

The effectiveness of mortgage payment 'safety-nets'

Current Government policy expects mortgage borrowers to protect themselves from loss of income following unemployment, accident or sickness through private insurance and the state safety-net for mortgagors has been cut substantially. Research by Elaine Kempson, Janet Ford and Deborah Quilgars has evaluated the effectiveness of both MPPI and the diminished state provision (ISMI) for those on Income Support (now Job Seeker's Allowance). They found that:

f In 1997, roughly 30 per cent of MPPI claims were rejected. Common reasons for rejection included mortgagors being sacked or leaving work voluntarily, the ending of temporary or fixed-term contracts and pre-existing medical conditions. Challenges to rejection decisions were rarely successful.

f Most successful MPPI claimants avoided arrears, but around 1 in 5 did not. Many mortgagors whose claims were rejected developed arrears. Arrears resulted from the inability to pay the mortgage during the 'wait' period before MPPI paid out, shortfalls in the payments received or the initial rejection of an eventually successful claim. Arrears were least likely where a second person in the household worked.

f MPPI was most effective where mortgagors had additional resources (savings and/or a second salary) and were unemployed for a relatively short period of time.

f Low-income mortgagors were particularly likely to develop arrears. They were less likely to claim MPPI successfully and found it harder to afford in the first place. If reliant on ISMI they had few resources with which to cover the 'wait' period and the shortfall in payments.

f Mortgagors often found the transition from MPPI to ISMI difficult. Almost half had a period when neither safety net paid out and administrative and communication problems hampered smooth transfers.

f Two-fifths of ISMI claimants developed arrears in the period before ISMI paid out. Eighty per cent had a shortfall in the payments they received, in almost half the cases due to the operation of a standard interest rate rather than the rate payable on their own mortgage. About half of all mortgagors receiving ISMI were in arrears at some point.

f Only a quarter of mortgagors claiming ISMI had ever had MPPI and less than a quarter had a live policy. A majority of those with live policies either could not claim due to inappropriate circumstances or had their claim rejected.

Background

For a number of reasons, a growing number of homeowners may be unable to keep up mortgage payments without recourse to an adequate safety net. In particular, the extension of home-ownership down the socio-economic scale has drawn in those at greater risk of unemployment; in addition, less secure employment and increased levels of relationship breakdown may make people more vulnerable to arrears.

Policy changes have also restricted the state safety net for mortgagors by delaying Income Support for mortgage interest payments (ISMI) to unemployed people for up to nine months and implementing tighter eligibility criteria. These changes were linked with the expectation that more borrowers would take out private mortgage payments protection insurance (MPPI) and therefore its costs would fall. It was envisaged that MPPI would bridge the nine-month 'wait' period for ISMI. There were also expectations that lenders and insurers would work to reduce the extent to which particular groups of borrowers were excluded from MPPI and mis-selling occurred.

In 1996/7, 12 per cent of mortgagors defined themselves as paying their mortgages but 'with difficulty'. While mortgage arrears and possessions are cyclical, and currently relatively low, in December 1998 there were 360,980 mortgagors owing two or more months payments. 33,820 properties were taken into possession in 1998. Following a period of decline, these figures are starting to rise again, suggesting possessions are likely to increase further in 1999.

Previous research has examined the extent and influences on the take-up of MPPI. This study examines how effective both private MPPI and state-funded ISMI are in helping people avoid arrears and how effectively the two systems are complementing each other.

Making a claim

In 1997, approximately 75,000 MPPI claims were made from the estimated 2.5 million policies in force. In total, under one per cent of all mortgagors were attempting to meet their mortgage payments through MPPI. By contrast, 450,000 mortgagors were in receipt of ISMI, some four per cent of all mortgagors.

While MPPI and ISMI cover some similar eventualities, for example, unemployment, they also cover different situations with different qualifying criteria. For example, MPPI pay-outs do not take into account a household's financial resources, whereas ISMI is only available to those with less than £8,000 in savings. ISMI is available to lone parents following relationship breakdown while MPPI does not cover this. Table 1 identifies the main circumstances that give rise to arrears amongst mortgagors and whether each eventuality can be met under IS/JSA, ISMI and MPPI.

