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In his eleventh consumer credit column, Richard considers how the payment protection insurance (PPI) industry has been "killed off".

Richard Mawrey QC, Henderson Chambers

THE BABY AND THE BATHWATER

When I was a lad, an agèd relative used, when in his cups, to sing an old music hall song. It had to be sung in an 'eartrending tone and a strong cockney accent which I shall not attempt to reproduce in print (it never works, see *Dickens passim*). Entitled "*A Mother's Lament*", the refrain ran:

(*Solo*) Your baby has gone down the plughole.

Your baby has gone down the plug.

The poor little thing was so skinny and thin,

He should have been washed in a jug, (*tutti*) in a jug.

This moving ditty always comes to mind when contemplating Government measures designed to protect consumers. The almost invariable custom on these occasions is to throw the baby out with the bathwater. To change the metaphor, as I pointed out in an earlier column, the consumerist response to mice in your kitchen is to dynamite the house to rubble (see *Article, Richard Mawrey QC's consumer credit column: December 2011*). It cures the mouse problem but …

And so, a dirge will I sing for Payment Protection Insurance – the dreaded PPI. To all intents and purposes, PPI has been outlawed since 6 April 2011. The banks and financial institutions marketing PPI have been treated (retrospectively *bien sûr*) as fraudsters lucky not to be in the dock at the Old Bailey, savagely fined by the FSA, and obliged to pay literally billions of pounds by way of "compensation" to customers who were allegedly "mis-sold" PPI. They have received no sympathy from the courts. Industry challenges were contemptuously thrown out in both *Barclays Bank plc and others v Competition Commission [2009] CAT 27* and in *R (on the application of the BBA) v Financial Services Authority [2011] EWHC (Admin) 999*. So, as we helplessly watch the baby's pathetic cadaver being borne remorselessly away on the tide of effluent to the Northern Outfall Works at Beckton, we might ask: how? – or indeed: why?

When the PPI "scandal" broke (which, being interpreted, means when the consumerists noticed that it existed), it was treated as if it was an entirely new concept – or, to quote the tabloids, a new "scam". Once more, those evil men in their capitalist lairs (think caricatures by George Grosz) had devised a fiendish scheme to defraud the Little Man (caricatures by Sidney Strube) of his hard-earned. In reality, however, this kind of insurance had been around for a long time and, back in the fifties and sixties, was discussed in detail by legal writers such as Prof Roy Goode (now, of course, Sir Roy Goode QC). In those days it was often known as "ASU Insurance" standing for "accident, sickness and unemployment".

By the early seventies, PPI was a sufficiently well-established institution for specific provision to be made for it in both the Consumer Credit Act 1974 (CCA) itself and in the Consumer Credit (Total Charge for Credit) Regulations 1980 (*SI 1980/51*). There were elaborate rules for when such a policy was or was not a "linked transaction" under the CCA section 19, whether the financing of the policy created a multiple agreement under section 18 and when the premium did or did not form part of the total charge for credit. We need not concern ourselves, however, with these arcana for aficionados. The basic point is that, back then, nobody in the consumer world, and certainly not the Crowther Commission whose report was the precursor of the CCA, considered that PPI was a wicked exploitation of the debtor, to be stamped on like a cockroach.

Indeed, nobody seems to have considered PPI to be a blot on the escutcheon of UK consumer law for (at least) the thirty years following the passing of the CCA. Furthermore, even those Ayatollahs of consumerism, the good bureaucrats of Brussels, did not see the need to proscribe it. The EU Consumer Credit Directive (*2008/48/EEC*) (CCD) makes special provision for such insurance and legislates for its treatment in such areas as computing the charge for credit.

This is not really surprising. Credit is, by its very nature, something taken out by those who cannot afford to pay cash. Equally the payment of interest and the repayment of capital will be spread over a period of time. Any prudent debtor and, indeed, any prudent creditor will try to ensure that the payment of capital and interest is structured in a way that will be affordable for the debtor. Nobody deliberately sets up a credit agreement to fail. But, in doing this, both debtor and creditor have to make assumptions about the future, the principal assumption being, of course, the assumption that the debtor will remain in a position to service the credit. Hence the need to protect both parties against the contingency of the debtor ceasing to be able to afford to pay. Accident, sickness and unemployment are the events likely to bring this about. The key is unemployment: many people are employed on terms whereby they will receive their pay if sick or injured in an accident but unemployment can be (financially) a killer. This is particularly the case when the country is in recession and unemployment figures are increasing. (Remind me – what is the current position? It is? Well! Well! Well!).

