendation. Mr and Mrs B already had significant related cover (at least two parts of which were arranged within the same group of businesses as the firm). Mr B was self-employed and the policy has restricted benefits for a self-employed person. The firm also failed to take cost into account in making its recommendation. It is clear that cost is a very significant part of Mr and Mrs B's concerns. They were, after all, seeking a consolidation loan primarily to reduce their monthly outgoings. The insurance they were recommended cost over £23,000. But the benefits payable under the policy were limited.

Policy conditions limit unemployment benefits to 12 months (and normally require a sustained return to work before further periods of claim would be successful) and only Mr B would be covered for the sickness and unemployment benefits. I calculate that he would have had to have made three separate successful unemployment claims (or a single disability claim), covering over 27 months of the 5-year policy, before the benefits payable under the policy would exceed £23,000. I have, for the purpose of this calculation, ignored the life benefits of the policy. These could readily have been obtained in a far more economic manner. And in the case of Mr and Mrs B, they had, in any event, told the firm that they already had some cover here. Indeed, when the facts are set out in such a manner, it is difficult to see how the product could have been recommended in good faith – or why a customer in a position to make an informed choice would have chosen to purchase such a policy on these terms.

Some further points should be made about cost. First, this policy included a "premium return" so that the policy premium would be returned to Mr and Mrs B, if they did not make a claim and kept the policy for five years. This was subject to various restrictive procedural requirements. (The Financial Ombudsman Service has considered cases on issues involving premium-refund provisions before – see, for example, case study 01/14 in the January 2001 issue of *ombudsman news.*) But this offer was heavily emphasised by the firm in its dealings with Mr and Mrs B.

What received less emphasis was that the premium was added to the loan and interest added. The monthly repayments of £210.96 for the PPI policy did not end after the five years covered by the policy. The repayments were set to continue throughout the 25 years of the loan. By my calculation, the cost of the PPI policy over the life of the loan would be over £63,000 (including nearly £40,000 of interest). At the end of the five years' cover, Mr and Mrs B would still need to pay the firm around £50,000 during the remainder of the term (although this would be reduced by any returned premium, especially if that was then used to reduce the level of outstanding debt).

By any normal standards, this PPI policy was exceptionally poor value for money for Mr and Mrs B. This is a consideration that the firm should have taken into account in making its recommendation. ICOB 4.3.6R provides that in assessing whether an insurance contract is suitable, the insurance intermediary must take into account at least *"the cost of the contract, where this is relevant to the customer's demands and needs; and the relevance of any exclusions, excesses, limitations or conditions in the contract."*

The firm was aware that Mr and Mrs B had some financial problems. They were, after all, seeking with the active encouragement of the firm to consolidate £89,000 of debt – clearly with the primary objective of reducing the outgoings of about £2,500 that they incurred each month on servicing that debt. Mr and Mrs B hoped for a significant improvement in their circumstances but they could not be certain. It appears clear to me that, in thinking about any loan and connected insurance policy, a relevant consideration was to consider how far that arrangement would be flexible, should the customer's circumstances change. In this market, it is not uncommon for customers to re-arrange their loans before the end of the planned term – particularly those in circumstances like Mr and Mrs B. The firm has provided no evidence to show that this was not, in fact, a relevant consideration for Mr and Mrs B. Indeed, in my view the balance of evidence suggests that it *was*.

I conclude that the firm did not consider whether or not Mr and Mrs B required flexibility in the PPI policy, when considering the product it should recommend. It should have done so. It is not sufficient for the firm to say that the customer did not emphasise the issue (and/or that the issue was not set out in a demands and needs statement by the customer). The firm was the professional insurance adviser which had (or should have had) a knowledge not just of the products available but also of the way in which the substance of those products was likely to interact with the common demands and needs of its customers – particularly where the feature was significant and unusual.

I note that ICOB (4.3.2R) requires an insurance intermediary, in assessing its customer's demands and needs, to:

> *"seek such information about the customer's circumstances and objectives as might reasonably be expected to be relevant in enabling the insurance intermediary to identify the customer's requirements. This must include any facts that would affect the type of insurance recommended, such as any relevant existing insurance."*

– and that the intermediary should "*have regard to any relevant details about the customer that are readily available and accessible to the insurance intermediary."*

The firm suggests that Mr and Mrs B had the opportunity during the sales process to become aware of the relevant facts surrounding the cancellation terms and other provisions of the policy – and that, accordingly, I should not uphold this complaint. But this ignores the fact that the firm recommended the product. Mr and Mrs B were entitled to place trust in the professional advice of the firm that this was a suitable product for them. I have concluded that the firm did not take reasonable care to ensure the suitability of its advice to Mr and Mrs B, and that Mr and Mrs B acted in reliance on that advice.

c) did the firm provide information that was clear, fair and not misleading?

