COMPETITION COMMISSION

Payment protection insurance market investigation: remittal of the point-of-sale prohibition remedy by the Competition Appeal Tribunal

Final report

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Payment protection insurance market investigation: remittal of the point-of-sale prohibition remedy by the Competition Appeal Tribunal

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Summary

1. On 7 February 2007, the Office of Fair Trading (OFT) referred the supply of all payment protection insurance (PPI) (except store card PPI) to non-business customers in the UK to the Competition Commission (CC) for investigation under section 131 of the Enterprise Act 2002 (the Act). In our report published on 29 January 2009 (the 2009 report), the CC found an adverse effect on competition (AEC) in markets for PPI and decided that a package of remedies (the remedy package), including a prohibition on selling PPI at the same time as credit, would form as comprehensive a solution as is reasonable and practicable to the AEC and detrimental effects on customers.

2. Barclays Bank PLC (Barclays) challenged the lawfulness of the decision to impose the remedy package. The Competition Appeal Tribunal (the Tribunal) in its judgment published on 16 October 2009 (the judgment) upheld Barclays' appeal in part. It found that the CC had failed to take into account the loss of convenience to consumers which would flow from the imposition of a prohibition on selling PPI at the point of sale of credit—a point-of-sale prohibition (POSP)—in assessing whether it was proportionate to include it in the proposed remedy package. The CC's decision to include the POSP in its remedy package was quashed and remitted to the CC for reconsideration. However, the AEC finding in the 2009 report was upheld.

3. In addition to reassessing the inclusion of the POSP in the remedy package, the Tribunal also directed us to address the following other factors during the remittal:

- the one-off and ongoing costs of implementation of the remedies;
- marketing costs; and
- an elasticity of demand of the type derived from an assumed price change by all distributors in the relevant market, rather than of a type appropriate when considering a price change implemented by a single distributor within a competitive market which included other distributors.

4. The Tribunal also said that during the remittal:

- we should address the question of the timescale over which the remedy package would take effect; and
- we may wish to bear in mind a question raised in the appeal, as to how the remedies would be effective for PPI sold with retail credit accounts (retail PPI), where the premium paid tracks the outstanding balance, when we found that competition by stand-alone providers was adversely affected by their inability to know the level of credit being extended by the retailer, adversely affecting the suitability of their products as alternatives for retail PPI customers to buy.

5. Whilst the Tribunal did not uphold Barclays' application in relation to the AEC finding, in light of the changed market conditions seen in the second half of 2008 and in 2009, we considered during the remittal the impact of developments in PPI markets. We concluded that none of the market developments caused us to amend our remedy package, including the POSP, as it was set out in paragraphs 10.567 to 10.572 of the 2009 report.

6. We looked at whether there would be a loss of convenience for consumers if we introduced a POSP. We looked at the evidence from experiments conducted by the

parties to the investigation, parties' internal estimates and surveys (run for parties and by Accent for us) which indicated that there would be a loss of convenience for some customers as a result of the introduction of the POSP. However, we concluded that the parties had overstated the loss of convenience that would result from the introduction of a POSP even before taking account of the benefits of the remedy package. This was because the evidence provided by the parties from the experiments and other evidence did not isolate the loss of convenience from other factors which might cause a fall in take-up. The experiments conducted by the parties also all suffered in varying degrees from problems of design, implementation and/or timing which meant that we could not rely on them to estimate the impact of the loss of convenience from introducing a POSP.

7. Evidence from our customer research indicates that some consumers (around 50 to 60 per cent, depending on the product) will experience a loss of convenience; other consumers (around 30 to 36 per cent, depending on the product) prefer the idea of having a gap between purchases of credit and PPI and would experience a positive benefit from the introduction of a POSP. Our modelling, using inputs from the Accent survey and other evidence, suggests that, without the benefits of competition which we expect to result from the remedy package, the introduction of a POSP would result in a drop in take-up rates of around 20 per cent for unsecured personal loan PPI (PLPPI), and of less than 5 per cent for first-charge mortgage PPI (MPPI).

8. In terms of the cost of the loss of convenience, the Accent survey found for PLPPI that the value of taking out PPI at the credit point of sale was £9.00 per month when compared with calling back after 24 hours and £7.30 per month when compared with being called after seven days. The mean monthly PLPPI premium was £30.50 per month. Those MPPI customers who preferred to buy PPI at the credit point of sale did not attach a statistically significant value to this preference. For those customers who expressed a preference for buying PPI either 24 hours or seven days after the credit point of sale, PLPPI customers expressed a willingness to pay £25.20 a month more to buy it seven days after the credit sale, and £19 per month more to buy it 24 hours after the credit sale. For MPPI customers, the equivalent figures were £30 and £18.70 per month.

9. We revisited our model of the effects of intervention to take account of the issues the Tribunal asked us to include in it, including loss of convenience. Using reasonable, and in some cases particularly conservative, assumptions for our base case, we found that the reduction in the price of PPI with the remedies in place is larger than the cost of the loss of convenience. The increase in sales as a result of competition outweighs the reduction in sales of PPI due to the loss of convenience and to the waterbed effect. We therefore found that the static benefits of intervention through introducing the remedy package including a POSP more than outweighed the costs of the loss of convenience and implementation, and any adverse effects associated with the loss of a relevant customer benefit of lower credit prices. This was without taking any account of the dynamic benefits we would also expect to accrue from implementation of the remedy package.

10. We also conducted tests to check the sensitivity of our results to various parameters, including the magnitude of the willingness to pay values calculated from the Accent survey, which in our view were higher than we might have expected both for delay and for simultaneous purchase. Under some assumptions, the model predicts that the remedy package could have an overall welfare detriment. However, we were confident that these scenarios were unlikely because the assumptions required to generate an overall consumer welfare detriment were a long way from our base case. This included reasonable (and in some cases conservative) assumptions, and we needed only partially to relax one of our conservative assumptions, that

customers will not search for PPI products—or otherwise anticipate the cost of PPI—prior to making decisions on credit with the remedy package in place, in order for the model to predict that consumer welfare would increase in those scenarios which were the least unlikely to occur.

11. We looked at parties' plans in light of our investigation, to reach a view on whether parties would continue to sell PPI with a POSP in place. We concluded that most large distributors reacted to the possibility of a POSP being introduced by developing products they could sell with a POSP in place. Those products were a mix of traditional PPI and, largely, short-term income protection (short-term IP) products. The work conducted, and the views on market opportunities, show that nearly all the main parties to our investigation have actively considered how they could sell PPI products with a POSP in place. We considered this evidence carefully, and we concluded that we expected those main parties to stay in the market, offering the products they have been developing to their credit customers, if a POSP were put in place. Whilst Lloyds Banking Group plc (LBG) has stopped selling PPI for the time being, we concluded that LBG is likely to re-enter the market once the remedy package is in place.

12. In terms of stand-alone provision, the evidence suggested to us that, with the remedy package in force, we would expect some of the traditional stand-alone providers to remain in the market (with underwriters supporting them), although we noted that there have been some recent exits as well as some recent new entries. There would, however, be, in our view, a key development: large PPI distributors would enter the stand-alone market. For customers this would mean that suppliers which have been providing most PPI policies will now be making stand-alone offerings available, increasing choice and increasing the number of household names offering them stand-alone policies. This gave us added confidence that, with the remedy package in place, there would be competition between PPI providers.

13. We considered whether the remedy package including a POSP would be an effective and proportionate package for each of the five major PPI products. We looked at four questions: whether the remedy package would be effective; whether the remedy package was no more onerous than needed to achieve the aim of comprehensively remedying the AEC; whether the remedy package was the least onerous if there were a choice; and whether the remedy package produced adverse effects which were disproportionate to its aim.

14. For PLPPI, MPPI, credit card PPI (CCPPI) and second-charge mortgage PPI (SMPPI) we concluded that the package would be substantially effective. For retail PPI, new evidence on customers' propensity to search led us to consider modifying our remedy package.

15. We concluded that for PLPPI, MPPI, CCPPI and SMPPI the remedy package was no more onerous than needed to achieve the aim of remedying the AEC.

16. We considered the time frame over which the remedy package would take effect for these products. We expected that the remedy package would have a substantial and immediate effect on competition for new sales from the date on which all elements of the remedy package come into force and that competition for new sales was likely to develop and grow in the years following this date. We also expect the remedy package to have a substantial effect on competition for existing PPI policies within two to three years of all elements of the remedy package coming into force. We acknowledged that some dynamic benefits may take longer to realize, particularly restoring the reputational damage caused by years of high prices and sales quality issues. However, we would expect some substantial dynamic benefits to materialize

within the first five years of all elements of the remedy package coming into force. Overall, we expected the remedy package to be substantially effective within two to three years of all elements of the remedy package coming into force.

17. We considered whether any alternative remedy packages put to us, which did not include a POSP, would be substantially effective. We looked at imposing only transparency remedies, having a clear break in the sales process instead of imposing a POSP, requiring customers to opt in to their policies on an annual basis instead of a POSP, and a menu regulation approach. We concluded that none of these would form effective remedy packages. We therefore concluded that for PLPPI, MPPI, CCPPI and SMPPI the remedy package including the POSP was the least onerous package to address the AEC.

18. In terms of whether the remedy package produced adverse effects which were disproportionate to its aim, we looked at qualitative and quantitative evidence and concluded that for PLPPI, MPPI, CCPPI and SMPPI the benefits of putting in place a remedy package including a POSP outweighed the loss of the relevant customer benefit of lower credit prices and the loss of convenience that some consumers may experience.

19. We concluded that in order to achieve as comprehensive a solution to the AEC that we had identified as was reasonable and practicable, the POSP was a necessary part of the remedy package for PLPPI, MPPI, CCPPI and SMPPI. Accordingly, we concluded that it was necessary for us to put in place a remedy package, substantially in the form set out in the 2009 report in relation to those types of PPI.

20. For retail PPI we decided not to impose a POSP as part of the remedy package. New evidence about customer behaviour meant that we could not be confident that such a remedy package would be substantially effective for retail PPI. In the light of this new evidence and taking into account its likely costs we concluded that introducing a POSP was unlikely to generate a sufficient increase in competition to justify its inclusion in the remedy package for retail PPI. We decided instead to impose a remedy package which would represent a proportionate approach to mitigating the AEC and resulting consumer detriment that we found in retail PPI markets. This remedy package includes a requirement to offer PPI separately from merchandise cover if a bundled product is offered, and a suite of remedies aimed at improving transparency and flow of information to consumers.

Decision

1. The remittal to the CC

1.1 On 7 February 2007, the OFT referred the supply of all PPI (except store card PPI) to non-business customers in the UK to the CC for investigation under section 131 of the Act. In our report published on 29 January 2009, the CC found an adverse effect on competition in markets for PPI and decided that a package of remedies, including a prohibition on selling PPI at the credit point of sale, would form as comprehensive a solution as is reasonable and practicable to the AEC and detrimental effects on customers.

1.2 On 30 March 2009, Barclays filed a notice of application with the Tribunal challenging the following aspects of the 2009 report: the decision to introduce a prohibition on distributors selling PPI at the credit point of sale; the findings in relation to the relevant market; and the findings in relation to the factors affecting the nature and extent of competition in the supply of (non-retail) PPI. LBG and Shop Direct Group Financial Services (SDGFS, for matters related to retail PPI) intervened in support of Barclays; the Financial Services Authority (FSA) intervened in support of the CC.

1.3 The Tribunal, in its judgment published on 16 October 2009,[1] upheld Barclays' appeal in part.[2] It found that the CC had failed to take into account the loss of convenience to consumers which would flow from the imposition of a POSP in assessing whether it was proportionate to include it in its proposed remedy package. This failure meant that the CC's decision to include the POSP in our remedy package should be quashed and remitted to the CC for reconsideration.

1.4 In addition to reassessing the inclusion of the POSP in light of its ruling on the loss of convenience, the Tribunal directed us to address the following other factors:

- the one-off and ongoing costs of implementation of the remedies;
- marketing costs; and
- an elasticity of demand of the type derived from an assumed price change by all distributors in the relevant market, rather than of a type appropriate when considering a price change implemented by a single distributor within a competitive market which included other distributors.

1.5 In addition, the Tribunal said that during the remittal:

- we should address explicitly the question of the timescale over which the remedy package would take effect; and
- we may wish to bear in mind a question raised during the appeal, as to how the remedies would be effective for retail PPI, where the premium paid tracked the outstanding balance, when we found that competition by stand-alone providers was adversely affected by their inability to know the level of credit being extended by the retailer, adversely affecting the suitability of their products as alternatives for retail PPI customers to buy.

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[1] www.catribunal.org.uk/238-3732/1109-6-8-09-Barclays-Bank-PLC.html.
[2] Paragraph 180 of the judgment.

1.6 On 26 November 2009, the Tribunal made an order quashing the CC's decision to impose the POSP as part of our remedy package, and remitted that part of our decision back to us for reconsideration in accordance with the principles set out in the Tribunal's judgment. The Tribunal did not set a deadline for the completion of the remittal. The Tribunal stated explicitly in its judgment of 16 October 2009 that this decision did not mean that the CC could not by that process lawfully decide to include the POSP in its remedy package as the result of its reconsideration.[3]

1.7 We published our general approach to reconsidering the POSP as part of the remedy package on our website for consultation on 11 December 2009 ('the overall consultation'),[4] our modelling approach for consultation on 4 March 2010 ('the modelling consultation'),[5] our provisional decision on 14 May 2010 and our provisional decision on retail PPI remedies on 29 July 2010.[6] We took into account the responses to these documents, as well as information gathered during our PPI market investigation and this remittal, in reaching our decision.

1.8 The Act provides little guidance on our obligations in the context of a remittal, in particular where only part of the CC's report has been quashed. In the context of a partial remittal the CC considers that it does not have a completely unfettered ability to take a new decision on those matters that were not quashed.[7] Our starting point is that we are bound by our previous findings where these have not been challenged, or where they have been unsuccessfully challenged. Accordingly, we took the view that because the Tribunal did not quash our decision on the AEC as set out in the 2009 report, that decision stands.

1.9 This is, however, subject to the constraints of public law, and in particular the obligation to take into account all relevant circumstances.

1.10 We believe that we should take into account any material change of circumstances since the publication of our 2009 report in reaching a new decision on remedies. In this context, we believe that the change of circumstance must not only be material in its nature, but also should be relevant to the decisions that we are required to take whether to include the POSP in our remedy package.[8] Accordingly, we have had regard to all relevant considerations, including relevant changes in the market, and have considered the extent to which those changes impact on our view of the competition problems that the remedy package is required to remedy, mitigate or prevent or on the scale of the resultant customer detriment that we are seeking to eliminate through our remedy package.

[3] Paragraph 181 of the judgment.
[4] *The Competition Commission's approach to reconsidering the point-of-sale prohibition as part of its remedies package*, paragraphs 11 & 12.
[5] www.competition-commission.org.uk/inquiries/ref2010/ppi_remittal/pdf/consultation_document%20on_the_model.pdf.
[6] www.competition-commission.org.uk/inquiries/ref2010/ppi_remittal/index.htm.
[7] Once a report is prepared and published pursuant to section 136 of the Act, the CC does not have the power, unless that report or part of it is quashed by the Tribunal, to revisit the decisions on the questions set out in section 134 which are contained within that report. Under section 138(3), a decision by the CC as to the action it should take to remedy the AEC and resultant detriment through its undertaking or order-making powers shall be consistent with its decisions as included in its report, unless there has been a material change of circumstance since the preparation of the report or the CC otherwise has a special reason for deciding differently. This reflects the CC's duty of consistency between its findings, as set out in its report, and the action that it takes as a result of those findings.
[8] We consider that the fact that this is consistent with the circumstances in which the CC is able to depart from the findings in its report when implementing its remedies decisions pursuant to section 138(3) supports our view that this is the appropriate approach for the CC to take in this case.

2. Description of the AEC and the remedy package

The AEC

2.1 Section 9 of the 2009 report set out our findings on the features or combination of features of relevant markets which prevent, restrict or distort competition in the markets for the provision of PPI (except store card PPI) to non-business customers in the UK such that there is an AEC.

2.2 In paragraph 9.2 of the 2009 report, we concluded that the following features of relevant markets, either alone or in combination, prevent, restrict or distort competition in the supply of PPI to non-business customers in the UK:

(a) Distributors and intermediaries (which we refer to collectively in this report as credit arrangers) fail actively to seek to win customers from their rivals by using the price or quality of their PPI policies as a competitive variable.

(b) Consumers who want to compare PPI policies (including PPI combined with credit), stand-alone PPI or short-term income protection (short-term IP) insurance policies are hindered in doing so. Product complexity (the variations in pricing structures (in particular, in relation to single-premium policies) and in terms and conditions, the way information on PPI is presented to customers); the perception that taking PPI would increase their chances of being given credit; the bundling of PPI with credit; and the limited scale of stand-alone provision act as barriers to search for all types of PPI policies. The bundling of retail PPI with credit accounts and with merchandise cover (also known as purchase protection insurance) acts as a barrier to search for retail PPI. In addition, the time taken to obtain accurate price information is a barrier in relation to the provision of PLPPI, MPPI and SMPPI. These barriers to search impede the ability of consumers to make comparisons, and therefore effective choices, between PPI policies. They also, therefore, act as barriers to expansion for other PPI providers, in particular providers of stand-alone PPI.

(c) Consumers who want to switch PPI policies to alternative providers or to alternative types of insurance policies are hindered in doing so. Terms which make switching expensive (in the case of single-premium policies) act as barriers to switching for PLPPI and SMPPI policies. Terms which risk leaving consumers uninsured (for a short period of time or in case they suffer a recurrence of a condition) act as barriers to switching for all types of PPI policies. In addition, the lack of access to consumers' balance information acts as a barrier for switching for CCPPI and retail PPI and the bundling of retail PPI with merchandise cover acts as a barrier to switching for retail PPI. These barriers to switching limit consumer choice. They also therefore act as barriers to expansion for other PPI providers, in particular providers of stand-alone PPI.

(d) The sale of PPI at the point of sale by credit providers[9] and, in relation to retail PPI, continued exclusive access to customer accounts further restricts the extent to which other providers can compete effectively.

2.3 Paragraph 9.4 of the 2009 report set out our findings as to the detriments arising from these features. We concluded that the detrimental effects on consumers of these features in relation to all types of PPI (except retail PPI) were higher prices for, and less choice in, PPI policies than would be expected in a well-functioning market. We

[9]We use the term 'credit arranger' for distributors and intermediaries arranging credit in this report.

also concluded that demand for PPI was distorted, and that it was possible that there was less innovation than would be expected in a well-functioning market. For retail PPI, we concluded that the detrimental effects on consumers of these features were higher prices for retail PPI policies than would be expected in a well-functioning market. We also concluded that it was possible that there was less innovation in relation to retail PPI than would be expected in a well-functioning market.

The remedies

2.4 In accordance with our duty under section 134(4) of the Act, we considered whether action should be taken to remedy the AEC. In our 2009 report, we proposed that the following package of remedies would form as comprehensive a solution as is reasonable and practicable to the AEC and detrimental effects on customers resulting from the AEC that we had identified:

(a) a prohibition on selling PPI at the credit point of sale and within a fixed time period of the credit sale ('the POSP') (paragraphs 10.34 to 10.38 and 10.80 to 10.156 of the 2009 report);

(b) an obligation to provide a personal PPI quote ('the personal PPI quote') (paragraphs 10.157 to 10.181 of the 2009 report);

(c) an obligation to provide information about the cost of PPI and 'key messages' in PPI marketing material ('information provision in marketing material') (paragraphs 10.182 to 10.222 of the 2009 report);

(d) an obligation to provide information to the OFT and the FSA[10] for monitoring and publication; and an obligation to provide information about claims ratios to any party on request ('provision of information to third parties') (paragraphs 10.223 to 10.242 of the 2009 report);

(e) a recommendation to the FSA that it uses the information provided to it under this obligation to populate its PPI price comparison tables;[11]

(f) an obligation to offer retail PPI separately from merchandise cover where both are offered together as a bundled product ('unbundling retail PPI from merchandise cover') (paragraphs 10.278 to 10.301 of the 2009 report);

(g) a prohibition on the selling of single-premium PPI policies and on charges which have a similar economic effect ('single-premium prohibition') (paragraphs 10.243 to 10.277 of the 2009 report); and

(h) an obligation to provide an annual statement of PPI cost and a reminder of the consumer's right to cancel ('annual statement') (paragraphs 10.302 to 10.332 of the 2009 report).

2.5 Details of these remedies were set out in Figures 10.1 to 10.7 of the 2009 report and are summarized in paragraphs 10.567 to 10.569 of that report.

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[10]Since the 2009 report, responsibility for operating the moneymadeclear website and the comparative tables has passed from the FSA to the Consumer Financial Education Body (CFEB).
[11]See previous footnote.

3. Our approach to reconsideration of the POSP

3.1 In this section, we set out first how we approach the reconsideration of the POSP, setting out our initial proposal for this, parties' views on this and our final decision on how we should approach this issue. Secondly, in paragraph 3.16, we set out briefly how the rest of this report is structured.

3.2 We set out our proposed approach to the remittal in the overall consultation document. In that document, we proposed to consider first whether the remedy package (including the POSP) would be a proportionate solution to the AEC that we found, and only if we were to conclude that the remedy package would not be a proportionate solution would we turn our attention to how we should modify the remedy package. We set out how we would approach the question of proportionality, including looking at developments in the market since the 2009 report, and how we would consider the loss of convenience and the other factors identified by the Tribunal. We recognized that we might have to reconsider whether there were any alternative remedy packages which were as effective as one including a POSP if, for example, new evidence came to light about the effectiveness of alternative remedy packages.

3.3 Several parties responded to say that this two-stage process was not the best way to proceed and that we should consider remedy packages not including a POSP in parallel.

3.4 HSBC Bank plc (HSBC) said that the correct approach would be to consider alternative packages without the POSP as part of the proportionality analysis, undertaking a comparative analysis which it said was described by the Tribunal in paragraph 120 of its judgment.

3.5 LBG expressed concern that it would leave insufficient time to consider alternatives if we concluded that a POSP was disproportionate, and created a risk that we concluded that the POSP was proportionate without having effectively examined other potentially superior options. LBG also said that, in giving preference to the POSP over other possible remedies during the original investigation, we had failed to take account of the loss in convenience, and so we should give further thought to considering the pros and cons of the POSP relative to other potential remedies. LBG put an alternative remedy package to us (see paragraphs 8.53 to 8.57) and conducted analysis of it, which it said showed that its package was more likely to have a beneficial effect on consumer welfare than the remedy package set out in the 2009 report. LBG said that our proposed approach was legally open to us, such that we were entitled to look first at whether the point-of-sale prohibition was justified in terms of proportionality and cost benefit and only then to look at other options.

3.6 The Association of British Insurers (ABI) said that our proposal was seriously flawed, and exploring alternative remedies concurrently could lead to more suitable solutions being developed, and a better outcome for consumers. It also raised concerns that our proposed approach risked there being a lack of time to consider other approaches.

3.7 SDGFS accepted the two-stage approach set out in our consultation document, but said that, as it believed the POSP could not be a proportionate remedy for retail PPI (as it said that there were no substitutes for retail PPI and therefore there were no competitors over which an advantage could be held), we should move immediately to a consideration of remedies without a POSP.

3.8 The British Bankers' Association (BBA) expressed concern that the approach could lead to our adopting a remedy which did not, in fact, represent the best outcome for consumers. It said that we might conclude that the POSP was a proportionate remedy without having considered whether other remedies were in fact superior to it; it also expressed concern that we would have insufficient time properly to consider alternative remedies.

3.9 Barclays said that we should look at the POSP remedy on an incremental basis—that is, we should look first at the impact of the remedy package without the POSP and then consider the incremental impact of adding the POSP to the remedy package.

3.10 Following our provisional decision, Barclays also said that our approach was irrational in economic terms, because the proportionality of a regulatory option must be judged, among other things, by its anticipated effects relative to other options.[12] In a hearing following the publication of the provisional decision, Barclays said that its reasoning on this matter was separate from legal arguments about the scope of what had been remitted to us by the Tribunal. By raising this economic argument, Barclays was inviting us to vary the remedy in the 2009 report and re-examine whether a further look needed to be taken at the effectiveness of other remedies in light of changes to the market since the 2009 report.

3.11 We considered these responses carefully. We noted HSBC's comment (paragraph 3.4) that a comparative exercise should be undertaken. We thought that such an exercise was only necessary to the extent that we should compare the remedy package with any other substantially effective remedy packages, or if we found that the remedy package produced adverse effects which were disproportionate to its aim.