PPI was available on the general insurance market but it was not easy to find and most intending debtors would never have had the capacity or the inclination to go looking for it. In real life, therefore, PPI was always offered by the creditor, as intermediary for the insurer. If PPI was compulsory, then the creditor would choose and impose its own insurer. Even if it was voluntary, however, the creditor would almost invariably have an insurer with whom it had links and whose products would be the only ones offered to the debtor. The customer would be sold the insurance at the same time as the credit product ("point-of-sale" marketing of insurance) and would neither ask nor be told of any other PPI product that might be available. In almost all cases (at least in recent years) the policy would be a single-premium policy and, as often as not, the cost would be added to the existing credit. As with all insurance intermediaries, the creditor would receive a commission from the insurer.

At this point, things get quite interesting. Most lawyers, applying normal rules relating to intermediaries and agents, would have thought that there might be an obligation on the creditor to disclose to the debtor that it was going to receive a commission on the insurance and possibly, if the amount was unusually high, its amount. The FSA, however, thought about the matter long and hard when compiling its then Insurance Conduct of Business rules (ICOB) as to whether there should be a duty on the insurance agent to disclose his commission and came to the conclusion that there should not. In *Harrison v Black Horse Ltd [2011] EWCA Civ 1128*, the debtors' claim for unfair relationship under CCA sections 140A to 140C was based on non-disclosure by the creditor of the (admittedly very large) commission payable to the creditor by the insurer. The claim failed because the creditor was found to have fulfilled its regulatory obligations under ICOB and the court felt it could not impose a different (and more onerous) obligation than that laid down by the appropriate regulator.

So the FSA's view was that commission was a matter between the creditor and the insurer and the debtor could legitimately be kept in the dark. So far so good.

What went wrong was that creditors became greedy. The true cost of PPI was grossly inflated so that the premium payable by the debtor was many times the cost to the insurer, and the balance was the creditor's commission. In *Harrison* the commission was 87% of the premium charged to the customer and that was said to be nowhere near the maximum. In essence, the creditors were buying the insurance cheap from the insurer and selling it dear to the customer.

So – the consumerists nagged the OFT and the OFT made a crafty sideways pass to the Competition Commission. Now you might have thought that the poor beleaguered credit industry, already regulated (an unkind person would say "over-regulated") by two regulators, the OFT and the FSA, did not need a third. The industry must have felt a bit like Britain in December 1941. Fighting for its existence against Germany and Italy, it is then the object of an unprovoked attack by Japan. The Competition Commission reported in January 2009 that (surprise! surprise!) the selling of PPI was not competitive. The FSA got in on the act and hurriedly changed its insurance rules, replacing ICOB with the Insurance Conduct of Business Sourcebook (ICOBS). As a result of diktats by the FSA and the Competition Commission, PPI was, in real terms, killed off. No more single-premium policies, no point-of-sale marketing (or indeed for seven days after sale) and so forth.

Insurance mis-selling? Well, any consumerist will tell you that it is received wisdom that all financial products are invariably mis-sold. Particularly PPI. There were lots of disgruntled people out there who had bought PPI and you know what? They hadn't got sick, they hadn't fallen under a bus and they had kept their jobs. Their premium must, therefore, have been a complete waste of money. Ergo, the insurance was mis-sold. I rest me case, m'lud.

So the banks were caned – again. PPI, though theoretically available, is no longer considered as a viable option by either creditor or debtor. And when the debtor gets sick or, as is happening all too often today, is handed the black bin-liner and the P45, he defaults. If his agreement is a hire-purchase agreement or is secured on his home, back goes the car or he and his family are turfed out of their home. There is no insurance. Tough. The creditors have a lot more bad debts. Their risks have increased and they may not choose to take those increased risks. The cost of credit will go up. Everybody loses – the debtor (who may lose his home), the creditor (which loses its security) and the insurer (which loses business). But at least, one hopes, the consumerists are happy.

And the PPI industry has been killed off, at a stroke, not by Government and certainly not by Parliament, but by the ukase of unelected regulators over whom the courts themselves have pitifully little control. The abuses, both real and perceived, could easily have been rectified with the baby still in the bath, but out went the bathwater and out went the baby.

All together, lads –

Your baby is now with the angels

He won't have to worry no more,

Your baby has gone down the plughole,

Not lost but gone before.