The conclusion I have reached on the recommendation made by the firm would be sufficient basis on which to determine this complaint in favour of Mr and Mrs B. But I think it will also be helpful to consider the information that the firm provided to Mr and Mrs B. The firm says that, in addition to the discussions with Mr and Mrs B, it sent them relevant information at the time of the sale, including a "Loan Agreement" and a "Policy Summary" (the "keyfacts" document).

The loan agreement included figures for the "cash loan", the "PPI loan" and the total. It also showed the total monthly repayments (that is, including interest) – broken down by original loan, insurance premium and total. It did not show the total or monthly *interest* to be paid on these items. The document notes that *"you have chosen to protect your repayments…"* and *"you have applied to purchase payment protection plan insurance."* The loan agreement also deals with early settlement, where the amount payable will be *"the balance of the Loan"*.

The "keyfacts" document is a closely written leaflet of eight pages of text. Towards the end of page six, the document says: *"7. Early Termination of Policy"*. This notes: *"Your policy will automatically terminate if your agreement ends. After the initial cooling off period we will only refund part of your premium. We will not calculate any refund on a pro-rata basis because most of the premium is apportioned to the earlier part of the term when most of the risk is borne. The premium refund will be calculated according to the premium refund rates applicable at that time and will be substantially less that the amount you originally paid."*

Whilst not perhaps of direct relevance to this decision, I would note in passing that this provision seems, as expressed, likely to be contrary to the requirements of the Unfair Terms in Consumer Contracts Regulations – as it gives the insurer a wide-ranging and ill-defined discretion. I note that the Financial Services Authority has made a number of decisions on similar points. Certainly, it is in my view a significant and onerous term. But it was not highlighted in the documentation in a way that was likely to bring it to the attention of Mr and Mrs B.

In the lengthy phone discussion with Mr B, and in a shorter second call with Mrs B, some mention is made of these matters. It is worth summarising the main phone conversation. The first and most significant call between Mr B and the firm (a recording of which has been made available to me) lasts about 20 minutes. The first six minutes are spent confirming the total debts Mr and Mrs B have and wish to consolidate. The firm's representative confirms that Mr B is making payments of some £2,500 a month on around £89,000 of debt. She then confirms that the firm *"basically had this approved on up to £95,000, okay, so if you want to, you can take the additional as basically funds for yourself."* (I note that, in the end, the firm will provide a loan of over £118,000 – once the PPI loan is added.)

Mr B confirms he would like to borrow the £95,000 offered. The representative then says: *"There are just a couple more questions I need to ask you. It's usually easy now, okay, and it's quite straightforward. It will be based around yourself, because I have got you on a slightly higher income now, okay? I need to ask you about what insurance you have in place to cover this loan all right?"*

This conversation takes a further four minutes, whilst the representative asks about – and then recommends – insurance (she does not at this stage mention the price). Only then does she confirm that the firm will offer the loan (with insurance) over 25 years. She asks Mr B about his present monthly outgoings on the debts he is consolidating (£2,500). She then (after 11 minutes) quotes the total price: "*if you take this fully protected it's only going to be £1072.35 per month, okay?*"

She introduces the total cost of the policy by saying, after setting out the benefits of the policy: *"At the end of the five years if you haven't claimed on the policy we are going to give you all your premiums back as a cash refund, okay? So at the end of five years you are looking to get back £23,265.50."*

After a discussion about the timing of the payments, Mr B asks: *"So I just start paying off everything?"* The representative replies: *"Exactly, this will basically put you in a much better position, okay? So I've got this final bit of script to read to you. Just bear with me one second, okay? So [Mr B], you have applied for [the PPI policy] ..."*

The representative then summarises the general benefits, and the restrictions on pre-existing conditions and on certain claims, and says: *"If you settle the loan or cancel the insurance before the end of the five year term, you will not get a full cashback refund and will not be proportional but will be significantly reduced and will not include a refund of the interest paid on the premium, okay? So the cost of your policy is added to the loan. However, our loans are not dependent on taking any insurance offered."* This takes place at the very end of the 20-minute call, and is read out much in the spirit of the small-print warnings at the end of certain financial advertisements.

It is hard not to conclude that the whole process that day, and subsequently, was designed to hide from Mr and Mrs B the true nature of the transaction they were recommended to enter in to. Mr and Mrs B say that they felt that accepting the PPI policy was necessary, if they were to obtain the loan they required. That was not the case – and that was confirmed at the time by the firm. But having listened to the phone call, I can see how Mr B formed the strong impression that accepting the PPI policy was, indeed, part of the assessment of whether or not the loan he wanted would be granted.