3.12 Similarly, we took the view that LBG's comparative modelling of the opt-in remedy and the remedy package (see paragraph 3.5) was relevant only if we concluded that LBG's alternative remedy package including the opt-in remedy was also substantially effective (albeit not as effective as the remedy package), or if we found that the remedy package produced adverse effects which were disproportionate to its aim—in which case it would be appropriate for us to consider remedies that were not substantially effective but which mitigated the AEC and resultant detriment.

3.13 We did not agree with concerns raised that we would fail to identify the best remedy package for the AEC identified (see paragraphs 3.5, 3.6 and 3.8). We have given extensive and careful consideration to alternative remedy options, both during the original investigation and during this remittal. We consider in paragraphs 8.43 to 8.61 whether there are any other packages which would be substantially effective in remedying the AEC, and conclude that there are not. Our judgement therefore remains that the POSP is an essential component of any substantially effective remedy package to the AEC. In light of this assessment and our statutory duties, we do not judge that it would be appropriate to be looking to implement other, markedly less effective, remedy packages, unless we found that the remedy package produces adverse effects which are disproportionate to its aim.

3.14 We did not agree with concerns about there being insufficient time to consider alternatives should the POSP remedy package be found not to be proportionate (see paragraphs 3.5 and 3.6). We thought that it was important to concentrate efforts on a thorough investigation of the proportionality of including a POSP in the remedy package—that was what was remitted to us for reconsideration. We recognized that in taking this approach we did risk creating an extra stage in the process, that of the consideration of how to mitigate the AEC if no substantially effective remedy package

[12] Barclays response to the provisional decision, Appendix 1, paragraph 6.

could be found that was also proportionate, but on balance we thought this was a risk that was worth taking in order to be able to conduct a thorough review of the proportionality of including a POSP in the remedy package. We also thought that, overall, our approach would be a more efficient use of time, as to consider alternative less effective packages at the same time as the consideration of the remedy package would increase the length of time taken to conduct analysis, much of which might not be needed.

3.15 We did not accept Barclays' suggestion of how we should approach proportionality of the POSP (see paragraph 3.9). We noted that Barclays raised this during the appeal,[13] but the Tribunal did not find Barclays' argument that we should have adopted an incremental approach 'at all persuasive'.[14]

3.16 The rest of this report is set out as follows. First, we look at developments in the market since the 2009 report. We then look at the existence and magnitude of the loss of convenience that would be felt by consumers if the POSP were introduced. Next we look at how parties reacted to the 2009 report in terms of developing new products, with a view to considering whether parties would remain in the market if a POSP were introduced. We then revise our modelling of the impact of the remedy package, taking account of the loss of convenience and other factors the Tribunal asked us to take into account. Next we conduct a revised assessment of the effectiveness and proportionality of the remedy package for each type of PPI. Finally, as we do not find that the remedy package is substantially effective for retail PPI, we consider what package of remedies to require for retail PPI.

4. Developments in PPI markets since the 2009 report

Introduction

4.1. In paragraph 3.16, we explained that we would review developments in the PPI markets since the 2009 report as part of our reconsideration of the inclusion of the POSP in the remedy package. We therefore sought the views of the parties on relevant market developments.

4.2. In addition to responding to our request for information about market developments, the parties made submissions about the impact of those developments for our findings on the AEC, the POSP and the other elements of the remedy package.

4.3. The context in which this assessment is to be undertaken is described in paragraphs 1.8 to 1.10. Accordingly, we considered whether the developments in the market had implications for our decision to include the POSP in the remedy package, and also on our decisions on any of the other elements of the remedy package. As our AEC findings had not been quashed, we did not repeat this part of our analysis. However, we did consider whether any of the changes that had been identified in the market were sufficiently material to cause us to amend the remedy package which is set out in our 2009 report, and we also considered the impact of these changes on the scale of the customer detriment arising as a result of the AEC. More detail on market changes since the 2009 report is set out in Appendix A.

4.4. The balance of this section is structured as follows:

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[13]See www.catribunal.org.uk/files/Judg_1109_Barclays_16.10.09.pdf, paragraph 117.
[14]Ibid, paragraphs 118 & 119.

(a) We summarize each of the developments in the PPI market since the 2009 report was published (and we note that the 2009 report included data up to and including the first half of 2008; this section focuses on data from the second half of 2008 and the first 11 months of 2009. Further details can be found in Appendix A).

(b) We summarize submissions we received from the parties on those market developments.

(c) We set out our views on the implications of those market developments for our remedy package.

(d) We set out our conclusions as to whether any of the market developments constituted a material change in circumstances or a special reason pursuant to section 138(3) of the Act, such that we should amend the remedy package which is set out in our 2009 report.

The regulatory environment

4.5. In our view, there have been three primary developments in the regulatory environment. The first was the request by the FSA in February 2009 that firms cease to sell single-premium PPI on unsecured loans. The second was an agreement between the FSA, relevant trade bodies and some firms, in October 2009, that MPPI customers would be refunded approximately £60 million by June 2010. The third was the FSA's consultation and decision on new guidance and rules for the fair handling of PPI complaints.

4.6. In addition, Barclays submitted that there were a number of other regulatory developments which we should take into account, including: FSA work in relation to the PPI back book, in particular in relation to complaints; and the FSA working together with the industry to develop price comparison tables on PPI, which had been launched on 23 June 2008 (and are now operated by CFEB).

Single-premium PPI policies

4.7. The FSA wrote to Chief Executives of firms in February 2009 requesting that they cease selling single-premium PLPPI policies by 29 May 2009.[15] The request was confined to the sale of single-premium PPI with unsecured personal loans[16] and arose as a result of the FSA's continuing concerns over poor sales practices. In fact, as we noted in paragraphs 10.247 and 10.260 of the 2009 report, some large PPI distributors had ceased selling single-premium PPI policies in December 2008 and January 2009, which the FSA had acknowledged in a press notice (in which it also said that it expected other providers of single-premium PLPPI to review their positions).[17]

4.8. We received the following submissions in relation to the impact on the market of the FSA's request that firms cease selling single-premium PLPPI policies:

- Barclays[18] told us that the withdrawal of single-premium PPI had had a significant impact on the sector, by changing the structure and sales processes of most

[15] www.fsa.gov.uk/pages/Library/Communication/PR/2009/031.shtml.
[16] The request did not extend to mortgages, secured loans, credit cards or other forms of credit.
[17] www.fsa.gov.uk/pages/Library/Communication/PR/2009/031.shtml.
[18] Barclays response to provisional decision, section 2.2.

providers. It also said[19] that the withdrawal meant that it was not correct to maintain, as it said the CC had, that barriers to switching remained 'as much of a problem as at the time of the 2009 report' and that each of the barriers to search identified in the 2009 report remained 'wholly or largely in place'.

- The Royal Bank of Scotland Group (RBSG)[20] told us that because single-premium policies were no longer being sold by PLPPI providers, any part of our AEC resulting from the sale of those products must fall away, such that the barriers to searching and switching which formed part of our AEC must be diminished.

- Nationwide Building Society (Nationwide)[21] said that sales of single-premium PPI having ceased meant that a barrier to consumer search had been removed. It said that firms had worked tirelessly to accommodate their sales processes to the FSA's stipulated requirements relating to optionality, accurate price information and terms and conditions, including exclusions/ability to claim.

4.9. We noted that the barriers to searching and switching that we identified in our 2009 report were not attributable solely to single-premium policies, though it was an important barrier identified.[22] We recognize that single-premium policies have largely or fully disappeared from the market at the moment. However, we noted that the FSA request that single-premium PLPPI policies no longer be sold was a request only, and that parties which had stopped such policies in advance of the FSA's request (see paragraphs 10.247 and 10.260 of the 2009 report and paragraph 4.7 above) were not included in the FSA's request.

4.10. We noted further that the FSA request related only to PLPPI policies, and did not extend to SMPPI policies, many of which had been sold on a single-premium basis (see paragraph 10.260 of the 2009 report). Although currently there are no major suppliers of single-premium SMPPI, there is no basis upon which we could conclude that single-premium SMPPI policies will not reappear. Nor is there any basis upon which we could conclude that those providers who were recipients the FSA's request, or who voluntarily withdrew their single-premium PLPPI policies at the request of the FSA, would not sell single-premium PLPPI policies in the future.

4.11. Accordingly, whilst there are no single-premium policies currently being sold by large distributors, this is due to a request from the regulator, which is not legally binding, and also the economic crisis which has reduced the appetite of credit providers for offering secured loans.

4.12. We considered whether the lack of single-premium policies is a change of market conditions that should lead us to modify our remedies.

4.13. Single-premium PLPPI and SMPPI policies were profitable products in the past (see paragraph 4.73 of the 2009 report) and in our view, absent any action by us, there is no legal impediment to the re-emergence of single-premium policies. Given the importance of the barriers to search and switching we previously found them to represent, we consider it appropriate to prohibit them. This enables us to deal with any possible risk that they will once more become an impediment to the development and maintenance of competition between providers of PPI and short-term IP (which, as noted in paragraph 4.38, we regard as a form of PPI). Further, the prohibition included a prohibition on separate charges for administration or for the set-up or early

[19] Barclays response to provisional decision, sections 3.4 & 3.5.
[20] RBSG response to provisional decision, section 1.1.
[21] Nationwide response to the provisional decision, paragraph 1.3.
[22] See paragraph 9.2*(b)* and *(c)* of the 2009 report for a list of the barriers to search and switch that we found.

termination of a policy, which we continue to believe are important potential barriers to switching.

4.14. We also noted that there are no parties we know of which are currently selling single-premium PPI (either PLPPI or SMPPI). As such, this element of the remedy package would not impose any costs on PPI providers and in our judgement there is no question of disproportionally in prohibiting its sale.

4.15. For the reasons set out in paragraphs 4.9 to 4.14, and paragraphs 10.243 and 10.245 of the 2009 report, we concluded that, whilst single-premium policies are not currently being sold, given their importance as a barrier to search and switching identified in the 2009 report, we did not think that this amounted to a change in market conditions that should lead to a modification of the remedy package, and it continues to be appropriate to prohibit these policies. We did, however, have regard to this development when we updated our profitability analysis (see paragraphs 4.53 to 4.59).

Refunds to MPPI customers

4.16. In October 2009, the FSA reached agreement with relevant trade bodies and some firms that around £60 million would be refunded to MPPI customers by June 2010. The industry acted in response to FSA concerns over increases in premiums and reductions in the level of cover offered by existing policies. The FSA's concerns centred on the terms permitting these changes, and how adequately these terms were disclosed to customers. The industry agreed to refund increases in premiums and restore the original terms of contracts to customers who had experienced these changes in 2009, to freeze premiums for existing customers, and to make amendments to contracts to ensure that customers are made aware of the circumstances in which firms have the right to vary premiums and cover.[23]

4.17. Again, parties did not make submissions to us directly in relation to this agreement to give refunds to MPPI customers.

4.18. However, we note, as we do in paragraph 4.22, that the FSA's ongoing work is not aimed at increasing competition between providers and has not had any material impact on the level of competition between participants in the market.

4.19. Accordingly, we concluded that this development in the market did not amount to a change in market conditions that should lead us to change our decisions on any element of the remedy package set out in paragraphs 10.567 to 10.572 of the 2009 report. However, we did have regard to the impact of this development when we updated our profitability analysis (see paragraphs 4.53 to 4.59).

New FSA guidance on PPI complaints handling

4.20. The FSA began a consultation on proposed new guidance and rules for the fair handling of PPI complaints in September 2009.[24] This was prompted by concerns about the way in which PPI was sold and the fairness with which firms assessed consumer complaints about past PPI sales. In light of responses received to that consultation, the FSA has revised its proposals and has consulted again, with that consultation

[23] www.fsa.gov.uk/pages/Library/Communication/PR/2009/135.shtml.
[24] www.fsa.gov.uk/pages/Library/Policy/CP/2009/09_23.shtml.

concluding on 22 April 2010.[25] It published its decision on 10 August 2010,[26] confirming its package of measures to protect consumers in the PPI market. Firms must implement the new measures by 1 December 2010.[27] It said that the package would ensure that customers were treated more fairly when complaining about PPI and better when buying the product; it includes:

- new handbook guidance to ensure that complaints are handled properly, and redressed fairly where appropriate;
- an explanation of when and why firms should analyse their past complaints to identify if there are serious flaws in sales practices that may have affected complainants and even non-complainants; and
- an open letter setting out common sales failings to help firms identify bad practice.

4.21. Parties did not make submissions to us specifically on the impact of this FSA consultation. However, Barclays[28] said that the CC had not attempted to measure the impact of the regulatory changes brought about through the introduction of Insurance Conduct of Business (ICOB) and Insurance: New Conduct of Business Sourcebook (ICOBS), many of which would not have yet been visible at the time of the 2009 report; Nationwide[29] said that we had failed to acknowledge the significant changes that had already taken place in the PPI market, specifically in response to FSA thematic reviews and subsequent regulatory intervention, which had aided removal of a number of consumer barriers to search; and RBSG[30] said that changes in the regulatory environment since 2007 meant that certain features of the CC's AEC were likely now to be overstated.

4.22. We note that the nature of the changes is not in itself likely to address the AEC. The FSA told us that the regulatory actions it had taken were intended to address specific causes of consumer detriment in the PPI market, rather than the AEC as a whole, and in its view further measures were still necessary to fully address the AEC.

4.23. We noted also that neither the FSA's work relating to sales processes and complaints handling nor parties' responses to the FSA's thematic reviews were directly aimed at increasing competition between PPI providers, and there was no evidence of them having had any material impact on the level of competition between participants in PPI markets.

4.24. For the reasons set out in paragraphs 4.18 and 4.19, we concluded that these market developments did not amount to a change in market conditions that should lead us to change our decisions on any element of the remedy package set out in paragraphs 10.567 to 10.572 of the 2009 report.

Changes at the business and product offering levels

4.25. We noted numerous changes at both the business and product level in the PPI market since the 2009 report.

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[25] www.fsa.gov.uk/pubs/cp/cp10_06.pdf.
[26] www.fsa.gov.uk/pages/Library/Policy/Policy/2010/10_12.shtml.
[27] In October 2010 the BBA announced that it was asking for a judicial review of some FSA and FOS decisions.
[28] Barclays response to provisional decision, section 2.3.
[29] Nationwide response to provisional decision, paragraph 1.3.
[30] RBSG response to provisional decision, section 1.2.

4.26. At the business level, the changes were largely caused by the severe financial crisis and subsequent recession. In October 2008, Alliance & Leicester plc (Alliance & Leicester) was taken over by The Santander Group (Santander), which already owned Abbey National plc (Abbey). In January 2009, Lloyds TSB Group plc (Lloyds TSB) and HBOS plc (HBOS) merged to form LBG. Cattles plc (Cattles), which was one of the largest suppliers of SMPPI through its Welcome Financial Services (WFS) brand, stopped selling PPI policies in February 2009 and WFS is no longer providing personal and secured loans.

4.27. We noted that the continued negative publicity around PPI, to which we referred in the 2009 report (see paragraphs 2.25 and 10.493), may have had an impact on developments at the business level. As noted in paragraph 10.493 of the 2009 report, we thought that this negative publicity was, in part, a consequence of the high prices for PPI and hence a consequence of the AEC. While we thought that it was important that we acknowledged this continued negative publicity in our assessment of the current state of PPI markets, we did not consider that this was a new phenomenon, nor did we attempt to quantify or measure its impact. We thought it was probable that the negative publicity had been one of the factors which had contributed to the decision of some parties to withdraw from the market (see paragraph 4.31) and to the reduction in sales volumes (see paragraphs 4.44 and 4.45). Beyond these effects, which we consider below, we did not consider that the continued negative publicity around PPI constituted a significant new development since the 2009 report.

4.28. We noted that although there had been consolidations among providers and exits from the market by others since the publication of the 2009 report, we did not see any basis upon which we could conclude that those consolidations among, and exits by, providers had produced increased rivalry among the remaining providers.

4.29. Further, we did not see any indication that distributors or intermediaries have been actively seeking to win customers from their rivals. Nor did we see much evidence that distributors have been actively marketing PPI products to anyone other than their own credit customers.[31] We did note, in particular, that Barclays' Income Insurance (BII) product, which was developed following the 2009 report, has recently started to achieve monthly sales of between 5,000 and 10,000, largely to non-Barclays credit customers. We also noted that some of HSBC's LifeChoices sales are to existing customers who do not have HSBC credit. We thought that these developments, which were in our judgement at least in part due to product changes in anticipation of remedies to come, were encouraging signs of the possible future direction of PPI markets. However, the volume of Barclays and HSBC sales to non-credit customers do not, in our judgement, represent a significant change in the market at this time.

4.30. We therefore concluded that the evidence of changes at the business level did not amount to a change in market conditions that should lead us to amend any element of the remedy package set out in paragraphs 10.567 to 10.572 of the 2009 report.

4.31. At the product level, we noted many changes (set out in detail in paragraphs 3 to 19 of Appendix A). Of particular note, in July 2010 LBG, the largest distributor of PPI advised us that it intended to stop selling PPI (see paragraphs 44 to 51 of Appendix G). We discussed LBG's plans with it, and saw internal documents relating to the decision. The evidence we saw and heard was that LBG was suspending sales of PPI because it did not think its current products would be economic to sell given the changes brought about by FSA and Financial Ombudsman Service (FOS) inter-

[31]Barclays' new BII product was available to all consumers, not just to Barclays' customers; as was HSBC's LifeChoices product. [✂] and HSBC is focusing its sales of LifeChoices on its existing customer base.

vention in markets, and that significant process changes would need to be made if a POSP were introduced. It did not think it sensible to make changes to those products until it saw the outcome of this remittal, at which time it would consider its options. [✂][32] Also, with the withdrawal of single-premium PLPPI (see paragraph 4.7), some parties moved to selling regular-premium PLPPI, while some have not yet replaced their single-premium products. There were also withdrawals of CCPPI products and of stand-alone products, which occurred for a variety of reasons, none of which, at least for the large PPI providers, were that the suppliers in question considered that they could not continue in the market because of the possible impact of our remedies.[33]

4.32. We received extensive submissions from parties on the changes at the product level of the market, and the impact of those changes.

4.33. In response to the provisional decision, Barclays submitted that we had failed to review both the features and our proportionality assessment in relation to stand-alone PPI or short-term IP that were not linked to any credit product, such as those offered by a number of credit providers including Barclays.

4.34. Barclays had a new short-term IP product, BII, which was launched on its Internet channel in November 2009 and, following pilots, was rolled out across the branch network from July 2010 although it has not yet been launched in telephony.[34] BII is positioned within a suite of insurance protection products (ie alongside, for example, life and health insurance products) and offers accident and sickness (AS) and/or unemployment (U) cover and a choice of cover for either up to 12 months or up to 24 months. The consumer nominates the level of cover, and the benefit is paid directly to the consumer. Barclaycard also has a short-term IP product, called LifestylePlan (LSP). LSP was launched in the online channel in June 2010 to existing Barclaycard customers, and as of September 2010 was available online to all customers (both new and existing) and potential customers. LSP is a fixed regular-premium insurance product that offers tailored cover against various risks specified by the customer. It is not linked to the balance of the customer's credit card.

4.35. Barclays told us that 'income protection' products were solely focused on the customer's own view of their financial protection needs. The benefit amount was chosen by the customer and was typically based on their outgoings (if the customer decided they wished to base the benefit amount on these). It said that for a product to be categorized as 'short term', it must have a benefit duration of less than five years. In practice, it said that a maximum of two years was currently more common in the market.

4.36. Barclays[35] also said that we had not considered whether the POSP was an appropriate or proportionate remedy in relation to stand-alone PPI or short-term IP products that were not linked to any credit product. Barclays submitted that the development of stand-alone products and short-term IP products which were not sold at the point of sale of credit were a change in the market which we were required to consider in deciding on the POSP element of the remedy package.

4.37. As set out in Section 6 and Appendix G, while many parties had been developing products that could be targeted at the customers of their competitors, none of those

[32]Publicly, LBG said that the reason for its decision was the uncertainty around the regulation of PPI sales and processes, and that further changes in regulation would make it uneconomic to continue to offer its products in their current form.
[33]See the section beginning with paragraph 6.14 for our consideration of the product changes that we expect will be prompted by the implementation of the remedy package.
[34]See the footnote to paragraph 4.29.
[35]Barclays response to provisional decision, section 3.1.

new products had yet come to market, with the exception of Barclays' BII product (see paragraph 4.34).

4.38. We did not accept Barclays' submission that we had failed to take account of stand-alone PPI or short-term IP that are not linked to any credit product, such as those offered by a number of credit providers including Barclays. Our analysis of short-term IP products is set out in detail in Appendix 2.3 of the 2009 report, and we note paragraphs 33 and 61 of that appendix, which say:

> we regard [credit point-of-sale] sales of short-term IP as enjoying the same advantages and giving rise to the same concerns as PPI sold at the point of sale.
>
> We concluded that:
>
> - short-term IP is a form of PPI;
> - short-term IP policies sold as a result of a referral during a credit sale are effectively sales of PPI at the point of sale; and
> - these conclusions apply to LifeChoices.

4.39. We were therefore satisfied that, in reaching both our original decision in 2009 and in conducting this remittal, we took full account of short-term IP products such as BII. Barclays' views in relation to the definition of 'income protection' and 'short term' (see paragraph 4.35) were, in our opinion, in line with our own view (see, for example, paragraph 27 and Table 1 of Appendix 2.3 of the 2009 report) as to what is a short-term IP product (though we noted that Barclays did not agree that a short-term IP product is a PPI product, which we concluded in paragraph 2.14 of the 2009 report). We note that the remedy package was tailored to take account of circumstances where short-term IP is sold as a genuine stand-alone product (see Appendix N for details of the implementation of the POSP and the different formats for personal quotes and annual statements for stand-alone PPI and short-term IP products in Appendices 10.1 and 10.2 of the 2009 report).

4.40. RBSG[36] said that 2009 was a transitionary year for the market (due to, for example, the severe economic conditions and regulatory changes) and the fact that firms had not yet launched new products could not be used to inform the CC's reconsideration of firms' ability to compete for their rivals' customers. It said that it expected us to look at the fact that a number of providers were developing stand-alone products and to take this into account as a relevant feature of the market in reassessing the AEC. [✂][37]

4.41. We disagreed with RBSG's submissions that the development of new products was a material change, as we found no evidence that the products under development are in the market, and all relevant parties have emphasized that no final decision on launch has been made—[✂] (see paragraph 6.25 for our assessment of RBSG's argument that the identities of providers planning to enter the stand-alone market represented a material change in the competitive environment).

4.42. The new evidence we received did not give us a basis upon which to change our conclusion, as set out in paragraph 1 of the 2009 report, that distributors hold an effective monopoly over the sale of PPI to their own credit customers. The new prod-

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[36]RBSG response to provisional decision, section 1.4.
[37]As noted in paragraph 6.27, the plans for development of products which could be sold on a stand-alone basis gave us confidence that, with the remedy package in place, there would be competition between PPI providers.

ucts to which parties referred us are not guaranteed to come to market without the imposition of a remedy package,[38] and the incentives to offer them on the market and actively seek to make sales to customers other than the bank's credit customers is greatly reduced if the POSP is not implemented and distributors are able to retain the monopoly provision of PPI at the credit point of sale which they currently enjoy. We did not accept that in such circumstances parties would have a strong incentive to launch and actively market stand-alone products.

4.43. We therefore concluded that the evidence of changes at the product level did not amount to a did not amount to a change in market conditions that should lead us to change our decisions on any element of the remedy package set out in paragraphs 10.567 to 10.572 of the 2009 report.

Changes in market outcomes

Volume and value of PPI sales

4.44. During 2008 and 2009 there was a significant reduction in the volume of PPI policies sold. Compared with 2008, there were fewer new policies sold in 2009 across all types of PPI. The number of new PLPPI policies sold by the largest distributors was about one-fifth of the policies sold in 2006; the number of new SMPPI policies sold was 98 per cent lower than in 2006; the number of new CCPPI and MPPI policies sold was about 45 per cent lower than in 2006; and the number of retail PPI policies sold was about half the number sold in 2006.

4.45. There were three main reasons for these reductions. First, there was a reduction in the amount of credit made available, as a result of the financial crisis and subsequent recession. Second, there has been a continuation in the long-term decline in PPI penetration rates. Third, there was the withdrawal of single-premium policies from the market, not all of which were replaced with PLPPI policies, either immediately or at all.

4.46. The decline in value of PPI sales (measured in terms of gross written premium (GWP)) was even more pronounced than the reduction in volume of policies sold. In 2009, there was, overall, a negative GWP earned by the large PLPPI distributors, which was driven by five of the large distributors[39] reporting negative GWP for that period.