Claiming MPPI and ISMI was in most cases relatively straightforward. Only a minority of mortgagors experienced any difficulty, mainly due to administrative inefficiencies. However, some MPPI claimants had problems providing the insurer with the evidence required to support a claim. Where claimants had left employers on poor terms or felt they had been unfairly dismissed, it could be difficult to approach employers. Providing formal evidence on job search could also be difficult. Interviewees resented the need to repeatedly forward medical evidence, particularly as this was often costly to obtain. Those whose claims were complex or had been rejected were concerned about poor communication, the absence of a single contact and, in some instances, delays in decision-making.

Some ISMI claimants also reported administrative delays (typically associated with the verification of

Table 1: Reasons for claiming, compared with reasons for arrears

	IS/JSA Claimants n=506 %	ISMI Claimants n=330 %	Successful MPPI Claimants n=298	All mortgagors with arrears
Own redundancy	63	26	41	} 42
Partners' redundancy	4	4	6	
Own illness/injury	14	28	48	} 6
Partners' illness/injury	3	6	16	
Separation from partner	5	21	n/a	14
Self or partner becoming a carer	2	4	n/a	} 38 ¹
Death of partner	-	5	n/a	
Other	10	7	n/a	}

Percentages may add to more than 100 due to rounding and a small number of cases where there was more than one reason for the claim.

Source: Postal Survey of IS and ISM1 claimants and postal survey of MPPI claimants: Survey of English Housing (1996/97)

¹ 'Other' includes the 16% of households in arrears due to reduction in earnings and 7% of households in arrears as a result of financial over-commitment

claims) and poor communication (particularly between the Department of Social Security and their lender). They also reported finding the process of claiming demeaning.

Rejection of an MPPI claim

Information from insurers suggests that currently around three in ten claims are rejected. Qualitative information from 45 mortgagors whose MPPI claim had been rejected indicated that the majority had claimed for things specifically excluded by their policy. These were mortgagors who had been sacked or left their job voluntarily, had been on a fixed-term or temporary contract or had a pre-existing medical condition. These cases were often less straightforward than those which were accepted. Some people said they had provided the information about their circumstances at the time of being sold the policy and so believed they could claim. Others knew people in similar circumstances who had made successful claims. Some recognised that they had not read the small print adequately. Others, however, contested the definition of their circumstances, for example, suggesting that they had been unfairly dismissed rather than sacked.

Thirteen mortgagors with rejected claims were interviewed in-depth. Of these, seven had complained but in only one case had the decision been reversed. In addition, two mortgagors with accepted claims had first had them rejected. However, there is no standard appeal or adjudication procedure and interviewees expressed considerable disquiet about the complaints process.

MPPI claims and mortgage arrears

One important indicator of MPPI's success is the extent to which it helps recipients avoid mortgage arrears when ill or unemployed. However, the relationship between the outcome of a claim and the development of any arrears was complex. For example, a rejected claim did not necessarily lead to arrears; half of rejected claimants avoided arrears. This group were more likely to have one or more of: savings, another household member in work, access to an occupational pension or a second source of income such as Incapacity Benefit. An early return to work also helped minimise the likelihood of arrears, but not where people took on low-paid and/or temporary work. Lenders were often unsympathetic to mortgagors whose MPPI claim had been rejected and in a number of cases had instituted possession proceedings.

Over three-quarters of those successfully claiming MPPI avoided arrears, but close to one in five did not. Such arrears typically occurred while people were waiting for the outcome of a claim or because of payment shortfalls. As with rejected claimants, access to savings or the earnings of another household member could make the difference between falling into arrears or not. Those returning to work at a lower

income than previously earned again often found themselves in arrears. Where arrears occurred while claims were being assessed, lenders were typically sympathetic. However, delays and errors once claimants were receiving MPPI were treated less favourably.

There was also evidence that the transfer from MPPI to ISMI was not always smooth. More than half making the transition reported that it was quite or very difficult. Sometimes there was a gap in payments, and on other occasions borrowers found it difficult to obtain information.