In any event, Mr and Mrs B were in a vulnerable position. It is clear that they needed the loan urgently. But the firm took advantage of this. I do not consider that, in the way it carried out this transaction, the firm acted with integrity or with due consideration to the need to manage conflicts of interest and the need to consider the interests of its customers. In insurance law terms, it did not exercise "utmost good faith" in carrying out its insurance functions. It certainly did not, in my view, provide a balanced and fair account of the policy it was recommending at the point of sale.

And I do not view the information provided after this in writing as sufficiently clear to correct the position. The arrangements being entered into were significant. It is reasonable to assume that Mr and Mrs B took some time and trouble to consider the matter. But only the most careful and assiduous reader of the documentation would have been able to identify the important factors here. I conclude that the firm did not pay due regard to the information needs of Mr and Mrs B.

I should also note that this attitude to information and its customer was also apparent in the way in which the firm dealt with this complaint. The offer of an "enhanced refund" was at best disingenuous. I am, in particular, disturbed that Mr and Mrs B were not reminded, at that point, that the policy provided for a full refund of premiums if no claim was made after five years.

summary of conclusions and findings relevant to the determination

For the reasons set out above I have concluded that in the case of Mr and Mrs B the firm:

- failed to take reasonable care to ensure the suitability of its advice;
- did not pay due regard to the information needs of its customers.

Overall, I conclude that the firm failed to pay sufficient regard to the interests of its customers, Mr and Mrs B, and that it did not treat them fairly. Accordingly, I conclude that I should determine this complaint in favour of Mr and Mrs B.

fair compensation

Having concluded that I should determine the complaint in favour of Mr and Mrs B, I now need to consider what award to make.

In determining the award, the law can provide a useful tool with which to analyse the variety of ways in which claims to compensation can be made. But it is for the ombudsman to arrive at a view as to what he considers fair compensation.
Where a consumer buys an insurance policy from an intermediary or insurer on the insurer's standard terms, there are a number of avenues that might be pursued in law, in the event that the consumer has suffered detriment as a result of the sales process. The various heads of claim that might be considered in such cases include negligent advice, breaches of obligation, misrepresentation, mistake, non-disclosure or a failure of contract formation.

The law provides slightly different remedies for a successful claimant in these different heads of claim. Some give rise to a right for the insurance to be regarded as cancelled from the start (for instance, where an insurer or its agent has failed to disclose significant features of the policy); others to a right to compensatory damages. If it is right to treat the insurance as cancelled from the start, the premium is refundable, but claims cannot be paid. Compensatory damages for unsuitable advice or other heads of damage may amount to the cost of taking out the policy – which arrives at the same general result but by a different route.

Taking account of these considerations, my normal approach is to try to put the customer back into the position he or she would have been in, but for the failure on the part of the firm. Mr and Mrs B would in my view not have taken the PPI policy if they had received a satisfactory recommendation and if the firm had given appropriate information.

Accordingly, in the circumstances of this case, I consider that the appropriate approach to fair compensation is to require the firm to compensate Mr and Mrs B by putting them (so far as is now practicable) in the position they would have been in, had they *not* taken out the PPI policy. This follows the general approach proposed by our adjudicator in her assessment of the case.

So, subject to Mr and Mrs B's agreement to the cancellation of the PPI policy and to the re-configuration of the loan, the firm should:

A. re-arrange the loan to Mr and Mrs B by writing off all amounts that remain outstanding in relation to the borrowing for the PPI premium, including any interest and charges, so that in future the number and level of outstanding repayments against the loan (and any charges and fees) are the same as would now have applied – had Mr and Mrs B taken the original loan sum (£95,000) *without* the PPI cover (with the firm waiving, for this purpose, any charges or fees that would normally apply to a change in the loan);

B. calculate the amount Mr and Mrs B have paid to the firm from time to time, up to the time of settlement in relation to the additional borrowing for the PPI premium (including interest charged), *less* any premium refund actually paid to Mr and Mrs B on cancellation of the policy;

C. to the sums calculated at (B) the firm should add interest from the points Mr and Mrs B made the payments to the firm to the point the firm settles this award in full, that interest should be calculated at a rate of 8% simple *per annum*.

The calculations of redress here are not straightforward. I would consider any necessary application from either party concerning the precise details of the calculations to be undertaken. So as to assist Mr and Mrs B, the firm should set out clearly an account of how it has made the calculations set out above – and provide a statement of the new instalments to be paid on the loan and the amount outstanding. It should pay the duly calculated amount to Mr and Mrs B and make the required changes to the loan without delay.

decision

For the reasons set out above, I determine this complaint in favour of Mr and Mrs B. I require the firm to pay Mr and Mrs B fair compensation in accordance with the calculation of redress I set out above and to make the required changes to the loan without delay. I make no further award against the firm.

Tony Boorman
ombudsman