4.47. The drivers of the steep decline in PLPPI GWP were twofold. First, as stated in paragraph 4.45, parties stopped selling single-premium PLPPI policies and not all replaced these with regular-premium products. Consequently they sold no new policies for part of the year, and those that did received GWP on those new policies only on a monthly basis, instead of receiving, as they had previously, a multi-year premium in one lump sum. Secondly, significant amounts were paid to customers in rebates for cancelled single-premium policies; in some cases, the rebates paid outweighed the GWP earned from policies in force.

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[38]We note that the catalyst for the development of many of these products has been the possible introduction of the POSP (for example, products under development by [✄]).

[39]In the 2009 report we included the following as the large distributors: Abbey, Alliance & Leicester, Barclays, Capital One Bank Europe plc (Capital One), Cattles, HBOS, HSBC, Lloyds TSB, MBNA Europe Bank Ltd (MBNA), Nationwide, Northern Rock plc and RBSG. We also focused on the four largest providers of retail PPI (Express Gifts Ltd (Express Gifts), JD Williams & Company Limited (JD Williams), Otto UK Home Shopping Group of Companies known as Freemans Grattan Holdings (FGH) and SDGFS). For the remittal, we replaced Northern Rock with Clydesdale and Yorkshire Bank, part of the National Australia Group (CYB), and focused on only two large retail PPI distributors—JD Williams and SDGFS.

Distributor income

4.48. Overall, the income received by the largest distributors in the years 2003 to 2005 remained at approximately £2.6 billion per year, although by 2006 and 2007 it had dropped to £2.2 billion per year. In 2008, the income earned by distributors[40] fell to £1.8 billion, and to £517 million in 2009. The reduced income was partly due to lower GWP, as explained in paragraph 4.47. For PLPPI, five of the large distributors reported negative income, for largely the same reasons as there was negative GWP reported. For MPPI in particular, income was reduced due to the increase in claims on the policies (see paragraph 4.50).

4.49. Most large distributors told us that during 2007 to 2009, they did not make significant changes to the prices of any of their PPI (including short-term IP) products. We noted some price increases; the only price decreases we saw in 2009 were directed by the FSA, reversing price increases made to MPPI policies.

Claims

4.50. The evidence showed that there was an increase in the total number of claims in 2009 relative to 2006.[41] The increase in claims ratios observed over this period can be attributed both to an increase in the value of claims paid and a fall in the net premiums earned (see paragraphs 22 to 31 of Appendix A on premiums earned and paragraphs 48 and 51 of Appendix A on claims frequency). There were adjustments to some contracts between MPPI underwriters and distributors in light of actual or expected changes in MPPI claims ratios though no adjustment to contracts for any other form of PPI.

4.51. Whilst for MPPI and, to a lesser extent PLPPI, the claims ratio had increased significantly, this increase in claims was largely driven by the rise in unemployment and we expect that claims would reduce as the economy improved. We also noted that even in 2009, during the recession, the claims ratios experienced for all PPI policies save MPPI were lower than the claims ratios in 2006 for motor, liability, accident and health and property insurance (see Table 4.3 of the 2009 report). And, importantly, we noted that even in the middle of a recession, large PPI distributors were still making significant excess profits on the sale of PPI (see paragraph 4.55 and Table 4.1).

4.52. While there was an increase in claims ratios in 2009 relative to 2006, we attributed this to an increase in the value of claims paid and a fall in net premiums earned (see paragraph 4.50), rather than to a reduction in the price of PPI (see paragraph 4.49) or any change in competitive conditions (see paragraphs 4.28 and 4.29).

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[40]Distributors generate income in the form of commission and profit share, as a proportion of GWP. The amount of income as a percentage of GWP is set out in the contract between distributor and underwriter. Commission is normally a percentage of GWP and profit share is a percentage of profits once claims and underwriter expenses have been taken into account.
[41]However, the number of claims per hundred policies in 2009 was still less than in 2002 for CCPPI and at a similar level to 2002 for SMPPI.

Profitability

4.53. We looked at distributor profitability in 2008 and 2009 by the five main product types as well as overall. We took the same approach as is set out in paragraphs 4.62 to 4.72 of the 2009 report.[42]

4.54. Table 4.1 summarizes the results of our profitability analysis for 2008 and 2009 (see Appendix A, paragraphs 59 to 62, for detail).

TABLE 4.1 **Results of profitability analysis for 2008 and 2009, for each main product type, and for all types of PPI in total**

	2008		*2009*	
	Economic profits £m	*Return on equity %*	*Economic profits £m*	*Return on equity %*
PLPPI	638.2	530	3.2	13
MPPI	94.7	542	50.2	292
CCPPI	279.9	475	187.0	321
SMPPI	67.6	577	5.1	53
RCPPI	5.5	129	5.7	134
Total	1,085.8	510	251.2	126

Source: CC based on data provided by the parties.

4.55. Our updated profitability analysis shows that, for 2008, despite a drop in GWP and income, economic profits remain at just over £1 billion for all distributors and all PPI products. Return on equity remained at approximately the same levels it was in the 2009 report.

4.56. For 2009, overall economic profits declined, although return on equity remained at very high levels. We noted that, for PLPPI, economic profits were closer to zero than for PPI products overall, and the return on equity was closer to a reasonable rate of return.

4.57. We took the view that 2009 was an anomalous year, because of the impact of the recession, and, for PLPPI, a decline in GWP resulting from a combination of factors, some of which we considered were one-off in nature (ie distributors ceasing selling PLPPI policies following FSA intervention, the launch by some parties of regular-premium policies to replace single-premium policies, rebates on cancelled policies outweighing the sum of GWP received on existing and new policies), as well as the continued fall in take-up rates.

4.58. In response to our provisional decision, Barclays[43] said that it would be incorrect to consider 2009 as a 'one-off' year, with the economy still in a fragile state. It said that an assumption of growth of PPI sales to pre-recession levels appeared very optimistic, and noted that in saying that as PPI prices reduced we would expect PPI take-up to increase, we did not say to what level.

4.59. We accepted that the economy has been in a recession, but the remedy package is aimed at achieving competition for the long term and we do not expect the economy to be at 2009 levels indefinitely. In our analysis of proportionality we take account of

[42]Broadly, the approach was to analyse profitability of PPI distinct from the underlying credit product, looking at economic profit and return on equity; more specifically, our model included the following inputs: costs of £100 per policy sold; tax of 28 per cent; capital base calculated as 12 per cent of revenues; capital cost calculated as 10 per cent of capital base; and return on equity calculated as post-tax profits divided by capital base. We saw no evidence to suggest that the cost of selling a policy or capital cost had changed since the report. For 2009, we maintained the capital base at 2008 levels (ie by calculating capital base as 12 per cent of 2008 revenues) due to the large drop in distributor income between 2008 and 2009.
[43]Barclays response to provisional decision, section 2.2.

both years of high sales and years of low sales, by averaging excess profits over the five years to 2009; thus taking into account years of high PPI sales and low PPI sales.

Conclusions on changes in market outcomes

4.60. We noted that 2008 and 2009 had been years of particularly low levels of credit sales, which had been a significant driver of lower PPI sales. Whilst sales of credit and PPI had been depressed, we found (as set out in Appendix A) that distributors continued to earn the same levels of commission as a percentage of GWP in all PPI products save MPPI, where worsening claims experience had led to a higher proportion of GWP being paid out in claims. Whilst the number of policies sold had decreased significantly, the stability in the contractual rates of commission payable to distributors meant that PPI distributors continued to earn very significant amounts of commission for each policy sold—especially so for CCPPI, PLPPI, SMPPI and retail PPI, but also for MPPI despite the reduction in GWP.

4.61. Whilst sales of credit were low, in 2009 it was generally held that sales would begin to recover during 2010 and 2011[44] and all the major credit providers were expecting a recovery in credit sales. More recent evidence has suggested that there is credit available, and though there has not yet been a strong upturn in lending, we have probably reached as low a point in terms of credit lending as will be seen in this recession.[45] The evidence suggests to us that we would expect credit conditions to lead over time to an increase in PPI sales going forward relative to sales achieved in 2008 and 2009.

4.62. We were satisfied that the low level of GWP in 2009 compared with previous years was not something which in itself indicated that competition was now effective or that distributors would no longer be able to earn significant economic profits from PPI and therefore was not something which should cause us to amend our remedy package.

4.63. We therefore concluded that those changes to the volume and value of PPI sales, distributor income, claims and profitability which we saw did not constitute a material change in circumstances, nor did they amount to a special reason which caused us to amend our decision on the nature of the required elements of the remedy package, as set out in paragraphs 10.567 to 10.572 of the 2009 report.

4.64. However, we did take account of the changes in market outcomes in our analysis of the scale of the detriment that flows from the AEC (through updating inputs to our modelling exercise relating to margins, excess profits, penetration rates, price of PPI

[44]For example, the 2009 pre-budget report (published in December 2009) stated that 'credit conditions are expected to recover into 2010 and 2011 and so support the recovery' (see p159 of www.hm-treasury.gov.uk/d/pbr09_annexa.pdf).
[45]In August 2010, the Council of Mortgage Lenders (CML) issued a revised prediction for gross mortgage lending in 2010 of £140 billion. This is about 2 per cent lower than gross mortgage lending in 2009, which was itself only just over one-half of the gross mortgage lending in 2008. The Bank of England Credit Condition Surveys, conducted quarterly, showed that availability of secured credit to households was broadly unchanged in the three months to mid-March 2010, and rose slightly in the three months to early June 2010, but availability was expected to fall back in the following three months, in part reflecting some lenders' expectations that wholesale funding market conditions might tighten in that period. Demand for secured lending for house purchase from households was reported to have fallen somewhat in the three months to June 2010. Demand for secured lending for remortgaging was reported to have risen for the first time since 2008 Q4, but only a small balance of lenders was anticipating demand to increase further in the next three months. Unsecured credit availability to households was reported to have stabilized in the first three months of 2010 and remained broadly unchanged in the second quarter. Lenders reported that demand for unsecured credit increased in 2010 Q2, especially for non-credit-card lending. Lenders expected demand for credit card lending to stabilize in the next quarter and demand for non-credit-card lending to fall back a little. In August 2010, the BBA published data which showed that the annual growth in the main high street banks' net mortgage lending was 4.1 per cent, compared with 0.9 per cent for the whole mortgage market in June. It said that gross mortgage lending remained stable, although demand for mortgages continued to be subdued. In terms of unsecured lending, it said that value of demand for personal loans was 16 per cent lower than a year ago. The number of credit card purchases fell back in July 2010 to be in line with the six-month average despite reports of slightly stronger retail sales volumes. Moreover, [✄].

relative to credit and extent of the waterbed—see Appendix I). Therefore, we have taken account of the relevant changes in our proportionality assessment, which is informed, in part, by our modelling of the impacts of our remedies.

Changes that impact on the point-of-sale advantage

4.65. In paragraphs 10.36 and 10.37 of the 2009 report, we explained how the POSP would contribute to addressing the AEC, by addressing the point-of-sale advantage, and also some of the barriers to search.

4.66. Barclays submitted, in response to our provisional decision, that market developments, such as the introduction of stand-alone PPI and short-term IP by large providers, eroded any point-of-sale advantage and lowered barriers to entry and expansion to the stand-alone PPI market.

4.67. However, we did not see any evidence upon which we could conclude that distributors had started either to offer or to inform customers of the existence of competing PPI products at the credit point of sale, such that our finding in paragraph 5.104 of the 2009 report that customer choice at that point (when they were most likely to be focused on their insurance needs) was restricted no longer stands.

4.68. We also noted that many providers offer PPI on an advised basis (see Table 2.8 of the 2009 report) focusing on the suitability of their own PPI product to meet a customer's needs and not advising on whether there are competing PPI policies which might better meet that customer's needs.

4.69. Both the Accent survey[46] and the CC BMRB 2007 survey[47] provided evidence that customers still believe that buying PPI will increase the likelihood of their credit application being accepted.

4.70. We did not see any evidence that searching for information about PPI policies had become any easier. We noted that there has been no change in the way in which price is quoted with the same approaches used as we noted in the 2009 report. We noted that search facilities remain as limited as we found in the 2009 report, despite the launch of the moneymadeclear comparison website towards the end of our investigation. We were told by one commercial comparison website company that the main change since the 2009 report was that several PPI providers had withdrawn their products from their website.

4.71. Accordingly, the evidence before us suggested that none of the market developments since the 2009 report had displaced the point-of-sale advantage, nor had customer search behaviour changed to any material extent. We thought, therefore, that the fundamental issues which prevent effective competition in PPI markets remain in place. PPI is still sold at the credit point of sale, at which time the credit arranger holds an effective monopoly over the provision of PPI, leading to the effects set out in paragraphs 4.67 to 4.70.

4.72. We therefore concluded that the point-of-sale advantage had not been eroded in any way which caused us to change our decision to remedy the AEC by way of implementation of the remedy package, including the POSP, as we set out in paragraphs 10.567 to 10.572 of the 2009 report.

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[46]See p31 of the survey report: www.competition-commission.org.uk/inquiries/ref2007/ppi/pdf/Consumer_attitudes_to_Payment_protection_24_June_2010.pdf.
[47]See: www.competition-commission.org.uk/inquiries/ref2007/ppi/consumer_research.htm.

Conclusions on the impact of developments in the market

4.73. We considered the evidence on the developments in the PPI markets—the changes in the regulatory environment; mergers within and exits from PPI markets; the changes at product level;[48] the reductions in numbers of policies sold and the decline in GWP; the increases in claims and reduced profit shares; and the changes in profitability—and the impact of those developments on the POSP and the remedy package more generally.

4.74. In our judgement, the fundamental issues which prevent effective competition in PPI markets remain in place. The monopoly provision of PPI at the point of sale of credit is still leading to a lack of competition among distributors and barriers to entry and expansion for stand-alone providers. Consumers are still not properly informed that they have options and what those options are and continue to face barriers when searching for new policies and when seeking to switch away from existing policies.

4.75. We therefore concluded that there were no market developments that constituted such a material change in circumstances or a special reason that it was necessary for us to amend the remedy package, including the POSP, as set out in paragraphs 10.567 to 10.572 of the 2009 report.

5. Loss of convenience

Summary

5.1 In this section we address two questions. First, we consider whether there is a loss of convenience for some or all customers associated with introducing a POSP, and second, we assess the cost of this loss of convenience to those customers who prefer to purchase PPI at the credit point of sale.

5.2 We conclude that, for some customers, there is a loss of convenience associated with the introduction of a POSP. However, we conclude that the parties are over-stating the extent of this loss of convenience and the impact on PPI sales that would result from it. We conclude that for PLPPI the loss of convenience, in the absence of any of the benefits of the remedies, would result in a drop in PLPPI volumes for distributors of around 20 per cent. For MPPI, the reduction would be less than 5 per cent.

Introduction

5.3 The Tribunal found that the CC had failed to take into account the loss of convenience to consumers which would flow from the introduction of a POSP in assessing whether it was proportionate to include it in the proposed remedy package. In this section we address two questions.

5.4 First, we consider whether there is a loss of convenience for some or all customers associated with introducing a POSP, and second, we assess the cost of this loss of convenience to those customers who prefer to purchase PPI at the credit point of sale. In addressing these two questions, we also consider the potential impact of this loss of convenience on the level of PPI sales.

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[48] Including LBG's decision to stop selling PPI for the time being; the voluntary withdrawal from sale of single-premium PLPPI policies; and the introduction of short-term IP products (see paragraphs 4.25–4.43 and Appendix A, paragraphs 4–19, for further detail).

5.5 The rest of this section is structured as follows:

(a) We start by setting out what a loss of convenience is (paragraphs 5.8 to 5.11) and the extent to which different types of evidence are able to isolate a loss of convenience from other factors which might cause a fall in take-up of PPI products offered by distributors (paragraphs 5.12 to 5.18).

(b) We then review the evidence—experiments, companies' internal documents and consumer research including a survey conducted for us by Accent—about whether there is a loss of convenience associated with the POSP (paragraphs 5.19 to 5.59).

(c) Next we look at what the Accent survey tells us about strength of preference, as a guide towards scale of the cost of the loss of convenience (paragraphs 5.60 to 5.87).

(d) Finally, we consider this evidence and reach conclusions on the magnitude of the loss of convenience associated with a POSP for consumers who prefer to buy PPI at the same time as credit, and the magnitude of the benefit associated with a POSP for those consumers who prefer delay (paragraphs 5.88 to 5.92) and the implications that might have for sales of PPI, in the absence of the benefits of the remedies.

5.6 This section does not deal with the benefits that might be expected to accrue from introducing the remedy package—for example, distributors offering better-value products, a larger and more dynamic stand-alone market developing to attract business lost by distributors, or the impact of consumers having more information about PPI policies. The evidence we saw was mainly concerned with a separation of the sales of credit and PPI, taken in isolation from the rest of the remedy package and its likely beneficial effects. It did not look at the dynamic ways in which the market might develop with the remedy package in place. We consider, for products other than retail PPI, what benefits might be expected to accrue and consider their relevance in Sections 7 and 8.

5.7 As we found that we could not be confident that our remedy package would be substantially effective for retail PPI (see paragraph 8.21), we do not consider the impact of loss of convenience from introducing a POSP for retail PPI in this section. For the same reason we do not model the impact of the remedy package for retail PPI in Section 7.

What is a loss of convenience?

5.8 For the purposes of this remittal we consider a loss of convenience to be any costs to consumers of not being able to buy PPI from their credit arranger at the credit point of sale, but instead—if they still wished to buy PPI from their credit arranger—either having to return to their credit arranger the following day, or waiting for a week to be contacted by their credit arranger. As a consequence of such a loss of convenience, some consumers may not purchase PPI.

5.9 During the original investigation many parties told us that being able to purchase PPI at the same time as credit was convenient for customers, as this was the time when the need to protect their ability to repay the credit extended to them was at the front of their minds (see paragraph 10.46*(b)* of the 2009 report). We were told that a large proportion of consumers would not bother to purchase PPI away from the credit point of sale as it would be significantly less convenient for them to do so. Providers would be likely to find it difficult to arrange another meeting or conversation with consumers following the conclusion of a credit arrangement. Consequently, the inconvenience to consumers arising from being unable to buy PPI at the point when they purchased the credit after the introduction of the POSP would lead to a reduced take-up of PPI, to the serious detriment of the PPI market.

5.10 The parties told us that the possible consequences of a loss of convenience for consumers are that they have to devote more time and effort taking out a policy, that they are not covered immediately, and, most importantly for most parties, that consumers would simply fail to take out PPI as a consequence of not being able to buy it at the point of sale of the credit. In this regard, AXA UK plc (AXA) (and others) referred us to behavioural research it had commissioned (*Turning Good Intentions into Actions*, by Decision Technology)[49] which showed that, in certain experimental situations, even small delays could significantly reduce the likelihood of taking action. The possible consequences for the market more generally would be a reduction in the number of policies sold.

5.11 We agreed with parties that it is important to consider the possible loss of convenience. This is because if there is a significant loss of convenience, resulting in many consumers not taking out PPI and the market contracting substantially, there could be unintended effects of the remedy package which could be disproportionate to its aim, such that putting the remedy package in place would in those circumstances not be appropriate.

Relationship between loss of convenience and take-up rates

5.12 One possible consequence of a loss of convenience is therefore that credit arrangers' take-up rates for PPI could decline, if customers are deterred from taking out PPI. However, in our judgement there are some other reasons why consumers might not take out PPI from their credit arranger following the introduction of the remedy package which would not be due to a loss of convenience.

5.13 First, some customers might decide to take out PPI with providers other than their credit arranger. Our remedy package contains measures aimed at raising customers' awareness of alternative providers and giving customers the opportunity and tools to consider these alternatives. An important effect of introducing the remedy package would therefore be to increase the degree of competition faced by credit arrangers, such that we would expect more customers to consider, and in some cases choose, the alternatives available to them.[50] Other customers might decide to take out alternative insurance products (eg life insurance) with the credit arranger or with another supplier.

5.14 Second, some customers, given the time, space and tools to consider their needs, would decide they either did not need or did not want PPI. We consider such sales to be 'unwanted'. For example, a customer might realize that they cannot benefit from the policy at all, that they already have alternative forms of cover and do not need more cover, or a customer might feel under pressure to take out the policy at the credit point of sale whereas, on reflection, they might choose not to take out the policy. To the extent that any decline in take-up of PPI is as a consequence of the elimination or reduction of unwanted sales at the credit point of sale, we do not regard the loss of such unwanted sales as indicative of any loss of convenience resulting from the POSP.

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[49] www.dectech.org/Links/Brief-AxaPart2.pdf.

[50] This would result in an increase in the firm-level elasticities of demand faced by individual distributors, relative to the current situation.

5.15 There is some evidence that there may have been some unwanted sales in the past—a survey conducted for us in late 2007 by BMRB[51] found that between 25 and 47 per cent of consumers of PLPPI, MPPI, CCPPI and SMPPI believed that their credit application was more likely to be accepted if they took out PPI. In addition, the Accent survey (see paragraph 5.48) noted that 11 per cent of PLPPI customers and 4 per cent of MPPI customers said that a reason for taking out PPI when they had was because either they thought they had to take out PPI or felt somewhat pressurized to do so.

5.16 Further, PPI currently suffers from a poor reputation, with most publicity relating to PPI being negative.[52] If consumers had the time and space to consider their options, a possible outcome under current market conditions is that some would choose not to buy PPI because of this negative publicity.

5.17 We noted in our overall consultation that we planned to look at mis-selling. Mis-selling can be thought of as one example of possible unwanted sales, though not all unwanted sales would be due to mis-selling. We received many responses from parties saying that we should not look at this issue—responses are summarized in Appendix B. Evidence from parties' internal documents and on the volume of consumer complaints upheld suggests that there have been significant sales quality issues in the market. The FSA considers there to be a problem with mis-selling (as evidenced by its thematic reviews, mystery shopping, enforcement actions, and the request to stop selling single-premium PLPPI). Similarly, while the FOS recognizes that it sees only a relatively small and potentially skewed proportion of complaints (and so an even smaller proportion of sales), from its casework it has seen evidence of mis-selling, as evidenced by the large proportion of cases where it reaches a change decision. Some PPI distributors disagree with the views of the FSA and the FOS on the extent of mis-selling. Overall, while there is clear evidence that there have been problems with sales quality in the past, this evidence was not conclusive on the extent to which, were there a POSP in place, we might expect the number of policies sold to decrease because of a reduction in unwanted sales.

5.18 We concluded that a drop in a credit arranger's PPI sales resulting from a break in the sales process could be caused partly by consumers actively deciding either that they did not need or did not want PPI, buying PPI elsewhere, or buying an alternative insurance product. To the extent that there was a drop in sales for any of these reasons, we do not consider this to be a consumer detriment, or a cost to consumers, and should not be included in any calculation of the costs of a loss of convenience arising from the remedy package.[53] We consider this in our modelling in Section 7. We would not expect unwanted sales to be a significant feature of PPI markets if we put the remedy package in place, as we would expect increased competition to ensure that products better suited to consumers' needs come to market and that sales quality is higher than it has been for some firms in the past. In this respect, we noted that several large distributors and underwriters have been developing new short-term IP products in anticipation of the remedy package coming into force and that these new products appear to perform strongly in customer research (see Section 6).

[51] www.competition-commission.org.uk/inquiries/ref2007/ppi/pdf/consumer_research_ppi_feb.pdf.

[52] For example, This is Money has campaigned since 2006 against what it said had been widespread mis-selling of PPI (see: www.thisismoney.co.uk/reclaim-ppi). In a table of the pros and cons of different types of protection insurance, Which? said that PPI had no obvious benefits, but that 'Policies are full of exclusions and are very poor value. Often sold inappropriately to people who already have better cover in place' (see: www.which.co.uk/money/insurance/guides/understanding-protection-insurance/types-ofprotection-insurance/).

[53] We would consider the exercise of informed choice by consumers to be a sign of a market in which information is being delivered in a way that consumers can use effectively.

Evidence on a possible loss of convenience

5.19 To consider whether there would be a loss of convenience associated with introducing a POSP, we considered evidence from four sources:

- experiments (including pilots specifically run to look at what would happen with a POSP) (paragraphs 5.23 to 5.33);
- parties' internal estimates of the likely take-up of PPI with a POSP in place (paragraphs 5.34 to 5.41);
- parties' survey evidence on the possible impact of selling PPI away from the credit point of sale (paragraphs 5.42 to 5.47); and
- a survey conducted for us by Accent (paragraphs 5.48 to 5.52).