ISMI and mortgage arrears

Earlier research indicated the extent to which the structure of ISMI gave rise to arrears, partly due to the 'wait' period before ISMI is paid and partly due to eligibility criteria meaning that less than 100 per cent mortgage interest can be paid. Forty-four per cent of the sample of ISMI borrowers interviewed for this project developed arrears during the 'wait' period, with a similar proportion only paying with difficulty. Eighty per cent of ISMI claimants reported a shortfall on their ISMI payments. A third of all ISMI borrowers were in arrears for this reason.

There were some interesting differences in the causes of arrears between pre- and post-October 1995 borrowers, as shown in Table 2.

Table 2 also shows the impact of increasing the wait period for those borrowing after October 1995 from two months to nine months. A higher percentage of these post-1995 mortgagors are in arrears before ISMI kicks in than is the case for pre-October 1995 mortgagors. Mortgagors also reported that the use of a standard interest rate to calculate mortgage interest (again introduced in October 1995) was a particularly significant contributor to arrears.

MPPI and ISMI

Theoretically, those eligible to claim ISMI in the event of unemployment or ill health are those most in need of MPPI. However, only a quarter of this group have taken out an MPPI policy. Amongst the sample of ISMI claimants, while a quarter had had MPPI at some point, only three per cent had a 'live' policy. The figure was 21 per cent for those receiving Income Support/Job Seekers' Allowance (IS/JSA), perhaps reflecting the growing recognition of the impact of the ISMI gap and more effective selling by lenders.

The effectiveness of MPPI for those eligible for IS/JSA was limited. Many were in receipt of IS/JSA for circumstances not covered by MPPI and so unable to make a claim. Forty-five per cent of pre-October 1995 mortgagors and 31 per cent of post-October 1995 mortgagors with MPPI were unable to claim for this reason. Amongst those with MPPI who could claim, more than half did so successfully, but the success rate was lower than that found amongst non-IS/JSA claimants.

**Table 2: Mortgage arrears amongst ISMI recipients
(all receiving ISMI and in arrears)**

Arrears due to	Column percentages	
	Pre-October 1995 borrowers	Post-October 1995 borrowers
Wait period only	16	25
ISMI shortfall only	23	6
Both wait and shortfall periods	37	37
Problems with the change from MPPI to ISMI	12	14
Other problems	12	20

Source: Postal survey of ISMI recipients

Percentages figures may exceed 100 due to rounding

Thus, lower-income mortgagors pay for MPPI but are less likely than other groups to be able to make a successful claim. Those in this position then face the ISMI gap, often followed by an ISMI shortfall, and the extent of arrears is therefore unsurprising. These arrears are, primarily, a product of the structure of both public and private safety-nets and not of borrower behaviour.

Attitudes to public and private safety-net provision

MPPI is typically sold rather than bought. Nevertheless, interviews with mortgagors who had recently claimed on MPPI indicated that, initially, they had viewed it positively. However, about half had more negative opinions following a claim. This included some mortgagors whose claims had been met, although those whose claims had been rejected expressed the most negative views.

Key reasons for this change of view amongst successful claimants included the experience of excessive delays, the 'wait' period before payment commenced (during which time a number had in fact returned to work) and the time limits on payments. Those whose claims were rejected felt they had wasted their money, that the product was not worthwhile, that they had done what was expected of them only to be let down by the insurers who were too unaccountable. Three-quarters of those rejected said they would not recommend MPPI to others and half of them had cancelled their policy by the time of the interview.

Amongst mortgagors claiming IS/JSA, a significant proportion were willing to consider taking out MPPI, although a sizable minority were strongly averse to the product.

Overall, there was a recognition that the private sector had a role to play, but that the strengths of the state safety net should not be undervalued.

About the study

Two national postal surveys were undertaken; one of MPPI claimants, accessed through two large MPPI insurers, and the other of IS/JSA and ISMI claimants, accessed through the Department of Social Security. Follow-up qualitative interviews were undertaken with a small number of successful and unsuccessful MPPI respondents and with IS/JSA and ISMI claimants.

How to get further information

The full report, **Unsafe safety-nets** by Elaine Kempson, Janet Ford and Deborah Quilgars, is available from Jane Allen, Centre for Housing Policy, University of York, Heslington, York YO1 5DD, Tel: 01904 433691, Fax: 01904 432318, e-mail: ja9@york.ac.uk (ISBN 1 874797 88 9, price £10 plus £1 p&p).