5.20 We then considered what the various survey evidence showed us about the extent to which a loss of convenience was likely to be felt by different consumers (paragraphs 5.53 to 5.57), and concluded on whether there would be a reduction in the sales of PPI with a POSP, in the absence of the benefits of the remedies (paragraphs 5.58 to 5.59).

5.21 When examining the different evidence that was submitted to us, we considered the extent to which each piece of evidence addressed directly the issue of convenience, and in particular:

(a) the extent to which the evidence isolates the impact of convenience—for instance, evidence on a drop in credit arrangers' take-up rates could be for other reasons than the loss of convenience (see paragraphs 5.12 to 5.18); and

(b) the extent to which the evidence properly represents the POSP (as summarized in Figure 10.1 of the 2009 report and Appendix N).

5.22 In addition, nearly all of the evidence that we review in this section focuses on the impact of introducing a delay into the PPI sales process, without also considering the beneficial effects that we expect to result from the introduction of effective competition into PPI markets through our remedy package.[54] We expect the remedy package, including the POSP, to introduce competition into PPI markets and thereby to give rise to a variety of beneficial effects (including lower prices, better information and increased customer awareness, selection pressure from increased choice leading to better products and improved reputation of PPI), all of which we expect to increase demand for PPI and customer welfare (see paragraphs 10.477 and 10.493 to 10.495 of the 2009 report). The different sources of evidence that we review in this section therefore told us about the impact of the loss of convenience resulting from the introduction of a delay into the sales process, in the absence of the benefits of the remedy package—in effect, in the hypothetical situation that the remedy package is wholly ineffective and does not introduce competition into the market. This does not invalidate such evidence, but in reaching our overall view on proportionality we will need to take account of the beneficial effects that we expect to result from introducing the remedy package. We do this in Sections 7 and 8.

[54]See paragraph 8.5, and paragraphs 10.477 and 10.493–10.495 of the 2009 report.

Experiments

5.23 Many parties told us that a POSP would result in a loss of convenience and that there were 'natural experiments' which would give an indication of the size of the reduced take-up that would occur as a consequence. In addition, LBG conducted a pilot specifically to inform its response to the remittal and HSBC ran a pilot which informed its response to the remittal.

5.24 The evidence put to us looks at how distributors' penetration rates might fall if the credit and PPI sales processes were split in different ways. We considered evidence from several sources. Details of the experiments and our analysis of them are set out in Appendix C.

5.25 The experiments were mainly concerned with a separation of the sales of credit and PPI, taken in isolation from the rest of the remedy package and its beneficial effects on competition. As noted in paragraph 5.22, this does not invalidate the experiments as a source of evidence but does mean that we are interpreting them as showing the potential effects of a POSP in the absence of the benefits that we expect to arise from the remedy package.

5.26 Parties' interpretation of their experiments showed a very wide variation in the reduction in sales that might be expected with a POSP in place—from a reduction of 97 per cent (Nationwide) to a reduction of 25 per cent (HSBC).

5.27 We found that all the experiments suffered from problems associated with one or more of the following: design, implementation and timing.

5.28 In terms of design, only the LBG 2009 and 2010 pilots allowed for customers to call back after 24 hours to take out PPI—which is a key design element of the POSP, allowing customers who are already decided on buying the credit arranger's PPI product to do so at an earlier stage (see paragraphs 10.117 to 10.126 of the 2009 report and Appendix N).[55] Other experiments did not provide much or any information to customers about PPI at the credit point of sale (for example, the Nationwide evidence), whereas the interaction of the POSP with the provision of a personal PPI quote and the other informational remedies is another key design element of the POSP (see paragraph 10.37 of the 2009 report and Appendix N), without which experiments might be expected to overstate the reduction in sales with a POSP in place. Conversely, one (Barclays) provided a one-page note to customers setting out information on four different insurance products, only one of which was PPI, at the credit point of sale. This encouraged customers to consider non-PPI products and might be expected to result in some customers using the time and space following purchase of the credit product to buy alternative products to meet their needs (see paragraph 5.12)—which we would not consider to constitute a loss of welfare but would be recorded as a loss in sales. In practice, the experiments did not precisely replicate the POSP—for example, the HBOS pilot involved a change in salesperson within one sales call, and the LBG 2009 pilot involved completing the PPI sale at the credit point of sale.

5.29 In terms of implementation, two of the pilots—the LBG 2010 pilot and the HSBC pilot—both experienced very low levels of personal PPI quote provision—at or below (significantly below in the case of face-to-face sales in the LBG 2010 pilot, where the percentage of quotes issued was less than a third of the normal penetration rate for

[55]As noted in paragraph 14*(a)* of Appendix N, we have amended the period within which consumers can return to purchase PPI from 24 hours to the next day, which will further reduce inconvenience to customers in this situation.

PLPPI sales) the usual penetration rate for sales of the product. We thought this indicated that there had been problems with the way the pilots were implemented. Some of the experiments were conducted on a very small scale, which can lead to results that are not statistically robust—for example, the Barclays experiment involved calls successfully made to only [50–60] customers; the LBG 2009 pilot involved 58 customers; and the HSBC pilot's scale was such that for CCPPI the pilot was unable to determine whether a POSP would cause an increase or a decrease in penetration rates, and for PLPPI the results were not as statistically significant as we would normally accept.

5.30 In terms of timing, all the pilots were conducted during a time when the publicity about PPI was overwhelmingly negative, reducing the chances that, given additional time to think about their purchase, consumers would choose to take out PPI.

5.31 In addition, the experiments do not isolate the impact of convenience from other factors that might reduce take-up rates (see paragraph 5.22).

5.32 In response to our provisional decision, Barclays[56] said that it was absurd, in an analysis of the impact of the loss of convenience, for the CC to claim that natural experiments intended to mimic the imposition of a POSP were not very informative on the impact of the remedies on the PPI take-up rates due to them not taking account of the other remedies. We do not dispute that experiments can in principle provide us with useful information about what would happen, even if they only cover one element of the remedy package (in this case a break in the sales process as an attempt to mimic the impact of the POSP, or attempts explicitly to model the POSP), and have regard to them in this light. However, to reach a full assessment of the proportionality of including the POSP in the remedy package we need to take account of all of the remedy package's likely effects, including the benefits of what has been designed to be a package of mutually reinforcing measures (see paragraph 10.478 of the 2009 report). We do this in Sections 7 and 8. We also found that all the experiments suffered from problems associated with design, implementation and/or timing and these problems are a relevant factor in determining what conclusions could reliably be drawn from the experiments.

5.33 We concluded from the experiments that:

- In the absence of the benefits of the remedy package, distributors are likely to experience a reduced take-up of PPI if the sales process between credit and PPI was in some way split. However, because of the problems with the experiments (see paragraphs 5.28 to 5.30 and Appendix C), which in our judgement tended to increase the reduction in take-up experienced, we could not reliably quantify from these experiments how large a reduction there might be. Overall, we thought that the experiments were likely to overstate the impact of the introduction of a POSP on take-up rates, even before taking account of the beneficial effects of the remedies.

- Some customers who currently purchased PPI might not purchase it with a split in the sales process between credit and PPI, because they are difficult to contact after the credit sale (eg by telephone)—although how many of these would have taken out PPI if contacted we were unable to quantify. Conversely, some customers have been both willing and able to engage with distributors about PPI away from the credit point of sale, either by initiating contact or by responding to

[56]Barclays response to provisional decision, p13.

contact initiated by distributors—although we were unable to quantify this from the experiments.

- The detail of how distributors choose to set up their sales processes—including the motivation of sales staff and the number of different members of staff to whom a customer talks during a sales process—can have a material impact on the penetration rates that can be achieved. As we found that nearly all distributors intend to continue selling PPI[57] if we put the remedy package in place (see Section 6 and Appendix G), we would expect them to have incentives to optimize these processes with the POSP in place.

Parties' internal estimates of PPI take-up with a POSP

5.34 We looked at internal documents submitted by parties to see what assumptions they had made about take-up rates of PPI with a POSP in place. Details of what we found are in Appendix D.

5.35 These internal documents generally looked at take-up rates for distributors' existing PPI products under a 'business as usual' scenario, before considering what actions could be taken to increase take-up rates, including, for example, introducing new products that are more suited to customer needs. Our review of internal documents relating to distributors' plans if we put the remedy package in place is in Section 6.[58]

5.36 The internal documents showed that, for PLPPI, parties expected sales to decrease significantly. Estimates of the immediate impact of the remedy package suggested a reduction in the range of 40 to 60 per cent before any action was taken to try and increase sales.

5.37 For MPPI, we found limited internal documentation. The documentation that was provided suggested that some parties expected that the remedy package would not have a significant impact on penetration rates, but overall the range of predictions was between a minimal fall in penetration rate and a 40 per cent fall.

5.38 For CCPPI, estimates ranged from a 20 to 60 per cent reduction in sales with the remedies in place (with one party in addition assuming a further 10 per cent fall in penetration due to the annual review).

5.39 We considered these estimates carefully. We recognized that these estimates were used for business planning purposes and as such carry some weight. Some of these were developed in light of experiments conducted by parties (see paragraphs 5.23 to 5.33). Others seemed to be based on individual executives' assessment. The documents were prepared to consider the adverse impact for a business of imposing a POSP on its existing business. The documents largely look at this in isolation, without considering whether mitigating action could be taken to reduce the impact. On balance, we thought that the estimates based on experiments were likely to suffer from the problems set out in paragraphs 5.28 to 5.31. We thought that those estimates that were based on the assessments of individual executives were likely to draw most heavily on their experience of how the current market structure operates—including the benefits derived by the distributor from the current arrangements—rather than on specific empirical evidence on how customers would respond to the remedy package. In addition, the estimates were not developed to isolate the effects of loss of conven-

[57]Either branded as PPI, or as short-term IP.
[58]See in particular Table 6.1, which shows consumer research into customer preferences, and paragraphs 6.13–6.27, where we note how some parties have responded in developing new products.

ience from other factors that could affect individual firms' sales of PPI (see paragraphs 5.12 to 5.18 for other factors that can impact take-up).

5.40 We also noted that if we used these estimates of a decline in take-up in our model as indicating the impact on sales of a loss in convenience (see Section 7), this would imply either that customers have a very high valuation of being able to purchase at the credit point of sale, or that there is a very large market elasticity of demand (or a combination of the two).[59] In both instances the estimates of these parameters that would result, for all products, were, in our judgement and in light of the evidence that we have considered in relation to these two parameters, unfeasibly large.

5.41 We concluded for these reasons that firms' internal business estimates of take-up rates were likely to overstate the impact of the influence of the POSP on convenience even before taking account of the benefits of implementing the remedy package.

Survey evidence

5.42 We considered evidence from surveys on customers' views of the possible impact of selling PPI away from the credit point of sale.

Evidence from surveys conducted by parties

5.43 We looked at evidence from surveys conducted by or for the parties to the investigation. Details of the evidence are set out in Appendix E.

5.44 During the original investigation, parties put forward evidence in relation to the convenience associated with purchasing PPI at the credit point of sale: convenience featured prominently in reasons given for purchasing PPI at the credit point of sale. For example, in GfK research submitted by [✂], 91 per cent of respondents cited convenience as a reason for simultaneous purchase of PPI and credit. Barclays submitted that 75 per cent of its PLPPI consumers considered that the best time to purchase PPI was before or at the same time as applying for the loan.

5.45 The evidence we found from parties during the remittal indicated that many customers express a preference for buying PPI at the credit point of sale, or think this is a good time to buy it, but there are also many who would prefer to buy it with a gap between credit sale and PPI sale. Some who expressed a preference for buying at the credit point of sale said that they would not buy it at a later time—either because they thought they would forget to, or for unspecified reasons. In terms of quantitative survey evidence:

- In June 2008, [✂] conducted quantitative research into customers' views on buying PPI. For [70–80] per cent of respondents, the best time actually to purchase PPI was when applying for the loan. This did not tell us that these customers would not buy PPI at any other time, but we recognized that some might not.

- In contrast, September 2008 research for [✂] asked whether respondents would prefer to take out immediate cover there and then or not to get cover straight away because they would want to think about it. [20–30] per cent of the 948

[59]The impact on sales of the loss of convenience depends both on the costs associated with the loss of convenience and the amount by which demand reduces as a consequence of these additional costs, which is measured by the PPI elasticity of demand.

respondents indicated that they would prefer to take immediate cover and [70–80] per cent indicated that they would prefer not to take cover straight away.[60]

- In October 2009, [✄] commissioned quantitative research which found that, with a POSP in place, around eight out of ten respondents would be more comfortable taking out protection after a seven-day period. Whilst [60–70] per cent of respondents said that they would actively seek cover from other providers during the seven-day period, around four out of ten respondents would be less likely to take up cover after a seven-day period. Of [30–40] respondents who had purchased a credit product with PPI, there was a roughly equal split between those who said that they would have taken out the PPI if there had been a POSP and those who said they would not have done.

- In November 2008, ABI commissioned a survey of 1,978 Great Britain adults. The majority of respondents (58 per cent) said that they would prefer to buy PPI from their credit provider at the same time as they take out their mortgage, personal loan or credit card. When asked what they would do if they were not able to buy PPI at the same time as they took out their mortgage, loan or credit card, 52 per cent of all adults said that they would probably not purchase PPI and a further 19 per cent said they did not know. We do not have evidence of what the other 29 per cent said. When asked for their views on the statement 'I would rather my lender offered me PPI two weeks after I arranged the borrowing so I have time to consider my options', 39 per cent strongly agreed or agreed, 37 per cent were neutral or didn't know, and 24 per cent disagreed or disagreed strongly.

5.46 The qualitative evidence also shows different results depending on what is asked, and how. Data gathered from face-to-face/branch/group surveys indicated the following:

- Qualitative research conducted for [✄] in 2008 found that the majority of consumers would like to take out PPI when getting a loan; however, consumers do want the option to purchase at any time.

- Some customers had concerns about a delay in the sales process and the fact that they could not purchase the product immediately.

- In April 2009, [✄] commissioned qualitative research which found that some respondents thought that if they did not purchase PPI at the credit point of sale, the likelihood that they would remember to do so later was minimal.

- In terms of the perceived opportunity to shop around, [✄] found that customers said they would be more likely to shop around for the best deal with the POSP change. [✄] found that a minority of the 40 to 45 customers interviewed said that having an interim period would result in them shopping around.

- [✄] found that customers were not happy that they had to take further action themselves, to call back, but [✄] found that phoning the provider back after 24 hours to take out PPI was one of the preferred options. [✄] research also found that most respondents felt that in reality they would get caught up with other things or forget to call back to take out the cover, and the majority of respondents were not averse to the provider contacting the customer to prompt purchase of PPI.

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[60]This sample of 948 included a sample of PPI customers (509 respondents) and a sample of non-PPI customers (439 respondents). For the sample of PPI customers, [30–40] per cent indicated that they would prefer to take immediate cover and [60–70] per cent indicated that they would prefer not to take cover straight away.

5.47 Data gathered from telephony surveys ([✂]) and evidence of consumer reactions provided by agents who participated in a POSP test in the telephone channel ([✂]) indicated that some consumers thought that it was helpful to have time to think about purchasing the product and the opportunity to shop around.

The Accent survey

5.48 We commissioned a survey from Accent on the attitudes of recent customers to buying PLPPI and MPPI, and the value they attach to buying PPI at the same time as credit or later. We did not conduct the Accent survey for SMPPI, CCPPI and retail PPI customers, for the reasons set out in Appendix F.

5.49 The objectives of the Accent survey were to:

- understand consumer likes and dislikes in purchasing PPI at the same time as the loan to which it is connected;
- understand how consumers view the convenience associated with taking out PPI at the time of the loan, and any consequent loss of convenience if they have to wait a period of at least 24 hours after the conclusion of the credit sale before they can purchase PPI from the same provider; and
- quantify any potential loss in convenience from the consumer perspective.

5.50 The Accent survey consisted of initial qualitative research, followed by quantitative research. The qualitative research helped inform the design of a quantitative questionnaire. The quantitative questionnaire used a stated preference exercise to understand both the preferences of customers and a conjoint analysis to understand the strength of those preferences. The main programme of research involved interviewing over 400 recent purchasers of each of PLPPI and MPPI. We report on the conjoint analysis from paragraph 5.60.

5.51 The Accent survey[61] found that for PLPPI, 60 per cent of customers said they preferred to buy PPI at the same time as credit, whilst 31 per cent said they would prefer to buy it later. For MPPI, 50 per cent of customers said that they preferred to buy PPI at the same time as credit, whilst 36 per cent said they would prefer to buy it later. In both cases there were some customers who were indifferent to whether they bought it at the same time as credit or later.

5.52 Parties raised many concerns about the Accent survey. These criticisms were mostly focused on the conjoint analysis element of the survey, but some—related to the use of the qualitative survey and the representativeness of the sample—could in theory also impact on the other stated preference element of the survey (though parties did not argue that we should disregard these results). These concerns are set out in summary form in paragraphs 5.69 and 5.70 and in more detail in Appendix F. After careful consideration, we did not agree that they impacted significantly on the results reported in paragraph 5.51, which we consider to be robust.

What the surveys told us about loss of convenience

5.53 The evidence from the surveys led us to believe that some customers would experience a loss of convenience with the introduction of the POSP. The survey

[61] www.competition-commission.org.uk/inquiries/ref2007/ppi/pdf/100505_Accent_Survey_report_2FINAL.pdf.

evidence as to the proportion of consumers for whom this was the case was mixed and depended greatly on the way in which the question was asked (see paragraphs 5.45 and 5.46). The Accent survey found that for PLPPI, 60 per cent of customers said they preferred to buy PPI at the same time as credit, whilst 31 per cent said they would prefer to buy it later. For MPPI, 50 per cent of customers said that they preferred to buy PPI at the same time as credit, whilst 36 per cent said they would prefer to buy it later.

5.54 RBSG said that we did not appear to consider that where customers buy at the point of sale they must value the point-of-sale purchase and would continue to buy there if they were allowed to do so. Aviva plc (Aviva) said that we had attached insufficient weight to evidence showing that a majority of consumers would like to purchase PPI at the credit point of sale.[62]

5.55 We noted these views. However, we have identified significant consumer detriment associated with the AEC. We are required to remedy the AEC and the consumer detriment that results from it in an effective and proportionate way. In doing so, some consumers who prefer to buy PPI and credit at the same time may suffer inconvenience. We agree with parties that this is a relevant consideration and we go on to consider the scale of this effect from paragraph 5.60. The evidence indicates that other customers would prefer to have a gap between the two sales and they will experience some benefit. We have taken full account of the impact on convenience of those customers that prefer to buy at the point of sale in our modelling of the impact of the remedy package in Section 7.

5.56 Barclays[63] said that it was undeniable from a review of all the survey evidence that the majority (and in some pieces of evidence over nine out of ten) of PPI customers prefer to purchase PPI at the same time as the loan, and that the evidence suggested potentially large reductions in PPI purchases when point-of-credit-sale convenience is lost.

5.57 We thought that Barclays had overstated its case. In our judgement, the survey evidence produced some conflicting results, but it is possible to draw some broad conclusions. Many customers like buying PPI at the same time as credit (a majority in the cases of [✂] and ABI research). Equally, however, many customers like the option of being able to buy PPI later ([✂] qualitative research), and many or most prefer to take it out later ([✂] and ABI) or are more comfortable taking it out later ([✂]). The Accent survey findings were not out of line with these other pieces of research (for example, the Accent survey found smaller proportions preferring to buy later than the [✂] and [✂] research, and a higher proportion than research from [✂]). We decided to use the Accent findings as our base case in our modelling (see Section 7) as we judge this to be a robust analysis that is not out of line with other survey evidence.

Conclusions on evidence of a possible loss of convenience

5.58 The experiments and parties' internal documents indicated that distributors expected to experience a drop in take-up rates if there was a separation in the credit and PPI sales processes and there were no competition benefits arising from the remedy package. We concluded, however, that these estimates overstated the impact of the loss of convenience.

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[62]Aviva response to provisional decision, p1.
[63]Barclays response to provisional decision, Annex 1, section 2.5.

5.59 The evidence from customer research (including the Accent survey) showed that many customers prefer to buy PPI at the credit point of sale, and that many other customers prefer to have a gap between buying credit and PPI. We concluded that the proportions found in the Accent survey—around 60 per cent of PLPPI customers and 50 per cent of MPPI customers preferring to buy PPI at the same time as credit and around 30 per cent of PLPPI customers and 35 per cent of MPPI customers preferring to buy PPI later—were good estimates of the split between these two preferences.

The cost to customers of the loss of convenience

5.60 Having concluded that, if a POSP were introduced but without the benefits of competition which we expect with the remedy package, there would be a loss of convenience for some existing customers, which would in turn lead to some drop-off of sales of PPI to existing customers, we consider now the scale of the costs to customers of the loss of convenience.

5.61 As set out in the first part of this section, the parties presented us with evidence on the expected impact of the POSP on take-up of PPI. We explained in paragraphs 5.28 to 5.30 why it was not reliable as a guide to the magnitude of any drop-off in sales arising from the POSP. Further, as noted in paragraph 5.31, none of the evidence presented to us isolated the effect of the loss of convenience from other effects that might cause a fall in credit arrangers' take-up rates; we thought it likely that some of the reduction in sales that would be expected would be due to some people using the time and space introduced by a POSP and deciding that they either did not need PPI or did not want, for whatever reason, to take out PPI from their credit arranger (see paragraphs 5.12 to 5.18).

5.62 We did not therefore have any satisfactory measure from the parties of the costs to customers of the loss of convenience. We next considered the results of the Accent survey (see paragraphs 5.48 to 5.51) which did provide an estimate of these costs. To do this Accent conducted a conjoint analysis stated preference exercise (see Appendix F for details).

The results of the Accent conjoint analysis

5.63 Taking all PLPPI customers together, the results of Accent's conjoint analysis were that on average customers would be willing to pay for a delay in PPI purchase. This implies that, on average, customers attached a negative value to purchasing PPI at the credit point of sale. The same result was found when all MPPI customers were taken together.

5.64 However, we knew from the stated preference part of the Accent survey,[64] and from other consumer research, that some consumers preferred to buy PPI at the same time as credit and some preferred delay, whilst a smaller proportion were indifferent to when they bought it (see paragraph 5.51). We therefore asked Accent to look at the results for each product, dividing respondents into those who, according to their other answers, preferred buying PPI at the same time as credit, those who preferred delay, and those who were indifferent.

5.65 Looking at only those customers who preferred to buy PPI at the credit point of sale, for PLPPI the Accent survey found that the average value of taking out PPI at the

[64]Question 19 in the Accent survey specifically asked about buying preference.

credit point of sale was £9.00 per month when compared with calling back after 24 hours and £7.30 per month when compared with being called after seven days, compared with a mean monthly PLPPI premium of £30.50 per month—hence the average cost of the loss of convenience was between 23 and 30 per cent of the average monthly cost of their PPI policy. The Accent survey found that the lower cost of the loss of convenience after seven days was a reflection of a preference for a longer delay, if there was to be a delay, rather than a preference for being called by the distributor over making contact with the distributor on their own initiative.

5.66 Those MPPI customers who preferred to buy PPI at the credit point of sale did not attach a statistically significant value to this preference.

5.67 Looking at customers who expressed a preference for buying PPI either 24 hours or seven days after the credit point of sale, PLPPI customers expressed an average willingness to pay £25.20 a month more to buy it seven days after the credit sale, and £19 per month more to buy it 24 hours after the credit sale. For MPPI customers, the equivalent figures were £30 and £18.70 per month. Hence the average value of convenience for customers preferring a delay was between 62 and 82 per cent of the average monthly cost of their PPI policy for PLPPI respondents and between 52 and 85 per cent for MPPI respondents.

Criticisms of the Accent survey and its results

5.68 We received many representations from parties criticizing the Accent research. These are set out in Appendix F, as are our views on the issues raised. We summarize some of the main points raised here, looking at criticisms of the qualitative survey, the representativeness of the sample, the design of the quantitative survey, and the magnitude of the results of the survey.

5.69 There were some criticisms of the qualitative survey run by Accent to help frame the quantitative survey. We concluded that the qualitative survey was sufficiently robust for the purposes of helping frame the quantitative survey. We did not need to rely on it to validate the results of the quantitative survey, as where Accent had noted in its report that the qualitative results were in line with the quantitative results, we noted that the quantitative results were also generally in line with what was found in other surveys conducted by parties to the inquiry (see paragraphs 5.45, 5.46 and 5.59).

5.70 Two parties raised criticisms of the representativeness of the sample of customers interviewed. We found that our survey sample was representative over most demographics. However, we found that it had an over-representation of PLPPI customers aged 35 and above and MPPI customers aged 44 and above. We asked Accent to provide a separate statistical analysis for each of the different age groups and they did not show any statistically significant differences in results between groups.

5.71 We also found that the sample had a slight over-representation among higher household income respondents; the evidence suggested that this might inflate the coefficient for delay (as higher-income respondents overall had a statistically significant preference for delay, whilst lower household income respondents overall had an preference for delay, though this was not statistically significant). We recognized that our results for PLPPI may be slightly biased towards delay because of the slight over-representation of higher household income respondents. To take this into account, we used in our modelling of the effects of the remedies on consumers, the lower positive valuation of the delay (ie £19 per month for PLPPI customers rather than £25.20; and £18.70 per month for MPPI customers rather than £30; see paragraph 5.67). We also checked the sensitivity of our results on consumer welfare to lower positive valuations for the delay.

5.72 Finally, we looked the representativeness of customers from different purchase channels—LBG said that we had oversampled customers who bought PLPPI over the telephone and that this skewed our results. We found that the proportion of customers buying PLPPI face-to-face was almost identical to the overall sample sent to us by parties, and concluded that the sample was not biased in terms of distribution channels.

5.73 Parties raised many issues relating to the survey design. These included:

- LBG said that the questions asked in the stated preference exercise underpinning the conjoint analysis more strongly favoured delay than non-delay. We considered whether there was any evidence that this was in fact the case. We concluded that there was not. First, the econometric analysis of choices used to derive estimates of willingness to pay would take account of any biased choices. If the choice between two options very strongly favours delay and the respondent chooses the delay option, the econometric analysis will only attach a small level of preference to that choice, whereas if the respondent chooses no delay, it will attach a high level of preference to the choice not to delay. Secondly, even using LBG's assessment of whether particular questions favoured particular answers, we did not agree with LBG that the questions more strongly favoured delay than non-delay (see paragraphs 46 and 47 of Appendix F).

- LBG also said that the options did not represent real-world choices. We disagreed; we were content that the options were realistic and understandable such that interviewees could both understand the options and trade off the choices.

5.74 Several parties raised concerns that the magnitude of the estimated values of customers' willingness to pay for a delay (or conversely to avoid a delay) (see paragraph 5.67) was too high to be realistic. We noted that the consumers' valuations of the cost or value of buying PPI tended to be significant when expressed as a proportion of the amount paid on policies over the life of the policies (this applied both to the positive valuations of those who prefer to buy later and the negative valuations of consumers who prefer to buy at the same time as credit). We considered whether these valuations may be higher than they should be due to respondents misinterpreting the price of buying later as a one-off cost rather than a monthly cost. However, respondents were presented both with the monthly cost and the annual cost comparisons in the conjoint analysis exercise, so should have been aware of the fact that it was a monthly price. We saw no evidence that interviewees had misunderstood the scenarios presented to them or were responding irrationally when making choices.

5.75 We also considered whether the willingness-to-pay results obtained in the analysis (for all the different attributes) may be explained by the technique that was used to analyse the results. The willingness-to-pay results were derived by comparing respondents' valuation for each attribute to their valuation of the price of PPI. Therefore, it is possible that the high levels obtained for the willingness-to-pay results may be partly due to the valuations of the price of PPI being small. This could have happened if the issue of price was 'overmasked' in the survey, for example if the difference in the price of the different options was not large enough or was insufficiently prominent for respondents to attach an accurate valuation to price. We have not found evidence of overmasking: the coefficients for the valuations of the price of PPI were all statistically significant[65] and so appeared to us to be robust. Even if such overmasking had occurred, it would affect the magnitude of both the

[65]Statistically significant at least at the 93 per cent confidence level, and mostly at or above the 95 per cent confidence level.

willingness to pay for delay and for buying PPI at the credit point of sale, but there is no reason to expect it to affect their relative values.[66]

5.76 We therefore judged that the relative values of the cost of buying later (for consumers preferring the point of sale) and the value of buying later (for consumers preferring a delay) found in the Accent survey were likely to be a good indicator of the relative strength of preference of the different groups of consumers. In addition, the absolute values of willingness to pay were statistically significant. In the absence of other reliable measures of the costs and values of buying later, we therefore used the Accent survey results in our base case (see Section 7), but conducted some sensitivity tests to check that our results were robust to lower valuations of the cost and value of buying later.

Conclusions from the Accent conjoint analysis

5.77 The Accent survey is the only piece of evidence we have seen which attempts to isolate and place a value on the importance of convenience to consumers. We considered in depth the validity of the results of the survey, aided by parties' comments both in response to our provisional decision and following access to a data room. We decided that we were able to rely on the results from the conjoint analysis, in particular, to reach the following conclusions.

5.78 The survey found that, although 50 per cent of MPPI consumers preferred to buy PPI at the credit point of sale, the valuation that these consumers associated with the ability to buy at the point of sale was small and not statistically different from zero. This showed that the preference for buying at the credit point of sale for MPPI consumers was not strong. We considered that this was a significant conclusion, as it indicated that there would be little loss in terms of convenience and consumer welfare for MPPI customers from not purchasing at the point of sale. For PLPPI customers, the reduction in price that would be needed to compensate those customers who preferred to take out PPI at the credit point of sale for the loss in convenience was between 23 and 30 per cent of the monthly premium. For both MPPI and PLPPI, respondents who preferred the option of buying later attached a very high willingness to pay to this preference, showing that their preference for delay was more strongly held than the preference held by those who preferred to buy PPI and credit at the same time.

5.79 We thought that the magnitudes of the willingness-to-pay results were higher than we might have expected both for delay and for simultaneous purchase. We looked carefully at whether the sampling had introduced a bias such that the willingness to pay for delay was too high, but we did not find a source of significant bias. There was also no evidence that the technique used to analyse the results had artificially inflated the valuation (paragraph 5.74). Even if this had been the case, it would affect the magnitude of both the willingness to pay for delay and for buying PPI at the credit point of sale, but there is no reason to expect it to affect their relative values.

5.80 We concluded that the Accent survey results were robust, and showed that the valuation of delay by consumers who prefer a delay between purchases of credit and PPI is larger than the costs of loss of convenience to customers who prefer buying both at the same time. We also concluded that, although there may be concerns that the magnitude of the customers' valuations was too high, these concerns applied both to

[66]The valuation for the delay and the valuation for buying at the point of sale are both derived by dividing the utility of the delay/ point of sale by the negative utility of price. If the negative utility of price were higher (in absolute value), this would therefore affect the valuation of the delay and of the point of sale in a similar manner, and the relative valuations should not be affected.

the positive valuations by customers who prefer the delay and to the costs of customers who prefer to buy PPI at the same time as credit. Therefore, even if the magnitude of the both the positive value and the cost of delay may appear high, the findings of the Accent survey about the relative magnitude of these two factors were robust.

5.81 We concluded that it was appropriate to use the willingness-to-pay figures calculated from the Accent survey as the base case in our modelling. We decided to conduct sensitivity checks around the effect of reducing their magnitude (while keeping their relative values constant), bearing in mind concerns expressed over whether the absolute values were too high to be plausible and because of a slight over-representation of higher household income respondents in the survey.[67]

5.82 We considered what these values meant in terms of a reduction in PPI take-up.

5.83 The Accent survey found costs of convenience (for 60 per cent of PLPPI consumers) of £7.30 (called after seven days) and £9.00 (call-back after 24 hours). Using the £7.30 figure (as, given that consumers would have a choice of when contact is made, they would choose the lower-cost option for them), this represented 24 per cent of the average monthly price of PLPPI.

5.84 For a market elasticity of demand for PLPPI of –1.4 (which is our base case assumption in the modelling),[68] an increase in price 'perceived' by consumers of 24 per cent would result in a reduction in volumes, from those customers who would suffer a loss of convenience, of 33 per cent at current PPI prices.

5.85 However, only 60 per cent of all PLPPI consumers prefer to buy PPI at the same time as credit (see paragraph 5.53), hence overall the reduction in volumes would be 60 per cent of this reduction—that is to say, the data from the Accent survey predicts a 20 per cent reduction in PPI take-up due to a loss of convenience if a POSP is introduced before taking account of the benefits of the remedy package. For MPPI, the predicted reduction is less than 5 per cent.

5.86 In our judgement, the impact of the loss of convenience for CCPPI customers is likely to be similar to that for MPPI customers as, like MPPI customers, they have multiple points of contact with the distributor—in particular, the CCPPI provider may be able to use the activation call to carry out the PPI sale ([✂]) or offer PPI to existing customers, through regular account management processes. However, as noted in paragraph 28 of Appendix I, for our modelling we used a cautious approach and used the PLPPI results from the Accent survey for modelling CCPPI. For SMPPI customers, we thought that the impact of the loss of convenience is likely to be similar to that for PLPPI customers, as the SMPPI sales process was, we thought, more similar to that of PLPPI than MPPI.

Conclusions on the cost of the convenience lost

5.87 The evidence from the Accent conjoint analysis suggested that the value placed on the loss of convenience for MPPI customers was not statistically significant, and, for those PLPPI consumers who preferred to buy PPI at the credit point of sale, was of the order of one-quarter of the monthly premium. We estimated that this would equate to a reduction in PLPPI sales of about 20 per cent, and a reduction in MPPI

[67]The results from these sensitivities are presented in Appendix J. We found that the output of the model did not change much if we reduced the magnitude of the valuations but kept the relative values constant.
[68]We consider the question of the correct level of elasticity to use in our modelling in paragraphs 7.53–7.55.

sales of less than 5 per cent before taking account of the benefits of the remedy package. However, we believe that the remedy package is likely to lead to increased competition and hence beneficial effects that will tend to increase demand for PPI and so these are not estimates of the impact of the overall remedy package on take-up rates. This is considered in Section 7.

Conclusions on loss of convenience

5.88 The evidence from experiments, parties' internal estimates and surveys (run both for parties to the investigation and for us) led us to believe that there would be a loss of convenience for some customers as a result of the introduction of the POSP. We concluded that experiments conducted by the parties all suffered in varying degrees from problems of design, implementation and/or timing which meant that we did not rely on them to estimate the impact of the loss of convenience from introducing a POSP. Further, this evidence and other evidence provided by the parties does not isolate the value of loss of convenience from other factors which might cause a fall in distributors' take-up rates. We have carefully considered the arguments and evidence put forward by the parties and concluded that they are overstating the loss of convenience that would result from the introduction of a POSP even before taking account of the benefits of the remedy package.

5.89 Evidence from customer research indicates that some consumers will experience a loss of convenience; other consumers would prefer to have a gap between purchases of credit and PPI and would experience a positive benefit from the introduction of a POSP. The Accent survey, which we used for our base case in our modelling in Section 7, found that for PLPPI, 60 per cent of customers said they preferred to buy PPI at the same time as credit, whilst 31 per cent said they would prefer to buy it later. For MPPI, 50 per cent of customers said that they preferred to buy PPI at the same time as credit, whilst 36 per cent said they would prefer to buy it later.

5.90 Our modelling, using inputs from the Accent survey, suggests that, without the benefits of competition which we expect with the remedy package, the introduction of a POSP would result in a drop in take-up rates of around 20 per cent for PLPPI, and of less than 5 per cent for MPPI. Whilst these figures are lower than the estimates of reduction in take-up put to us by the parties, in our judgement there are reasons which explain the differences (see paragraphs 5.28 to 5.31 and 5.39).

5.91 In terms of the cost of loss of convenience, the Accent survey found for PLPPI that the value of taking out PPI at the credit point of sale was £9.00 per month when compared with calling back after 24 hours and £7.30 per month when compared with being called after seven days, compared with a mean monthly PLPPI premium of £30.50 per month. Those MPPI customers who preferred to buy PPI at the credit point of sale did not attach a statistically significant value to this preference. For those customers who expressed a preference for buying PPI either 24 hours or seven days after the credit point of sale, PLPPI customers expressed a willingness to pay £25.20 a month more to buy it seven days after the credit sale, and £19 per month more to buy it 24 hours after the credit sale. For MPPI customers, the equivalent figures were £30 and £18.70 per month.

5.92 As noted in paragraph 5.6, this analysis does not take account of the static or dynamic benefits that we expect from the introduction of competition into PPI markets as a result of the remedy package. We consider what will be the overall impact on sales and customer welfare, taking into account all of the effects of the remedy package, in Sections 7 and 8.

6. Parties' plans

6.1 We looked next at what parties would do if a remedy package including a POSP were put in place. Because our 2009 report was challenged and we are undertaking a remittal, we are in the unusual position of being able to look at how parties reacted to the 2009 report in terms of developing new products. We thought that this evidence was useful in gauging parties' internal views on the scale of any reduction in convenience—if parties intended to continue supplying PPI we thought that they must take the view that the reduction in sales likely in a world where remedies, including a POSP, were put in place would not be so large as to render the supply of PPI uneconomic.

6.2 We asked parties for internal documents relating to their reactions to the remedies set out in our 2008 Notices of Possible Remedies, our 2008 provisional decision on remedies and the 2009 report. We looked at these to understand parties' plans, and to enable us to take a judgement on the extent to which parties were likely to remain in the markets for supply of PPI if a POSP were put in place.

6.3 We set out the evidence we found on parties' intentions in Appendix G. We summarize our findings here.

Consideration of the opportunities available

6.4 We found that all the main parties to our investigation have been actively considering for some time how to respond to the remedies we were either considering or that we set out in the 2009 report. The parties had also responded to the FSA's action on single-premium PLPPI.

6.5 Several parties showed us customer research they had conducted. Highlights from this research are summarized in Table 6.1. This evidence indicates that they found consumers to be strongly supportive of the development of short-term IP products, with consumers valuing the flexibility and choice that these products would give them.

TABLE 6.1 **Research related to the introduction of short-term IP products**

Distributor	*Research comments*
[✂]	Respondents generally reacted positively to the proposition of covering income People liked idea of cover being centred around their income rather than their outgoings—they retain control of their bills Seen as a product which protects their lifestyle
[✂]	The key strengths of the proposition that was tested were the related elements of: • Flexibility/tailoring of cover in relation to needs—which improves perceptions of value and cover quality • Focus on lifestyle—which improves and widens appeal and relevance • Its perceived status as a stand-alone product—which instils more confidence in the purchase/sales process
[✂]	Market research indicated that customers would also like a more flexible product that covered more than their loan repayments. This product would be similar to a Lifestyle or Bill Protector product and would allow customers to protect their monthly outgoings which could include payments such as mortgages, loans and utility bills. However this would be the subject of future discussions with [✂].
[✂]	The customer research revealed that customers perceive real value in the areas covered by PPI and that they would welcome a new product that will give confidence and peace of mind in this challenging economic time. The research suggested that the new product should offer more flexibility and transparency than PPI and should represent good value for money. There would be real value in a product offering protection of income rather than being related to a credit product. There appears to be a strong rationale to launch short-term IP—the format tested does appear clear and understandable. Keeping descriptions clear and simple help to differentiate and distance from PPI. Combating PPI mistrust and generating explicit rationale. The call to action is helped by its stand-alone nature; this should be emphasized.
[✂]	A research presentation in April 2009 concluded that a menu-driven protection product was likely to be popular, with the opportunity to receive discounts for multiple policies, the opportunity to mix short- and long-term cover, and the flexibility to tailor the cover to a customer's needs being attractive features.

Source: Parties' internal papers.

6.6 An internal [✂] document noted a benefit of selling PPI away from the point of sale: 'The quotation and application sales process provide customers with suitable time to "walk away" and think about the policy without being pressurised into purchasing cover'.[69]

6.7 LBG noted that there were potentially many more opportunities to sell a product not directly related to an underlying credit product. It identified that there were up to [✂] million branch interviews that did not involve the sale of a credit product compared with less than half that number of branch interviews ([✂] million) where a credit product was discussed/taken out.

6.8 We noted other documents from some parties commenting on the opportunities available. For example, an internal [✂] document noted that: 'There is a significant revenue opportunity in providing payment protection to customers, outside of the process for selling and fulfilling credit products. Current modelling predicts £120Million pa, (income after claims)' (July 2009). An internal [✂] document said that its new product project 'creates commercial opportunities in both new and existing markets for new and existing products'. An internal [✂] document said:

> The proposed CoCo remedies will introduce measures to drive comparison and switching behaviour—more akin to other GI products. It is expected that this will open up opportunities to acquire customers through different approaches, separate to the traditional associated credit product.

[69] [✂] said that the context for this was that it was written specifically for the purposes of obtaining sign-off [✂] from the [✂] marketing department, and that it did not constitute an internal view on whether or not customers felt pressured into purchasing PPI.

6.9 We obtained data from GfK NOP Consumer Services (GfK)—from its FRS survey—on the number of different financial institutions with which consumers have a relationship. The data is shown in Table 6.2.

TABLE 6.2 **The number of financial institutions with which customers have relationships**

per cent

*Number of relationships with financial institutions**	*Total (all 18+)*	*PPI: MPPI customers*	*PPI: CCPPI customers*	*PPI: PLPPI customers*	*PPI: SMPPI customers*	*PPI: Mail order loan customers*	*PPI: Any form of PPI*
None	1	-	-	-	-	-	-
1	17	3	6	8	6	2	5
2	20	10	16	17	13	21	14
3	18	17	17	19	17	24	18
4 or more	41	71	62	57	63	52	61
Total†	100	100	100	100	100	100	100
Average number of relationships	3.6	5	4.5	4.1	4.6	4.2	4.5

Source: GfK FRS database.

*Financial institutions have been grouped by brand ownership, so that if a customer has a relationship with both Lloyds TSB and HBOS, for instance, this counts as only one relationship.
†Sums do not quite equal 100 per cent due to rounding.

6.10 This shows that 18 per cent of the overall population have relationships with one financial institution or none, whereas 82 per cent have relationships with two or more financial institutions. PPI customers tend to have relationships with more financial institutions, with only 5 per cent of PPI customers overall having a relationship with only one financial institution.

6.11 On average, PPI customers have relationships with four or five different financial institutions.

6.12 Data from GfK also showed that there is significant scope for cross-selling. For example, 59 per cent of PLPPI customers also have a credit card and 22 per cent also have a CCPPI policy. And as noted in paragraphs 6.9 to 6.11, most PPI customers have multiple relationships with credit providers, optimizing the opportunities for them to be approached by distributors to buy PPI even if they do not hold credit with that provider. The evidence suggested to us that the cross-sales opportunities for distributors are significant.

Responses of the main distributors

6.13 We looked at how the various main parties to the investigation responded to our likely remedies. We looked at how retail banks, monoline credit card providers, underwriters and stand-alone providers responded.

6.14 The internal documents we received indicated that [✂] the retail banks that are main parties to this investigation reacted to the remedies we considered by developing new products. These products were often ones that are not linked to a specific credit product but offered wider and/or more flexible cover. The products were also often designed with sale to a distributor's non-credit customers (or sale to customers with whom they had no existing relationship) in mind. Table 6.3 summarizes the new product development work conducted by the retail banks that are main parties to this inquiry. In July 2010, LBG announced that it was stopping selling PPI—see paragraph 4.31 and Appendix G. Having considered all the evidence from LBG, we believe that LBG is likely to re-enter the market once the remedy package is in place.

This judgement is based on what LBG told us, the extensive work already done on looking at a replacement product and the continuing work on this, and the significant opportunities available to it to sell a product to its customers that it considers to be valuable to them.

TABLE 6.3 **New income protection initiatives—retail banks**

Company	*Product/project*	*Covers*	*Present status*	*Comments*
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]

Source: Parties' internal papers received in January 2010.

6.15 In terms of the main credit card companies (Capital One and MBNA), we found the following strategies for responding to the CC remedies.

6.16 [✂]

6.17 [✂]

Responses of underwriters

6.18 In terms of underwriters, we saw evidence that [✂] have been active in marketing short-term income/lifestyle protection products to the distributors, with products that are menu driven for the customer to select from options that vary from protection against specific loan products to more general IP. [✂] saw the development of these products as necessary to address the needs of distributors for a more flexible income-based product.[70] [✂] also appeared to have been considering alternative products but appeared less advanced in its thinking. [✂] appeared to be taking a less dynamic approach to the new environment for PPI although [✂].

Stand-alone providers

6.19 As noted in Appendix A, we found at least five companies (Ant Insurance, Columbus Direct, Wessex Group, Millennium Insurance and MMS) which had introduced new products, branded as PPI, short-term IP or Lifestyle protection, after the publication of the 2009 report. As also noted in Appendix A, Post Office Financial Services (POFS) and Churchill Insurance Company Ltd have exited the stand-alone market since the 2009 report was published. Other stand-alone providers remain in the market and, if the CC's remedies are introduced, in our view have the incentive to seek to expand as they will be able to attract customers who are searching the market before buying a policy, rather than seeking to attract switching customers or customers who have had credit without insurance for some time but think they may be liable to need insurance (and therefore be more likely to claim).

The stand-alone market

6.20 We also looked at who would take part in the stand-alone market.

[70][✂]

6.21 We noted in paragraph 6.19 that, although there had been new entrants, there had also been some parties that had stopped offering stand-alone PPI or reduced their product offering, and in Appendix A we found that the number of stand-alone policies sold in 2009 had almost halved compared with 2008 levels.

6.22 We also noted that there was a different type of stand-alone PPI provider that could supply customers—distributors which currently offer PPI at the credit point of sale. As noted in paragraphs 6.14 to 6.17, we found that several distributors that are main parties to this investigation (including [✂]) have been developing policies that can be sold to their non-credit customers, and to customers with whom they do not currently have an existing relationship. Cardif Pinnacle told us that online providers were preparing for a world where remedies were in place.

6.23 Some parties, such as Aviva,[71] told us that a stand-alone market would not develop because of concerns including adverse selection, customer inertia and financial capability. RBSG[72] said that the comments in our provisional decision regarding the exit of some traditional stand-alone providers, and the fact that the CC considered that a key development was that large PPI distributors would enter the stand-alone market, represented a material change in the competitive environment.

6.24 We considered some of the points made by Aviva in the 2009 report—see paragraphs 10.23 to 10.28 on adverse selection and 10.487 on creating a remedy package which would increase the number of consumers shopping around. In terms of financial capability, the remedy package includes measures which provide customers with useful information, including about how to access the CFEB's moneymadeclear website, which is a source of impartial information about insurance. We are also recommending to CFEB that it populates its tables with PPI price and features information as we believe that the tables with this information will help to increase customer awareness of price and features of PPI. In our view, these measures will help increase customers' financial capability and confidence when making decisions about PPI. Further, as customers become more used to having choice of PPI products in a competitive marketplace, and have better information about the options available, this will strengthen their capability to exercise such choice.

6.25 We were not persuaded by RBSG's argument that the identities of the providers who were planning to enter the stand-alone market represented a material change in the competitive environment. In the 2009 report, we concluded that it was necessary to introduce a remedies package that would lead to a new, more competitive, market structure (paragraph 10.72 of the 2009 report), and in paragraph 10.479 of the 2009 report we said that we expected one effect of our remedies across all PPI sectors would be to increase substantially the competitive constraint posed by stand-alone PPI in relation to all types of PPI. We remain of that view, and believe that the products under development by distributors may be expected to form a significant part of that constraint if they do come to market—but we cannot be sure that these products will come to market without the introduction of a POSP. We see no reason therefore to consider this as a material change that should cause us to change our assessment.

Conclusions on parties' plans

6.26 We concluded that most large distributors reacted to the possibility of a POSP being introduced by developing products they could sell with a POSP in place. Those prod-

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[71] Aviva response to provisional decision, p2.
[72] RBSG response to provisional decision, sections 1.3 and 2.1.1.

ucts were a mix of traditional PPI and, largely, short-term IP products.[73] The work conducted, and the views on market opportunities, show that nearly all the main parties to our investigation have actively considered how they could sell PPI products with a POSP in place. We considered this evidence carefully, and we concluded that we expected those main parties to stay in the market, offering the products they have been developing to their credit customers, if a POSP were put in place. The exception to this is [✂].[74] Whilst LBG has stopped selling PPI for the time being, the internal documents we have seen, and what it has told us, led us to conclude that it is likely to re-enter the market once the remedy package is in place (see paragraph 6.14).

6.27 In terms of stand-alone provision, the evidence suggested to us that, with the remedy package in force, we would expect some of the traditional stand-alone providers to remain in the market (with underwriters supporting them), although we noted that there have been some recent exits as well as some recent new entries. There would, however, be, in our view, a key development: large PPI distributors would enter the stand-alone market. For customers this would mean that suppliers which have been providing most PPI policies will now be making stand-alone offerings available, increasing choice and increasing the number of household names offering them stand-alone policies. This gave us added confidence that, with the remedy package in place, there would be competition between PPI providers.

7. Modelling the effects of intervention

Summary

7.1 We revisited our model of the effects of intervention to take account of the issues the Tribunal asked us to include in it, including the loss of convenience to customers of not being able to purchase PPI at the credit point of sale.

7.2 We revisited the base case assumptions for inputs to the model—relating, in particular, to the extent to which excess profits were passed through to customers in the form of lower credit prices (‘the waterbed effect’), the elasticity of demand for PPI and the costs to customers of the loss of convenience.

7.3 Using reasonable, and in some cases particularly conservative, assumptions, we found that the implementation of the remedy package resulted in positive benefits for consumers even after allowing for the costs of the loss of convenience and implementation, and any adverse effects associated with the loss of a relevant customer benefit of lower credit prices. This was even before taking account of the dynamic benefits that we would expect from more competitive PPI markets.

7.4 We also conducted sensitivity tests around this base case. Under some assumptions, the model predicts that the remedy package could have an overall negative effect on consumer welfare. However, we were confident that these scenarios were unlikely because:

- other factors, such as our conservative assumptions on customer myopia (the extent to which customers will search the market for PPI products with the remedy package in place), only needed to be relaxed a little in order to outweigh the negative associations of any one of the assumptions that could give rise to welfare detriment; and

[73] Which, as we noted in paragraph 4.38, are a form of PPI.
[74] [✂]

- the assumptions required were a long way from our central assumptions and unlikely to occur—and by extension even more unlikely to occur in combination.

Introduction

7.5 In this section we revisit our model of the effects of intervention, used in the 2009 report, to take account of the issues the Tribunal asked us to include in it, including the loss of convenience to customers of not being able to purchase PPI at the credit point of sale. The section is structured as follows:

- we set out the model developed in the 2009 report and how we use it here (paragraphs 7.6 to 7.14);
- we set out the changes we made to the model's inputs, both those requested by the Tribunal and those made to make use of more up-to-date data on the market (paragraphs 7.15 to 7.70);
- we look at the results of the model (paragraphs 7.71 to 7.95). Within this we look at the results of the model in the base case (paragraphs 7.72 to 7.74), and conduct a series of sensitivity checks to our base case and look at the likelihood of negative impacts occurring for each of the products (paragraphs 7.75 to 7.95); and
- finally we conclude on what our modelling tells us (paragraphs 7.96 and 7.97).

The model developed in the 2009 report and its use here

7.6 The Act[75] enables the CC to have regard to the effect of any action it proposes to take on any relevant customer benefits of the feature or features of the market concerned. In the 2009 report we found that credit prices for personal loans (secured and unsecured), mortgages and credit cards were lower than they otherwise would have been because of PPI income generated at the credit point of sale. This phenomenon is sometimes referred to as a 'waterbed effect'. We further concluded that these lower credit prices were a relevant customer benefit within the meaning of the Act (see paragraphs 10.458 to 10.460 of the 2009 report).

7.7 In the 2009 report, we used a series of models in order to help us decide whether to modify our remedies to preserve this relevant customer benefit and to quantify the scale of the static consumer benefits arising from our remedy package, after taking into account the possible loss of relevant customer benefits in credit markets. The modelling approach in the 2009 report (and the results from the modelling) were presented in paragraphs 10.480 to 10.496 and Appendices 10.9 to 10.11 of the 2009 report.

7.8 We decided to use a similar approach to modelling static consumer benefits as was used in the 2009 report. In brief, the models we developed simulate the effects of the remedies on markets for PPI and credit.

7.9 To this end, we assumed that, before remedies, a number of distributors competed in the markets for credit but were effectively monopolists over PPI sales to their respective credit customers. This assumption reflected the considerable evidence in the 2009 report about the limited competitive constraints facing PPI distributors (see, for

[75] Section 134(7) and (8).

example, paragraphs 3.139 and 4.96 of the 2009 report), which our analysis of developments in the market since the 2009 report found remained the case (see paragraph 4.71). We also assumed that, before remedies, there was a waterbed effect, so that some or all excess profits on PPI were passed on to credit consumers in the form of lower credit prices. We then analysed the effects of remedies in these models by examining what happens when the price of PPI reduces to the level which removes excess profits.

7.10 As in the 2009 report, we continued to use as our base case for modelling the effects of the remedy package, a model where we assumed that all consumers are 'myopic', both before and after the remedies, in the sense that they do not anticipate the price of PPI prior to making decisions about credit.[76] We acknowledge that this is not a realistic assumption, not least because there is evidence that some consumers currently search for PPI before the point of sale of credit.[77] We also expect that the remedy package will increase this type of search: in paragraph 10.487 of the 2009 report we noted that none of our remedies was aimed at reducing PPI prices without also improving the ability to search for the PPI price at the same time as the credit price, and we were confident that we would not be in a situation of imposing an effective remedy which had no impact on search. This assumption should therefore be thought of as a simplifying assumption, which reflects a cautious approach to the modelling of benefits as it tends to understate the benefits of intervention.

7.11 The Tribunal, in its decision, asked us to include certain factors in the model used for the quantification of static consumer benefits from the remedy package, and therefore we modified some of the inputs and some of the assumptions in the modelling. We also updated some of the inputs of the model to reflect more recent market conditions (in particular, margins, excess profits, penetration rates, price of PPI relative to credit and the extent of the waterbed). We conducted a consultation on the changes to the models, and our approach was informed by the responses we received.

7.12 As in the 2009 report, we were unable to use this modelling exercise to quantify the dynamic benefits that we expect to result from the remedy package, but we updated our analysis of the scale of static benefits after taking into account effects in credit and PPI markets. By their nature, many of the dynamic benefits of introducing competition to PPI markets through the remedy package cannot be anticipated in detail. We expect the remedy package to generate the following categories of dynamic benefits, over and above the purely static effects included in the modelling (see paragraph 10.493 of the 2009 report):

(a) arresting any decline in the size of the PPI sector that results from the current lack of competition, for example negative publicity associated with high prices and issues around sales quality;

(b) increased advertising and far more interest in (and awareness of) the sector, such that the demand for PPI should increase once it is sold at competitive prices; and

(c) selection pressure, encouraging companies that develop products which benefit consumers and punishing those that develop poor products.

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[76] In the 2009 report, the model that embedded this assumption was referred to as the 'non-system model'.
[77] See Table 3.2 of the 2009 report and p33 of the Accent report and paragraphs 42–44 of Appendix I; moreover, as noted in paragraph 26 of Appendix E, research conducted for [✂] showed that [10–20] per cent of customers who received a quote but did not make a purchase during a pilot of a POSP-style sales process said that they searched for and compared products elsewhere.

7.13 These types of benefits are inherently difficult to quantify: the introduction of competition into a market will fundamentally change the dynamics of the market including the ways in which customer choice drives innovation and the quality of the products that are offered, but while we expect this process to be beneficial, we cannot predict the precise way in which any market will develop with competition (we were able to note, however, the parties' planned innovations in response to the 2009 report, set out in Section 6, which gave us confidence that, with the remedy package in place, there would be competition between PPI providers).

7.14 Although we were not able to quantify these dynamic benefits, we noted that the decline in the size of the PPI sector since 2002, which in our view results to a significant extent from the negative publicity surrounding the market, has been substantial.[78] The PPI sector has built up a negative reputation for both overpricing and sales quality issues over more than a decade. While this perception may prove difficult to shift, we would expect consumer perceptions of the market to improve with experience of increased competition as providers start to offer better value for money, as fewer sales quality issues are associated with selling PPI at the credit point of sale and as improved value for money is reflected in lower prices and higher claims ratios. These improved consumer perceptions are likely to stimulate demand. In such circumstances, we would expect material reputational benefits to be seen within the first five years of all elements of the remedy package coming into force (see Appendix M). This suggested to us that benefits resulting from arresting the decline in the size of the PPI sector resulting from the negative publicity, which is just one of the dynamic benefits that we expect to result from increased competition, could be very large.

Changes to modelling inputs requested by the Tribunal

7.15 The Tribunal, in its decision, asked us to include the following factors in the model:

- the one-off and ongoing costs of implementation;
- marketing costs;
- the loss of convenience to consumers from not being able to purchase PPI at the same time as credit; and
- an elasticity of demand of the type derived from an assumed price change by all players in the relevant market, rather than of a type appropriate when considering a price change implemented by a single distributor within a competitive market which included other distributors.

7.16 We set out here how we addressed each of these issues, as well as other changes which were put to us by the parties. Details of the modelling are set out in Appendices H, I and J.

Costs of implementing the remedies and marketing costs

7.17 We set out an assessment of the cost of implementing the remedy package in paragraphs 10.497 to 10.508 of the 2009 report.

[78] See Table 2.5 of the 2009 report: between 2002 and 2007, PLPPI penetration rates dropped from 62 to 40 per cent; MPPI penetration rates from 26 to 10 per cent; CCPPI from 33 to 21 per cent; SMPPI from 83 to 56 per cent.

7.18 During the remittal we received internal documentation from the parties which provided the largest estimates of costs of implementation in the 2009 report, which allowed us to update some of these estimates. Our analysis of this is set out in Appendix K.

7.19 In light of the new evidence available to us we concluded that the one-off costs of implementing the remedy package in relation to PLPPI, MPPI, CCPPI and SMPPI would be in the range £61–£69 million with ongoing costs of £37–£42 million per year.

7.20 We split the costs of implementing the remedies between PLPPI, MPPI, CCPPI and SMPPI according to the proportion of new policies sold in a year, using the number of PLPPI, MPPI, CCPPI and SMPPI policies sold in 2007. The results are set out in Table 7.1. On the basis of these calculations, we attributed 48 per cent of the costs of implementing remedies to PLPPI, 37 per cent to CCPPI, 12 per cent to MPPI and 2 per cent to SMPPI.

TABLE 7.1 **Proportion of new policies sold for different product types**

Type of PPI	*Number of policies sold*	*Proportion of all policies sold*
PLPPI	1,667,123	48
MPPI	427,354	12
CCPPI	1,293,514	37
SMPPI	78,524	2
Total	3,466,515	100

Source: CC based on data provided by the parties.

7.21 We noted in paragraph 10.503 of the 2009 report that most of the set-up costs were for IT system changes (likely to be largely fixed costs); whereas most of the ongoing costs related to marketing and communication (likely to be largely variable). We saw nothing in internal documentation during this remittal to indicate that this had changed.

7.22 In so far as most ongoing costs appeared to be variable, these could be expected to be reflected in the pricing of PPI, and therefore we added the estimated ongoing costs of implementation to our calculation of the unit price of PPI after remedies in the model. Details of how we did this are in Appendix I.

7.23 We found that adding the ongoing costs of implementation of the remedies to the existing costs of selling PPI, the average cost per policy increased by between 1 per cent (for SMPPI) and 6 per cent (for CCPPI).

7.24 We also included an allowance for marketing and advertising costs to increase after the remedies are in place, and for these additional costs to be included in the price of PPI after the remedies (as these are ongoing costs). To do so, we examined evidence on advertising-to-sales ratios in related industries to get an order of magnitude for the level of marketing and advertising that might be expected to take place after the remedies are in place (see paragraphs 109 to 111 of Appendix I). We were conservative in our approach to marketing and advertising: we would expect marketing and advertising to result in an increase in PPI sales (by raising awareness of PPI away from the credit point of sale, for instance). However, the model only takes into account the costs of advertising and marketing without also modelling the resulting benefits, in terms of an increase in PPI demand, which could be expected to occur as a consequence.

7.25 We used the estimates of the unit ongoing cost of implementing the remedies and of marketing and advertising in our calculation of the price for PPI after the remedy package is in place.

7.26 Regarding the one-off implementation costs of the remedies, a number of parties told us, in response to the modelling consultation, that one-off implementation costs might in future be passed on to consumers, and should therefore be taken into account in the modelling in the form of higher costs after the remedies. Barclays told us that spreading the one-off costs over a number of years would be the appropriate way to model the impact of the one-off costs on PPI pricing.

7.27 We did not agree that one-off costs would be reflected in PPI pricing. Indeed, we would not normally expect one-off fixed costs to be passed on through higher prices to consumers, unless the one-off implementation costs affected the long-term profitability of selling PPI. The evidence from distributors' plans did not suggest that this was the case: we concluded in paragraph 6.26 that we expected nearly all the main parties to stay in the market, offering the products they have been developing to their credit customers, if a POSP were put in place. We asked distributors for evidence of where they had passed through the one-off costs of changes required by regulation to consumers, but we received no such evidence in response. We therefore did not incorporate an allowance for the one-off costs of implementation in our calculation of the post-remedy unit price in the model. Instead, we used the model to calculate a net benefit or detriment to consumers, and compared that number with the one-off implementation costs (see paragraphs 8.88 to 8.90).

7.28 We also conducted a sensitivity analysis to see whether the inclusion of one-off costs into the pricing of PPI after the remedies would change the results of the modelling. To do so, we included an allowance for the one-off costs in the average cost pricing after the remedies, so that the one-off costs are spread over a period of three to five years. The results are in Appendix J; we found that including the one-off costs does not materially change the results from the modelling. We were therefore able to conclude that whether we included the one-off costs within the model or took account of them outside the model did not make a difference to our conclusions on proportionality.

The loss of convenience

- *How we modelled loss of convenience*

7.29 We set out the details of how we modelled the impact of the loss of convenience with the remedy package in place in Appendix I. We modelled the loss of convenience as a cost to those PPI consumers who prefer to buy PPI at the credit point of sale: at any given PPI price, the surplus that these consumers derive from PPI will decrease due to the cost of loss of convenience, so that the demand for PPI by these consumers reduces at any given PPI price. We refer to this effect in the model as representing a downward shift in the demand curve.

7.30 Using this approach to modelling, we find that if, for instance, the costs from the loss of convenience are equal on average to 10 per cent of the current price of PPI for all PPI consumers, the downward shift in the demand curve would be such that we would expect, without taking account of the benefits of our remedy package, a reduction in volumes of PLPPI purchased of about 15 per cent at constant PPI prices and constant credit volumes.

7.31 To model the change in demand for PPI with and without remedies, in the base case model we continued to assume that all consumers are 'myopic', that is they do not anticipate the reduced price of PPI when making decisions about credit. We extended the model so that we were able to relax this assumption, bearing in mind that we know this is not the case for all customers even before the remedy package is in place (see paragraph 7.10).

7.32 We used the results from the survey conducted for us by Accent to derive an estimate of the possible costs of the loss of convenience to consumers arising from the POSP. As noted in paragraph 5.63, for PLPPI and MPPI consumers, the Accent survey found that, on average, consumers associate the delay between credit and PPI purchase with a monetary gain rather than a cost. Therefore, the results from the Accent survey would suggest that the demand for PPI would increase (at a given PPI price) rather than decrease after the remedies are in place

7.33 Further analysis of the Accent results showed that there were broadly three categories of PPI consumers (see paragraph 5.64):

- those who prefer to buy PPI at the point of sale of credit (all other things being equal), and who associate a cost with the delay in the purchasing of PPI;
- those who prefer to buy PPI after a delay of 24 hours or seven days, and who associate a monetary gain with the delay in the purchasing of PPI; and
- those who are indifferent between buying at the point of sale and buying after a delay, and who do not associate any significant cost or gain with the delay in the purchasing of PPI.

7.34 Although the consumers who prefer to buy after a delay are fewer than those who prefer to buy at the point of sale of credit, the Accent survey suggests that their preference for delaying the purchase is stronger, which drives the average positive valuation for the delay. Given the diversity in consumer preferences around buying PPI at the point of sale of credit, we considered that using the average positive value associated with the delay in the purchase in the modelling would hide the fact that the POSP is likely to impact different consumers in different ways. We therefore decided to model the impact of the remedies on the three categories of consumers identified in paragraph 7.33. We modelled the PPI demand curve of three different categories of customers as follows (details are presented in Appendix I):

- those who prefer to buy PPI at the point of sale of credit (in the absence of the benefits of the remedy package): the demand for PPI of these customers reduces at any given price when the remedies are in place, to reflect the fact that these customers associate a cost with the delay in purchasing PPI;
- those who prefer to buy PPI after a delay of 24 hours or seven days: the volumes demanded by these consumers do not increase at given price, but the surplus derived from purchasing PPI by these customers increases at any given PPI price when they can buy after a delay, to reflect the fact that these customers associate a monetary gain with the delay; and
- those who are indifferent between buying at the point of sale and buying after a delay: the demand curve for PPI of these consumers is not affected by the delay introduced by the remedies.

7.35 We noted that there was also at least a possibility that some people who do not currently take out PPI at the point of sale might receive a personal PPI quote, consider the quote and decide to take out PPI even without any other changes (such as a change in price). This would be because those consumers would have time to consider the policy without responding to what they may perceive to be a pressured sales environment by automatically declining to take out the policy. The model does not take account of this potential beneficial effect of the remedy package and is, in this sense, conservative.

- *Parties' comments about our approach to modelling loss of convenience*

7.36 We received many comments about our approach to modelling the loss of convenience. These related to:

(a) the modelling of the loss of convenience for those customers who value the ability to purchase PPI at the credit point-of-sale; and

(b) the modelling of benefits for those customers who prefer delay.

7.37 Many distributors commented on our approach to modelling the impact of the loss of convenience on PPI demand and consumer welfare. Barclays and LBG told us that convenience should be modelled as a cost both to those who cease buying and those who continue buying. We agreed, and our modelling of the loss of convenience as a downward shift of the demand curve of consumers who prefer to buy at the point of sale addresses this concern: this means that, at given price, the surplus derived from buying PPI for consumers who prefer the point of sale will reduce, whether they decide to buy PPI after the remedies or not. The modelling therefore takes into account both the negative effect of a loss of convenience on quantities consumed by those consumers who prefer to buy PPI at the credit point of sale and who do not buy PPI if there is a delay, and the reduction in the surplus for those consumers who prefer to buy PPI at the point of sale but continue to take out PPI with a delay.

7.38 MBNA told us that, if convenience was modelled only as a cost, this would ignore the adverse effect on consumers who failed to take out insurance even though it would be in their interest to do so. We disagreed: consumers who fail to take out PPI are those for whom the cost of PPI in combination with any loss of convenience arising from the POSP exceeds the expected surplus they derive from consuming PPI. Because the model takes into account the possible impact of the loss of convenience on sales to consumers who prefer to buy at the point of sale, this effect is therefore taken into account. MBNA responded to this by saying that, if that were the case, it was clearly entirely disproportionate to restrict consumer choice by removing the option from customers to purchase PPI at the point of sale. It said that any such restriction would, almost by definition, result in a loss of consumer welfare, and that it could not see how the POSP could be a proportionate remedy if the CC took the view that consumers chose on the basis of properly assessed costs and benefits.

7.39 We agreed that, for those consumers who disliked delay, the POSP imposed a welfare cost and this was fully taken into account in the welfare analysis of the model. The purpose of the model is to help evaluate this negative effect in the context of the other effects, both positive and negative, of introducing the remedy package in respect of consumers as a whole. We did not agree with MBNA that restricting consumer choice by removing the option to buy PPI at the point of sale would by definition result in a loss in consumer welfare: the impact of the POSP on consumer welfare depends on whether the benefits from the remedies (such as, for instance, lower PPI prices) exceed the negative effects for consumers (such as the loss of convenience). We did not agree with MBNA that there was an inconsistency in assuming that consumers made decisions based on properly assessed costs and benefits.

7.40 LBG told us that the way in which we had taken into account the negative cost of delay in our modelling systematically understated the true welfare effect, because our approach ignored the impact of the remedy package on the ability of consumers properly to evaluate costs and benefits of protection. LBG said that the CC had failed to consider properly the various elements of convenience associated with the availability of PPI at the point of credit sale, and that such availability provided more than the avoidance of shopping around costs. LBG said that availability of PPI at the credit point of sale provided the consumer with the opportunity to evaluate protection needs at the perfect time—the moment before the consumer committed to a loan—and that after the remedies were in place, consumers would not have sufficient information on PPI at the credit point of sale and may therefore fail to consider it even though they would buy it if they had the information.

7.41 We were not persuaded by LBG's arguments. Our package of remedies is designed to increase the amount of information available to consumers at, and before, the credit point of sale. We believe that, after the remedies are in place, consumers will be in a stronger position to make an informed decision on PPI at the credit point of sale, given the extra information that will be available to them about their ability to obtain alternative products and the enhanced ease of searching for the best product for them.

7.42 In response to our provisional decision, a number of parties (including LBG) said that the modelling should not take into account the positive willingness to pay of some consumers for the delay, because this was not a benefit of the POSP. We were told by several parties, including MBNA and LBG, that people who expressed a preference for buying after the point of sale were already able to do so now.

7.43 In the 2009 report, we found that large distributors tended not to offer PPI for sale independently of a credit product and many consumers did not know that they could buy PPI from anyone other than the credit provider—survey evidence we saw showed that between 31 and 65 per cent of consumers did not believe that they could have gone to a different PPI provider (see paragraphs 5.52 and 5.53 of the 2009 report). Further, we found that around one-half to three-quarters of customers had not considered PPI before approaching their lender (paragraph 5.93 of the 2009 report). As shown in paragraphs 7.44 and 7.46, for PLPPI and MPPI some distributors do not allow customers to delay a PPI purchase, and others allow customers only a limited window of opportunity. For CCPPI (paragraph 7.47), it is more generally possible to buy CCPPI away from the credit point of sale but distributors do not generally make a point of telling their customers of this option. The evidence suggested to us that customers are offered PPI at the credit point of sale but are not encouraged to go away and think about it and come back—indeed in our judgement the incentives on sales staff of all PPI products are to complete the sale of PPI at the same time as credit. In effect, customers are offered PPI as a 'now or never' option, so if they wanted to search around they would have to hope that they found alternative products that met their needs and were value for money.

7.44 In light of parties' suggestion in paragraph 7.42, we asked some providers about the extent to which customers could buy PPI after the credit point of sale. In terms of regular-premium PLPPI:

- LBG told us that when Lloyds TSB offered regular-premium PLPPI, its customers could not buy PLPPI after drawdown of credit due to system constraints.

- LBG also told us that when HBOS offered regular-premium PLPPI, its customers could buy PLPPI up to 28 days after drawdown of credit; the 28-day limit was a business decision.

- Santander said that customers were not able to take out PLPPI after the credit point of sale. It said that this was because of an increasing risk of adverse selection after the credit point of sale.

- Barclays said that in relation to its previous PPI products customers were given a quote for PLPPI at the credit point of sale which was valid for 30 days, and that they could take out PLPPI for up to 30 days after the sale of credit. It said that the 30-day limit was chosen as it would be the same as the length of time for which the credit quotation was valid, and prevented the two products from being misaligned.

7.45 Although it may now be more straightforward to return to a credit arranger to purchase PLPPI or SMPPI after the credit sale as a result of the removal of single-premium PPI, we do not consider that this change will in itself have increased customer awareness of the possibility of making such a delayed purchase—as noted in paragraph 7.43, the regular-premium PLPPI providers we asked generally told us that its availability after the credit point of sale was very limited.

7.46 In terms of MPPI:

- LBG told us that customers could take out Lloyds TSB MPPI products sold until the suspension of all PPI sales at any time. Customers could take out HBOS MPPI products sold until the suspension of all PPI sales at any time until the drawdown of credit, which it said could be up to three months after the mortgage offer.

- Santander said that its MPPI product was available through intermediaries at the credit point of sale and within 30 days of the mortgage completion date. It said that the cut-off was imposed by its underwriters because of the risk of adverse selection. Santander said that its retail customers could take out MPPI at any time to cover a Santander mortgage.

- Barclays said that in relation to its previous PPI products a decision on whether to buy MPPI as quoted alongside a mortgage quotation had to be taken when the mortgage application was submitted for processing. However, MPPI was available to customers on an ad-hoc basis if a stand-alone enquiry was made.

7.47 In terms of CCPPI:

- LBG said that its customers could take out CCPPI at any time during the life of the credit card. It did not explicitly tell its customers at the credit point of sale that they could. It told us that customers could not return to branches to take out CCPPI, but that they would be offered CCPPI on activation of the card.

- Barclays told us in relation to its previous PPI products that its CCPPI product was available to its credit card customers at any time. It said that it did not explicitly announce to customers that they were able to purchase CCPPI at any unlimited point in the future, simply because it was never suggested otherwise.

- MBNA said that its customers could take out CCPPI at any time; it said that there was no reference to time limits (or the lack of time limits) in which to take out CCPPI in any internal or external communications, the focus being on telling customers that it was an optional product.

- Capital One said that its customers could take out CCPPI at any time. Its customers were told this if they asked.

- Santander said that CCPPI was not available to its retail distribution customers after the credit point of sale, with the exceptions of selected customers who were able to take out PPI with a post-credit application through outbound telemarketing conducted by a third party provider.

7.48 In our judgement the current market structure does not give parties the incentive to make their customers aware of the ability to delay a purchase, and many customers do not know that they can buy PPI elsewhere. To the extent that they do, the evidence suggests that in many cases they can only do so if they decide not to buy the credit arranger's PPI product or have only a small window of opportunity to find an alternative policy before they lose the ability to buy the credit arranger's product. By contrast, the evidence that we saw from parties' future plans suggested that large PPI distributors were intending to enter the stand-alone market, if our remedy package including the POSP were put in place (see paragraph 6.27). We thought that this development, in combination with the operation of the POSP, would significantly increase customer awareness of the possibility of making such a delayed purchase, compared with the current situation.

7.49 We therefore thought that it was appropriate to take into account the positive willingness to pay of some consumers for the delay, as a relevant benefit of including the POSP in the remedy package.

7.50 HSBC, LBG and RBSG told us that there would be some double counting if we took into account the positive valuations of the delay by consumers who prefer a delay. This was because some consumers who valued a delay may include, in their valuation of the delay, the expectation that they would be able to buy PPI at a lower price if they delayed the purchase and shopped around. HSBC argued that this, together with all its other concerns regarding the willingness-to-pay results from the Accent survey meant that we should therefore not take into account any of the positive willingness to pay for the delay, whereas LBG said that in its view, for almost half of the respondents the CC's use of the Accent results involved double counting with the additional welfare gains of price cuts, and suggested that we only take into account the positive willingness to pay for the delay for consumers who said they preferred the delay because of reasons other than for shopping around.

7.51 The Accent survey was designed to estimate consumers' willingness to pay for a delay, or for buying at the credit point of sale, at a given price. In principle, therefore, we would not expect the willingness to pay results to include an expectation of a lower price by consumers. However, we recognized that in practice some consumers may have factored this in to their responses. We thought this might be the case for those consumers who said that they preferred a delay because it gave them the ability to shop around for PPI (and who gave no other reason for this preference). Even then, we did not think that these consumers' valuation of the delay would only reflect the discount they expect to obtain by shopping around; there are other benefits to consumers from shopping around than the expectation of a better price (such as product characteristics and quality of the product, and being able to satisfy themselves that they had obtained good value for money). Moreover, the fact that a respondent only mentioned the ability to shop around as a reason for preferring the delay does not necessarily mean that this consumer does not perceive other benefits to the delay (time to think, etc).

7.52 We therefore decided not to take into account the positive valuations for the delay by those consumers who said that they preferred a delay only because it gave them the ability to shop around. This represented 32 per cent of PLPPI consumers who preferred to buy after a delay, and 39 per cent of MPPI consumers who preferred to buy after a delay. We therefore discounted the positive willingness to pay in the model, so as not to include the valuation of the delay by these consumers. (In practice, for PLPPI we therefore assumed the willingness to pay for the delay by consumers preferring a delay was 68 per cent of the value found from the Accent survey; for MPPI, we assumed the willingness to pay for the delay was 61 per cent of the value found from the Accent survey.)[79] We also conducted sensitivity checks around this figure. We did not believe, however, that we should completely discount the positive willingness to pay for delay. At present, credit consumers often are not aware that they can buy PPI elsewhere (see paragraphs 13 to 16 of Appendix 3.4 of the 2009 report), and even if they were, their ability to do so is very limited given the current lack of availability of PPI outside of the credit point of sale (see paragraph 3.40 of the 2009 report and paragraphs 7.43 to 7.47). Therefore, we thought that the ability to delay the PPI purchase was a benefit from our remedy package for at least some customers, and that our cautious approach was a reasonable and appropriate way of accounting for the effect, drawing on the evidence that we had seen.

Elasticity of demand for PPI

7.53 The model in the 2009 report used the firm-level price elasticity of demand for PPI to estimate the impact of a general reduction in the price of PPI after the remedies on the aggregate demand for PPI. The Tribunal said that we should have used a different elasticity of demand in the model, namely the market-level price elasticity of demand for PPI.

7.54 We agree that, in principle, the market-level price elasticity of demand is the correct measure to be used in the modelling. The difference between the market-level price elasticity and the firm-level price elasticity is determined by the extent to which sales are diverted to or from other PPI sellers in the event of a price change, rather than lost to the market. For example, if a PPI distributor increases PPI prices, the overall effect on this distributor's sales of PPI (ie the firm-level elasticity) will be a combination of the market level substitution (amount of sales which are lost to PPI) and cross-substitution (amount of sales which are diverted to a different PPI distributor). Although there are no direct estimates of the market-level price elasticity of demand for PPI, the evidence suggests strongly that the proportion of consumers who will switch to a different PPI provider if their current provider increases prices by a small amount is very low. Indeed, it is this very lack of sales diversion to other PPI providers, which results from the point-of-sale advantage, which is at the core of the AEC, causing the firm-level elasticity to be so low, the prevailing price-cost margins to be so high, and the potential for the price reductions from competition to be so considerable. The evidence on elasticity of demand is presented in Appendix I.

7.55 For these reasons, we think that the market-level price elasticity of demand is currently very similar to the firm-level price elasticity of demand.[80] In the modelling, we therefore adjust the firm-level price elasticity estimates to allow for some limited cross-effects, such that the market elasticity of demand is 10 per cent lower than the firm-level elasticity of demand. We also conduct some sensitivity testing to check whether our results are robust to lower levels for the market elasticity of PPI demand.

[79] This is in fact equivalent to assuming that consumers preferring the delay only because of the ability to shop around are in fact indifferent as to whether they buy at the credit point of sale or later (at given price).
[80] We expect this to change when the remedies are in place: the increase in competition between PPI providers after the remedies are in place implies that firm-level elasticities will increase when the remedies are in place compared with the market elasticity.

Updating the inputs to the model

7.56 Many distributors put to us that we should update our analysis to account for recent market conditions. We set out what has happened in the market since our original investigation in Section 4 and Appendix A.

7.57 We updated the inputs to our model on margins, penetration rates, prices and excess profits to take into account more recent market conditions. Our general approach was to use averages over a number of years, rather than one-year data, for updating the inputs—therefore taking into account both periods of high credit and low credit sales. Our detailed approach to updating the inputs in the model is set out in Appendix I.

7.58 In our model we assumed that the remedy package would be substantially effective for PLPPI, MPPI, CCPPI and SMPPI markets (see paragraph 8.33), and therefore the extent of gross customer detriment being addressed (ie the level of excess profits) is a good indicator of the extent of gross customer benefit arising from implementing the remedies for these four products.[81]

The waterbed effect

7.59 In the 2009 report, we assumed a pass-through rate of excess PPI profits to lower credit prices of 80 or 100 per cent when illustrating the static consumer benefits arising from the remedy package. The assumption of 100 per cent pass-through was presented as being a cautious assumption: even if there was 100 per cent pass-through, we found that static consumer benefits from the remedies would be in excess of £200 million per year (see paragraph 10.494 of the 2009 report).

7.60 We reviewed the evidence on the extent of pass-through, and decided to use the 80 per cent assumption in our base case for the modelling. The reasons for using the 80 per cent assumption rather than the 100 per cent assumption are set out in Appendix I. In summary:

- We thought that the credit crunch and subsequent recession may have led to a reduction in the amount of pass-through from PPI markets to credit markets (see paragraphs 10.461 to 10.463 of the 2009 report).

- There was evidence from the parties' internal documents that the amount of cross-subsidization had reduced. In particular, one large distributor (Barclays) told us consistently from the start of our investigation that it did not cross-subsidize credit prices with PPI profits, and another ([✂]) told us that, [✂], there was no longer any cross-subsidization between PLPPI and credit. Given that these two distributors account for about [more than 20] per cent of sales of PPI, we think this is strong evidence that implies that, in aggregate for the whole market, the amount of pass-through of PPI profits is unlikely to be more than 80 per cent.

7.61 Given this evidence, we assumed in our base case that 80 per cent of PPI profits were competed away in the credit market. This assumption reflected the less conservative assumption that was used in the 2009 report.

7.62 Some distributors (Barclays, LBG and HSBC) commented on our use of an 80 per cent pass through for our base case. Barclays told us that there was no evidential

[81] As noted in paragraph 7.67, the level of excess profits calculated were based on conservative assumptions and are therefore likely to understate the extent of the detriment.

basis for assuming a waterbed effect of 80 per cent. HSBC said that the reduction in cross-subsidization, if it has occurred, appeared to be related to the current conditions in credit markets, and that the CC had not considered whether these conditions would persist in this context. LBG said that the CC revised its waterbed assumption based on what appeared to be weak reasoning and there was little or no empirical support for the revised assumption of 80 per cent. LBG argued that the move to stand-alone profitability by some distributors might reflect, among other things, the need for distributors to prepare for a post-remedy world where PPI take-up rates may be substantially lower.

7.63 We do not agree with the parties that the choice of an 80 per cent pass-through level as our base case represents a large change in approach compared with the 2009 report. Indeed, the 2009 report calculated consumer welfare from the remedies using two different assumptions: a 100 per cent pass-through assumption, and an 80 per cent pass-through assumption. The assumption of 100 per cent pass-through was presented as a somewhat extreme assumption, reflecting a cautious approach.[82] We also noted in paragraph 10.463 of the 2009 report that we could not be confident that the scale of the waterbed effect that we observed in the period up to December 2006 would persist at that level in the future. Consumer welfare was also calculated for an 80 per cent pass-through assumption.

7.64 We think that the combination of evidence on the impact of the credit crunch on incentives to lower credit prices, and the evidence that some large distributors do not cross-subsidize credit prices with PPI profits (paragraph 7.60) strongly suggests that the degree of pass-through is likely to be well below 100 per cent. Although it is not possible to determine precisely the degree of pass-through, we thought that using the 80 per cent assumption that was used in the 2009 report would be reasonable, and checked the sensitivity of our results to higher, and lower, pass-through rates.

The price of PPI policies with remedies in place

7.65 Because the remedy package has been developed to be a comprehensive solution to the AEC and resultant consumer detriment (which included prices being higher than they otherwise would have been), we expect that the POSP, combined with the other elements of the remedy package, will result in competitive markets for PPI. This increase in competition will result in lower PPI prices and better-value products.

7.66 To reflect our expectation that the remedy package will result in competitive markets for PPI, we assumed, in the modelling, that the price of PPI policies would go down to the competitive level after the remedies are in place, ie a price such that PPI distributors would no longer make excess profits on PPI (taking into account all recurring costs, as well as the costs of capital). This assumption reflected our belief that the package of remedies would be substantially effective in remedying the AEC and thereby removing the source of customer detriment.

7.67 We used the results from the updated profitability analysis to estimate the price that we would expect to prevail if there was competition between PPI distributors. The profitability analysis erred on the side of caution by using estimates for the costs of

[82] In paragraph 10.491 of the 2009 report, we note that under certain circumstances, where a number of fairly extreme assumptions combine, intervention might not be welfare enhancing. The degree of pass-through of 100 per cent is one of these 'fairly extreme assumptions'. In paragraph 10.494 of the 2009 report, where we calculate the consumer benefits from intervention, it is made clear that the 100 per cent pass-through assumption is a conservative assumption: 'Even if we assumed that all PPI profits are used to fund lower credit prices, we found that these considerations implied an annual net deadweight loss ... in excess of £200 million'.

selling PPI which are likely to be overestimates.[83] Based on the results of the profitability analysis, and taking into account both the ongoing costs of implementation of remedies and increased marketing and advertising costs after the remedies, our modelling assumed that the price of PLPPI would reduce by 52 per cent; the price of CCPPI would reduce by 6 per cent; the price of MPPI would reduce by 40 per cent; and the price of SMPPI would reduce by 41 per cent after the remedies are in place.

7.68 RBSG[84] said that there was limited evidence to support such significant price reductions, pointing to the Accent survey which it said indicated that only 12 to 18 per cent of all respondents would prefer to shop around. It also said that it would expect the informational remedies in the remedy package to increase shopping around, but the Accent survey results did not provide conclusive evidence on significant levels of shopping around by consumers. We did not agree with RBSG's analysis and their interpretation of the Accent survey results. The Accent survey was not designed to determine consumers' appetite for search, and the 12 to 18 per cent that RBSG referred to are the respondents who said that they preferred to buy after a delay because they wanted to shop around. This is very different from an estimate of the percentage of consumers who would shop around; for instance, consumers who prefer buying at the point-of-sale may still have an appetite for shopping around given the opportunity to do so by the remedy package, if this enables them to get a better price. In our view, by removing barriers to search and giving customers the information and opportunity to shop around more effectively, the remedy package is likely to increase the number of customers searching which will in turn lead to increased competition and significant reductions in price for PPI (see paragraph 10.477 of the 2009 report).

7.69 Moreover, it would not be necessary for all consumers to start searching and switching policies for providers to feel competitive pressures and for prices to be forced down. In this respect, we noted that a proportion of customers are already inclined to search, despite the barriers to search that currently exist (see paragraph 7.10) and we expect this proportion to increase as these barriers are removed by the remedy package.

7.70 We therefore concluded that it was appropriate to use competitive prices (ie the prices at which our profitability assessment indicated that no excess profits would be earned, which are likely to be overestimates (see paragraph 7.67)), as our base case, though we also tested the sensitivity of our results to smaller reductions in the price of PPI after the introduction of the remedy package.

Results from the modelling

7.71 We calculated the results from the model for a 'base case' for PLPPI, MPPI, CCPPI , and SMPPI separately. The details are in Appendix J. The base case assumes the following after the remedies are in place:

(a) The price of PPI reduces after the package of remedies is in place to the level for which PPI distributors no longer make excess profits.

[83]We assumed the fully-allocated costs of selling a PPI policy at £100, which was between [1 and 5] times higher than the evidence on the fully-allocated cost of selling a PPI policy submitted by [✄]. Because in assessing profitability we rely on estimates of costs which are themselves likely to be on the high side. this is likely to produce competitive prices that are equally over-estimates
[84]RBSG response to provisional decision, sections 2 and 2.1.2.

(b) The reduction in PPI prices results in an increase in the price of credit because of the existence of a waterbed prior to the remedies; we use an 80 per cent pass-through of PPI profits to credit prices in our base case.

(c) All credit consumers are myopic, in the sense that they do not anticipate that the price of PPI has reduced before making decisions on whether to purchase credit.

(d) The proportion of consumers who prefer to buy at the point of sale and those who prefer to buy later—and their respective valuations—are as found in the Accent survey, but the base case does not take into account the positive valuations for the delay of consumers who gave as their only reason for preferring to buy PPI after a delay that it gave them the ability to shop around.

Results in the base case

7.72 For the base case, we found that the reduction in the price of PPI with the remedies in place is larger than the cost of the loss of convenience. The increase in PPI sales as a result of competition outweighs the reduction in sales of PPI that arises from the loss of convenience and higher credit prices.

7.73 The model predicts in this base case that the package of remedies will increase net consumer welfare for PLPPI, MPPI, CCPPI and SMPPI. We found that the results from the modelling in the base case predicted an increase in consumer welfare of about £100 million per year for PLPPI, £56 million per year for MPPI, £77 million per year for CCPPI and £17 million per year for SMPPI.

7.74 We also modelled the impact of the remedies in light of the time frame over which we expect that the remedies would become substantially effective. Our analysis of this is set out in paragraphs 8.88 to 8.90, Table 8.2 and Appendix M. We found that, even allowing both for the remedies to take time to take full effect, and for the one-off costs of implementation, there are significant positive benefits of intervention for PLPPI, MPPI, CCPPI and SMPPI within three years of the remedies coming into force. We noted that these positive results were robust to the assumptions made on time frame—the benefits of intervention are significantly greater than the costs of implementation under any reasonable set of assumptions about timescale over which the remedies would become substantially effective.

The sensitivity of the modelling results to changes to inputs and assumptions

7.75 We then ran sensitivity tests to check the robustness of the results:

- To changes to the values of the inputs to the model, namely: the market elasticity of PPI demand: the market elasticity of credit demand; the PPI penetration rate; the PPI excess profit margin; and the price of PPI relative to credit.

- To relaxation of the assumptions in paragraph 7.71(a) to (d). We therefore tested whether the results were robust if the price of PPI after the remedies remained above competitive levels; if the extent of pass-through was more or less than in our base case; if after the remedies a proportion of consumers search for PPI prior to making credit decisions; and if inputs from the Accent survey were varied. In relation to the valuations found by the Accent survey, we tested in particular whether the results were robust if the costs of the loss of convenience were larger than found by Accent, if the magnitude of the costs and valuations of the delay were smaller than found by Accent, and if the positive valuation of the delay by consumers who prefer to buy later was ignored.

- To changes in the market size. We tested the robustness of the results to the possibility that the future size of PPI markets, absent remedies, would be smaller than is indicated by the average market size over the past five years.

7.76 We also considered whether our conclusions on the welfare impact of the remedies would be different if we had taken into account, in the modelling, the possibility that some consumers may decide not to purchase PPI given the time to think about their purchase, ie if a substantial proportion of current PPI sales were in fact ‘unwanted sales’ which the remedies would remove (see paragraphs 5.14 and 5.15). If this was the case, it may not be appropriate to use a five-year average level of PPI sales as the departing point for our welfare analysis—because a proportion of PPI consumers who currently buy PPI (or who did so in the recent past) do not derive a positive surplus from this purchase.

7.77 The assessment of the welfare effects of the remedies could therefore be different because the size of PPI markets on which we calculate the welfare effects after the remedies are in place would be smaller. We considered that the sensitivity we ran on the size of PPI sales dealt with this possibility: if we assumed that half of current PPI sales were in fact unwanted sales, we found that the model still predicted that the remedies would increase net consumer welfare in the base case. We were therefore confident that, even if a significant proportion of current sales were in fact unwanted, our conclusion that the remedies would increase net consumer welfare would not be affected.

7.78 We also note that if, given time to think, some consumers decided that they did not want PPI, then these consumers would be better off after the remedies are in place. The sensitivity analysis in the preceding paragraph does not take this into account as an additional welfare benefit and to that extent represents a conservative approach to considering this issue; we do not need to rely on this to support our conclusion.

- *PLPPI*

7.79 For PLPPI, there were four main departures from the base case where the model predicted that consumer welfare might decrease:

(a) if the pass-through of PPI profits to credit was over 90 per cent prior to the remedies (ie more than 90 per cent of PPI profits are competed away in the form of lower credit prices);

(b) if we ignored, in the model, three-quarters or more of the positive valuations associated with the POSP by consumers who prefer to buy later;

(c) if the market elasticity of the demand for PPI was much lower than our base case value (–0.9 or lower); or

(d) if the costs of the loss of convenience were substantially larger than found by Accent (34 per cent of the price of PLPPI or more).

7.80 We thought that it was unlikely that any of these situations would occur in practice, for the following reasons:

(a) Given the evidence that suggested there would be substantially less than a 100 per cent waterbed effect (see paragraphs 7.60 to 7.64 and Appendix I), we thought that it was unlikely that there could be a waterbed effect as large as 90 or 100 per cent.

(b) In light of the substantial positive valuations associated with delay by some consumers, we considered that it would be incorrect not to attach any positive benefit for the more than 30 per cent of consumers who have a preference for delaying the sale of PPI (see paragraph 7.52). We thought it more likely that many of these consumers would, in practice, experience a benefit from the introduction of the POSP which was not taken into account by other factors in the model.

(c) A negative welfare result required a market elasticity of demand of –0.9 or lower for PLPPI. Our analysis of the correct market elasticity of demand for PLPPI is set out in Appendix I. We concluded that the firm-level elasticity of demand for PLPPI is around –1.5, and the market elasticity is likely to be around –1.4. A market elasticity of –0.9 or lower would imply a higher level of substitution between PPI providers (ie, a larger gap between the firm-level elasticity and the market elasticity), or a firm-level elasticity lower than our estimate (around –1.1). However, we concluded in Sections 3 and 4 of the 2009 report that there was currently limited substitutability of PPI policies offered by different providers, and limited switching between providers. This means that the levels of substitution between PPI providers are unlikely to be large enough to be consistent with a market elasticity of –0.9 or less, given firm-level elasticities of –1.5. In addition, a firm-level elasticity of below –1.4 is unlikely: this would imply profit margins of 70 per cent or more (substantially higher than the margins we found in our profitability analysis).

(d) For the costs of the loss of convenience, the model predicts that consumer welfare will decrease if the costs of the loss of convenience are such that, at constant prices, PPI volumes will reduce by 28 per cent. This is equivalent to a cost of loss of convenience which amounts to 34 per cent of the monthly price of PPI (at constant elasticity). This would imply that the actual costs of convenience to consumers who prefer to buy at the point of sale are 40 per cent higher than found by Accent. We think it is unlikely that the results from the Accent survey are wrong by such a large margin of error. In addition, given that the concerns that were raised with us indicated that, if anything, the Accent survey was likely to overstate (rather than understate) the valuations placed by consumers on a break in the sales process (see Section 5), we think it is unlikely that the costs of convenience would be this high.

7.81 The model also predicted that consumer welfare might decrease if the pre-remedy excess profit margins were substantially lower than our base case values (if excess profit margins were 41 per cent or less for PLPPI). As set out in Appendix J, we thought it was unlikely that margins would be so low. Indeed, in our base case, we used a 55 per cent margin. This figure was based on the average profit margin for 2005 to 2008, which we then reduced by seven percentage points to take into account the fact that 2009 margins may be lower. We were conservative in our estimation of the excess profit margins, by allowing high costs of selling PPI in our estimation of the margins: we assumed the fully-allocated costs of selling a PPI policy at £100, which was between [1 and 5] times higher than the evidence on the fully-allocated cost of selling a PPI policy submitted by [✂]. We were therefore confident that profit margins absent remedies were significantly higher than 41 per cent.

7.82 We noted that the model was built on a number of conservative assumptions. Even if the value of the inputs were such that the model predicts a decrease in consumer welfare, this may be a result of the conservative assumptions applied. In particular, we made the following conservative assumptions:

- We were cautious in our estimation of the level of the excess profit margins, by allowing high costs of selling PPI in estimating the margins, and by reducing the level of margins by seven percentage points for PLPPI, compared with the average for 2005 to 2008.

- We did not take account of any of the dynamic benefits that we expect from the remedies.

- We did not take into account the increased demand for PPI because of increased marketing and advertising in the modelling, even though marketing and advertising costs are factored into the model.

- There is at least a possibility that some people who do not currently take out PPI at the point of sale might receive a personal PPI quote, consider the quote and decide to take out PPI even without any other changes (such as a change in price). This possibility—which would constitute an additional welfare benefit—is not taken account of in the model.

- We assumed that all credit consumers were 'myopic', so that they did not anticipate that the price of PPI had reduced when making decisions on credit (see paragraph 7.10).

7.83 We relaxed this last conservative, and unrealistic (see paragraph 7.10), assumption to see whether these negative welfare effects continue to hold if we no longer assume that all consumers are myopic once the remedy package is in place. We therefore examined what would happen if we assumed that a proportion of credit consumers search for PPI—or otherwise anticipate the cost of PPI—prior to making decisions on credit after the remedies are in place.

7.84 We found that, if 30 per cent or more of credit consumers searched for PLPPI—or otherwise anticipated the cost of PLPPI—prior to buying credit, the model predicted that consumer welfare would increase even if there was full waterbed, if we ignored all the positive valuations of the delay by those consumers who prefer to buy later, if the market elasticity of PPI demand was at the lower end of our possible range, or if the costs of the loss of convenience were 70 per cent higher than found by Accent. In Table 3.2 of the 2009 report we found that 12.3 per cent of PLPPI customers already compared policies.

7.85 We thought that it was very likely that, after the remedies are in place, at least 30 per cent of personal loan credit consumers who are potential PPI customers would search for PPI, or otherwise anticipate the lower cost of PPI, prior to buying credit. As set out in paragraphs 7.10 and 7.84, there is already some search taking place prior to the remedies being in place. We expect the proportion of such customers to increase with the introduction of a remedy package that removes many of the barriers to search that we have identified and that will also increase customers' awareness of the potential benefits of search (see paragraph 10.477 of the 2009 report). We also expect that the package of remedies will provide distributors with incentives to increase marketing of PPI to consumers away from the point of sale of credit (see paragraphs 10.44 and 10.493 of the 2009 report) and we noted that several large distributors have been developing new PPI and short-term IP (a form of PPI) that can be sold separately from credit (see paragraph 6.14 and Table 6.3). We were therefore confident that, even if any of the conditions in paragraph 7.79 occurred, the package of remedies would nonetheless result in benefits to consumers.

- *MPPI*

7.86 For MPPI, we found that the results of the model were robust to almost all the sensitivities we ran, ie the model predicts that the package of remedies will increase net consumer welfare for all but one of the sensitivities that we tested. The only case in which the model predicts a reduction in consumer welfare is if the costs of the loss of convenience are much larger than found by Accent (35 per cent or more of the current MPPI price). Given that Accent found that the costs of the loss of convenience were not significantly different from zero, we think it is unlikely that the costs of loss of convenience would be this high.

- *CCPPI*

7.87 For CCPPI, the model predicted that consumer welfare might decrease:

(a) if there was full pass-through of PPI profits to credit (ie 100 per cent pass-through); or

(b) if the costs of the loss of convenience were substantially larger than in our base case (40 per cent of the price of CCPPI or more).

7.88 For the reasons set out in paragraph 7.80*(a)* and *(d)*, we thought it was unlikely that either of these situations would occur in practice. In addition, for CCPPI, we were cautious and used the PLPPI survey results for the costs of the loss of convenience, even though we found that the costs of the loss of convenience are likely to be much lower and more similar to MPPI (as explained in paragraph 5.86). Therefore, for CCPPI, we thought that the costs of convenience were likely to be lower than in our base case, not larger.

7.89 The model also predicted that consumer welfare might decrease if the pre-remedy excess profit margins were substantially lower than our base case values (if excess profit margins were 39 per cent or less for CCPPI). As set out in Appendix J, we thought it was unlikely that margins would be so low. Indeed, in our base case, we used a 59 per cent margin. This figure was based on the average profit margin for 2005 to 2009. We were conservative in our estimation of the excess profit margins, by allowing high costs of selling PPI in our estimation of the margins: we assumed the fully-allocated costs of selling a PPI policy at £100, which was between [1 and 5] times higher than the evidence on the fully-allocated cost of selling a PPI policy submitted by [✂]. We were therefore confident that profit margins absent remedies were significantly higher than 39 per cent.

7.90 Moreover, we noted the conservative assumptions in our modelling (paragraph 7.81) and relaxed our assumption on consumer myopia (paragraph 7.83). We found that, if 12 per cent of credit consumers or more searched for CCPPI, or otherwise anticipated the cost of CCPPI, prior to buying credit, the model predicted that consumer welfare would increase even if either of the conditions in paragraph 7.87 occurred. Whilst we had no survey evidence on the current proportion of CCPPI customers who search the market, we were confident that with the remedy package in place at least that proportion of customers would search the market, bearing in mind the changes that the remedy package would bring about (see paragraph 7.85).

- *SMPPI*

7.91 For SMPPI, the model predicted that consumer welfare might decrease for the following main departures from the base case:

(a) if the pass-through of PPI profits to credit was 95 per cent or more before the remedies;

(b) if we ignored most of the positive valuations associated with the POSP by consumers who prefer to buy later (so that their positive valuation was less than 10 per cent of current price); or

(c) if the costs of the loss of convenience were substantially larger than in our base case (32 per cent of the price of SMPPI or more).

7.92 For the reasons set out in paragraph 7.80*(a)*, *(b)* and *(d)*, we thought it was unlikely that any of these situations would occur in practice.

7.93 Moreover, we noted the conservative assumptions in our modelling (paragraph 7.81) and relaxed our assumption on consumer myopia (paragraph 7.83). We found that, if 30 per cent of credit consumers or more searched for SMPPI—or otherwise anticipated the cost of SMPPI—prior to buying credit, the model predicted that consumer welfare would increase even if there was a full waterbed effect, if we ignored all the positive valuations of the delay by those consumers who prefer to buy PPI later, or if the costs of the loss of convenience were close to 70 per cent higher than found by Accent. In Table 3.2 of the 2009 report we found that 11.3 per cent of SMPPI customers already compared policies.

7.94 We thought it was very likely that, after the remedies are in place, at least 30 per cent of secured loan credit consumers who are potential PPI customers would search for PPI, or otherwise anticipate the lower cost of PPI, prior to buying credit, for the reasons set out in paragraph 7.85.

- *A combination of negative outcomes occurring together*

7.95 It is also theoretically possible that more than one of the negative outcomes set out in paragraphs 7.79 and 7.81 could occur together. If there was a combination of the values of the inputs which individually led to negative outcomes in our model, the overall prediction of the model on welfare would be more negative. However, we thought that individually these circumstances were unlikely to occur, and that in combination they were even more unlikely to occur.

Conclusions on the modelling

7.96 Using reasonable, and in some cases particularly conservative, assumptions for our base case, we found that the reduction in the price of PPI with the remedies in place is larger than the cost of the loss of convenience. The increase in sales as a result of competition outweighs the reduction in sales of PPI due to the loss of convenience and to the waterbed effect. We therefore found that the static benefits of intervention through introducing the remedy package including a POSP more than outweighed the costs of the loss of convenience and implementation, and any adverse effects associated with the loss of a relevant customer benefit of lower credit prices. This was without taking any account of the dynamic benefits we would also expect to accrue from implementation of the remedy package.

7.97 We also conducted sensitivity tests. Under some assumptions, the model predicts that the remedy package could have an overall welfare detriment. However, we were confident that these scenarios were unlikely because the assumptions required to generate an overall consumer welfare detriment were a long way from our base case assumptions. In addition, the model included some conservative assumptions and we needed only partially to relax one of these, our conservative assumption on customer myopia, in order for the model to predict that consumer welfare would increase in those scenarios which were the least unlikely to occur.

8. Revised assessment of proportionality

Introduction

8.1 In this section, we assess whether we should impose the remedy package set out in the 2009 report. In doing this, we draw on the 2009 report, and focus new analysis primarily on the questions the Tribunal required us to answer or suggested we consider (see paragraphs 1.3 to 1.5) and consider the impact of any relevant developments in the market. As we find that the remedy package would not be substantially effective for retail PPI, we then go on to consider what remedy package we should impose for retail PPI in Section 9.

8.2 The remedy package whose proportionality we considered was:

(a) A prohibition on selling PPI at the credit point of sale. PPI cannot be sold by the credit arranger (or any business covered by the prohibition—see paragraph 10.127 of the 2009 report) at the same time as the credit product, nor within seven days of the conclusion of the credit sale period, or the provision of a personal PPI quote, if one were not provided during the credit sale period. As a limited exception to this point-of-sale prohibition, the distributor or intermediary arranging the credit (or any business covered by the prohibition), may sell PPI to the consumer the day after the conclusion of the credit sale provided that the consumer has initiated the transaction over the Internet or by telephone and the consumer has confirmed that they have seen the personal PPI quote (see paragraph 8.36—this is a change from the 2009 report where we required a 24-hour break).

(b) Provision of a personal PPI quote. All credit arrangers must provide a personal PPI quote to the consumer in a durable medium, if the credit arranger provides information about PPI to the consumer during the credit sale. If the credit arranger does not provide a personal PPI quote during the credit sale period, but subsequently contacts the consumer to offer PPI, a personal PPI quote must be provided at that time. Stand-alone providers are required to provide a personal PPI quote to the consumer in a durable medium if the consumer asks the provider about the cost and/or features of a stand-alone PPI policy, including short-term IP, sold by that provider.

(c) Information provision in marketing materials. All PPI providers must disclose prominently the following information in any PPI marketing materials that include pricing claims or cost information, any indication of the benefits of the PPI product or its main characteristics: the monthly cost of PPI per £100 of monthly benefit[85] (CCPPI providers must also show the cost of PPI per £100 of outstanding balance); that PPI is optional (stand-alone providers do not have to include this statement) and available from other providers (without specifying those other providers); and that information on PPI, alternative providers and other forms of protection can be found on the CFEB's moneymadeclear website.

[85]If the benefit pays out for less than 12 months, notice of this fact must also be clearly disclosed to consumers alongside the cost of the policy.

(d) Provision of information to third parties. All PPI providers must provide comparative data to the CFEB, as specified by, and in the format requested by, the CFEB. In addition to the information that the OFT may request from time to time for the purposes of monitoring and reviewing the operation of the remedies package, all PPI providers that meet a specified threshold must provide the following information to the OFT on an annual basis: annual GWP, split by product type; distributor penetration rates, split by product type; and aggregate claims ratios for each provider, split by product type. In addition, all PPI providers must provide to any person on request aggregate claims ratios, split by product type, for the previous year. These can be provided in the form of a range to be specified by the CC.

(e) Recommendation to use information for price comparison tables. The CC should recommend to the CFEB that it use the information provided to it pursuant to this remedies package to populate its PPI price-comparison tables with data on all PPI and short-term IP products.

(f) A prohibition on the selling of single-premium PPI policies. PPI cannot be charged on a single-premium basis. Subject to the prohibition on charging PPI on a single-premium basis, premiums can be charged monthly or annually. Where an annual premium is paid by a consumer, then a rebate must be paid to consumers on a pro-rata basis if the consumer terminates the policy during the year. No separate charges can be levied on a customer for administration or for the set-up or early termination of a PPI policy.

(g) Annual reviews. PPI providers must provide an annual review for PPI customers. Provision of this annual review will be the responsibility of the company that sold the PPI policy to the consumer, other than for sales made by intermediaries where provision of this annual review will be the responsibility of the company with whom the consumer has an ongoing relationship.

(h) Compliance reporting requirements to support the above elements, as summarized in paragraph 10.566 of the 2009 report.

Whether to impose a remedy package including the POSP

8.3 In order to reach a decision on whether to impose a remedy package imposing a POSP, we look at the evidence relating to four key questions:[86]

- Is the remedy package effective (paragraphs 8.5 to 8.33)?
- Is the remedy package no more onerous than needed to achieve the aim of remedying the AEC (paragraphs 8.34 to 8.37)?
- Is the remedy package the least onerous if there is a choice (paragraphs 8.38 to 8.61)?
- Does the remedy package produce adverse effects which are disproportionate to the aim (paragraphs 8.62 to 8.99)?

8.4 Finally we conclude on whether we should impose the remedy package for PLPPI, MPPI, CCPPI and SMPPI.

[86] These correspond to the principles set out in paragraphs 19 & 20 of the Tribunal's judgment, which we consider to be an alternative way of expressing the principles set out in our guidelines: *Market Investigation References: Competition Commission Guidelines, June 2003* (CC3), section 4.

Is the remedy package effective?

8.5 We concluded in the 2009 report that the remedy package was a comprehensive and effective solution in all PPI markets where we had found an AEC (see paragraph 10.509 of the 2009 report). In paragraph 10.513 of the 2009 report, we further concluded that the remedy package would remove barriers to searching and switching and would lead to a larger stand-alone market whilst still enabling distributors to offer combinations of credit and PPI and to compete on the terms of the combination as well as of its component parts. The remedy package would lead to more active competition for PPI consumers: through more active marketing before the credit sale; in response to increased consumer search just after the credit point of sale; and by encouraging switching during the life of the credit product. This competition would manifest itself through more PPI advertising and lower prices. In reaching these conclusions, we had regard to how each element of the package contributed to addressing the AEC, both individually and in combination (see paragraphs 10.477 and 10.478 and, for the POSP, 10.36 to 10.38 of the 2009 report). Our conclusions on these matters were not quashed by the Tribunal.

8.6 In this remittal, we considered two aspects of whether the remedy package was effective. First, we considered a question raised by the Tribunal, that of whether the remedy package was effective for PPI policies where the premium tracked the outstanding balance (see paragraphs 8.8 to 8.14). Second, we considered whether, despite the AEC and our findings on the effectiveness of the remedy package not having been quashed, there was any material change in circumstances which should cause us to amend any of the component elements of the remedy package that would be required to address the AEC for any type of PPI product—see paragraphs 1.8 to 1.10 for our analysis of the legal framework underpinning this. We therefore looked at whether there was any new evidence relating to any of the five PPI products which was relevant to this assessment (paragraphs 8.15 to 8.30).

8.7 In considering the extent to which the remedy would be 'effective to achieve the legitimate aim in question'—the first limb of the test of whether a remedy is proportionate,[87] we looked at whether the remedy will be substantially effective—the wording preferred by the Tribunal for how effective the remedy package would need to be to constitute a comprehensive solution to the AEC.[88]

The effectiveness of the POSP for PPI products where the premium tracks the credit balance

8.8 This was raised by the Tribunal as an issue to consider during the remittal in relation to retail PPI. The Tribunal explained the issue in paragraph 178 of its judgment:

> The point which caused us concern was this. The Commission's decision that the proposed remedies package would be substantially effective to remedy the AEC in relation to all types of PPI, including retail PPI, involved a judgment that stand alone providers would be able to offer real competition to distributors. Yet its findings included recognition that, in relation to retail PPI, competition by stand alone providers was adversely affected by their inability to know the level of credit being extended by the retailer, on a constantly fluctuating credit account, so that they could not tailor a stand-alone PPI policy to the amount owed from time to time by the consumer. Shop Direct's submission was that

[87] See paragraph 137 of the Tribunal judgment in the Tesco case, set out in paragraph 20 of the Tribunal's judgment.
[88] See paragraph 102 of the Tribunal's judgment.

the Commission's remedies package contained no solution to this conundrum, so that it could not therefore rationally be expected effectively to remedy the AEC in relation to retail PPI.

8.9 SDGFS submitted that there was no substitute for retail PPI—as there was no alternative policy its customers could take out which would insure exactly the outstanding balance—and therefore imposing remedies, such as the POSP, which were predicated on customers being able to find alternative policies, would be ineffective and therefore disproportionate.

8.10 We considered the issue first for retail PPI, and then for CCPPI, as some parties told us that the same issues arose for CCPPI as for retail PPI. Finally, we considered it for other PPI products, as LBG said that the difficulty which the Tribunal identified with the CC's reasoning in respect of retail PPI applies not only to retail PPI and CCPPI, but also to MPPI and PLPPI, where monthly payments may vary with changes to interest rates and rescheduling of the underlying credit. Our detailed analysis is set out in Appendix L.

8.11 In relation to retail PPI, new evidence from customer research carried out by GfK for the CC[89] indicated that many customers preferred fixed-balance policies to the current retail PPI policies that tracked outstanding balances. We also saw evidence that several large distributors of CCPPI have been developing, in response to the 2009 report, short-term IP policies which do not track outstanding balances, for sale to their credit customers including their credit card customers (and ultimately other companies' credit customers). We considered that this development was also relevant to retail PPI.

8.12 These pieces of new evidence convinced us that the advantage held by retail PPI providers by their ability to tailor insurance premiums to a customer's outstanding credit balance was not a significant impediment to the effectiveness of the remedy package—in effect, any incumbency advantage associated with knowing the outstanding balance on the credit product was capable of being overcome by stand-alone providers offering good-value, fixed-balance products.

8.13 We thought that these two pieces of new evidence were equally relevant to CCPPI. We saw no reason to expect that CCPPI customers would value tracking of balances significantly more than retail PPI customers. Similarly, we thought that CCPPI distributors would not be developing IP policies which do not track outstanding balances (see paragraph 8.11) if they did not expect to be able to attract credit card customers with such an offer. We therefore concluded that the advantage held by CCPPI providers by their ability to tailor insurance premiums to a customer's outstanding credit balance was not a significant impediment to the effectiveness of the remedy package.

8.14 LBG told us that the difficulty for stand-alone providers to ascertain the amount of credit to be insured from month to month also applied to MPPI and PLPPI where monthly payments might vary with changes in interest rates and rescheduling on the underlying credit. LBG told us that it would expect the CC to take account of this issue in respect of these PPI product types. However, for the reasons set out in Appendix L, we did not think that LBG's argument was a strong one.

[89]GfK NOP Social Research – Retail PPI Qualitative Research Findings, April 2010.

The effectiveness of the remedy package for retail PPI

8.15 We saw new evidence from the GfK survey, related to customers' interest in searching for alternative PPI policies if the remedy package were in place (see the GfK report on retail PPI[90]).

8.16 The GfK survey found that retail PPI customers would welcome time and space to think about their policies, and search for alternatives. However, the qualitative research showed that only one interviewee had actually tried to find PPI anywhere else and no interviewees said that they would actually use these opportunities to search for alternative policies.

8.17 A key driver for this attitude to searching appeared to be that retail PPI customers generally pay small insurance premiums each month and most take a monthly view of their finances. This is consistent with evidence from retail PPI providers (see paragraph 6.8 of the 2009 report). SDGFS told us that average monthly premiums, including merchandise cover, were between £[✂] and £[✂] per month. Other distributors told us that their average premium income was lower: JD Williams receives on average £[✂] per year in premium income per customer, consistent with average monthly premiums of between £[✂] and £[✂] per month. As these are average figures, many customers will be paying less than this.

8.18 To customers paying small monthly premiums, retail PPI is not a significant monthly outlay, and therefore not something to which they pay much attention, or for which they would be likely to seek a better deal. In our view, this evidence suggests that there would not be many retail PPI customers who would in practice search for alternative policies. Those more likely to search would be those whose retail PPI premiums were larger than average, and/or who held other PPI policies or short-term IP policies already.

8.19 Moreover, we noted that retail PPI is, unlike other forms of PPI, the tertiary product sold by the distributor. The primary transaction relates to the consumer goods being offered; credit is then offered with a subset of customers taking up the offer of credit; and a further subset take out retail PPI as a tertiary product. We thought that this was an additional factor, unique to retail PPI, which would inhibit customers' appetite for searching, even with the remedy package in place.

8.20 We found that retail credit customers have, on average, relationships with more than four financial institutions (Table 6.2), and thought that those relationships would encourage them to consider alternative PPI products offered by those financial institutions. However, given that many retail PPI customers perceive the cost per month to be low, we were not confident that many retail PPI customers would search proactively, and given that there are relatively few retail PPI customers for other financial institutions to target, we thought that there was unlikely to be significant levels of marketing by stand-alone providers targeted at retail PPI customers and their use of retail PPI.

8.21 Based on the new evidence, we concluded that customer inertia, driven by the low monthly balances typically paid for retail PPI, and the fact that retail PPI is a tertiary product sold by retail PPI providers (after goods and credit), meant that we could not be sure that by imposing a POSP as part of the remedy package we would encourage sufficient customers to search to generate competition between providers. As a

[90]GfK NOP Social Research – Retail PPI Qualitative Research Findings, April 2010.

result, we could no longer be confident that our remedy package would be substantially effective for retail PPI.

The effectiveness of the remedy package for CCPPI

8.22 We considered whether the new evidence that we had found in relation to retail PPI was a reason to change our minds on the effectiveness of the remedy package for CCPPI. To this end, we reviewed the evidence relevant to the issue of whether there was any difference in likelihood of search for retail PPI and CCPPI customers.

8.23 We noted first that a quantitative survey of 601 CCPPI customers conducted for us in 2007 by BMRB[91] found that:

- 16 per cent of CCPPI customers had considered IP as an alternative to CCPPI to protect credit card repayments;
- 20 per cent of CCPPI customers had considered bill payment protection as an alternative to CCPPI to protect credit card repayments;
- 15 per cent of CCPPI customers had considered PPI and decided to purchase it before approaching the lender;
- 6 per cent of CCPPI customers had considered PPI before approaching the lender and decided that they wanted to discuss it with the lender; and
- 2 per cent of CCPPI customers had considered PPI before approaching the lender and decided that they did not want to purchase it (but nevertheless did after discussing it with the lender).

8.24 Whilst we thought that these percentages were small, they show that some CCPPI customers already see benefit in searching and in alternative policies and that some CCPPI customers already give active consideration to their PPI purchase before approaching a lender. By raising customers' awareness of alternatives, and providing additional opportunities to shop around, we would expect the remedy package to increase the proportions that see benefit in searching for the best-value policy.

8.25 We noted further that, unlike retail PPI, CCPPI is not sold as a tertiary product, is not bundled with merchandise cover and is offered by a larger number of providers than retail PPI. We also noted that the amounts insured by CCPPI polices are around four to six times greater than the amounts insured by retail PPI—the average outstanding balance insured by CCPPI policies in 2008 was around £1,100 (if nil balance accounts were included) or £1,700 (if nil balance accounts were excluded),[92] compared with typical outstanding balances insured by retail PPI policies of around £300.

8.26 In light of the substantially greater amounts insured, we also found that the potential benefits for CCPPI customers from searching and switching—in terms both of the cover provided and the premiums paid—were typically greater than for retail PPI customers. In the 2009 report, we found that, while there was relatively little variation in the price of CCPPI expressed as a percentage of outstanding balances covered, the amount of benefit received each month if a customer made a valid ASU claim varied substantially between providers, ranging between 3 and 15 per cent of the

[91] *Payment Protection Insurance Market Investigation Research Project Report*, February 2008, BMRB.
[92] Capital One told us that its average balance for credit card accounts with PPI was lower, at £[✂]. We noted this, but it did not change our analysis of the evidence.

outstanding balance at the time of making a claim.[93] Based on these figures, a customer with a typical outstanding credit card balance of £1,500 when they became unemployed would receive £225 per month if they had chosen a policy with the most generous policy terms, compared with £45 per month if they had chosen a policy with the least generous policy terms. While the level of cover also varies between retail PPI providers (see paragraphs 6.96 to 6.98 of the 2009 report), the potential improvement in monthly benefit achievable by a typical CCPPI customer from shopping around or switching is at least double that achievable by a typical retail PPI customer. Similarly, we found that typical monthly premiums for CCPPI customers—which we estimate at around £8.50 (if nil balance accounts are included—the figure is around £13.50 if nil balance accounts are excluded)—are also around two to three times the level of typical monthly premiums (excluding merchandise cover) for retail PPI customers which we estimate to be around £4 to £4.50 (based on a typical outstanding balance of around £300).

8.27 We concluded that the cumulative effect of all these differences was that CCPPI customers were more likely than retail PPI customers to take the opportunity provided by the remedy package to focus on the cost and product features of different PPI products.

8.28 We also expected that CCPPI consumers would be a significantly more attractive source of potential custom for stand-alone providers than retail PPI customers. The GWP of the CCPPI market is an order of magnitude larger than that of retail PPI (in 2007: £750 million compared with £78 million); there are far more CCPPI customers to seek (in 2007, there were 6.8 million CCPPI customers with the 12 largest distributors alone, compared with 1.4 million retail PPI customers), and average income among CCPPI customers was twice that of the average income of retail credit customers (we do not know the average income for retail PPI customers). Moreover, CCPPI is held by 11 per cent of personal loan customers, 22 per cent of PLPPI customers, 9 per cent of mortgage customers and 15 per cent of MPPI customers. This suggested to us that significant numbers of CCPPI customers have other types of PPI policies that they can combine into lifestyle protection policies if these come to their attention, and that they have active relationships with other PPI providers who can use those relationships to offer new products to them (bearing in mind our findings that some of the large distributors are moving towards offering products to their non-credit customers in response to the 2009 report). In contrast, retail credit is held by 1 per cent or less of each of these customer groups (and retail PPI by fewer still).

8.29 This led us to conclude that there is already significantly more general interest among CCPPI customers than retail PPI customers in alternative policies, and that if the remedy package is introduced, this level of interest is likely to grow. Further, there is likely to be significantly more interest among stand-alone providers in targeting CCPPI customers, and similarly more opportunities for stand-alone providers to make contact with CCPPI customers. We therefore concluded that the new evidence regarding retail PPI customers should not cause us to change our decision on the effectiveness of the remedy package for CCPPI.

The effectiveness of the remedy package for PLPPI, MPPI and SMPPI

8.30 We did not find new evidence that caused us to revisit our decisions on effectiveness of the remedy package for the other PPI products. We consider the time frame over which the remedy package would become substantially effective from paragraph 8.88

[93] Appendix 5.1, paragraph 74, of the 2009 report.

and in Appendix M; we conclude that the remedy package will be substantially effective within three years of coming into force.

Conclusions on effectiveness

8.31 We conclude that there was only a limited preference for PPI products where the premium tracks the credit balance and that as a result stand-alone products which do not track balance could be effective substitutes for these policies. As a result, there would be no adverse impact on the effectiveness of the remedy package of the inability of stand-alone providers to offer policies that track customers' credit balances.

8.32 The new evidence on searching by retail PPI customers caused us to reconsider our decisions on the remedy package for retail PPI. Our decisions about remedies in relation to retail PPI are set out in Section 9.

8.33 We did not find new evidence that led us to change our conclusions about the effectiveness of the remedy package for PLPPI, MPPI, CCPPI and SMPPI. For these products, we conclude that the remedy package would be substantially effective.

Is the remedy package no more onerous than needed to achieve aim of remedying AEC?

8.34 In paragraphs 10.466 to 10.479 of the 2009 report, we considered whether it was necessary to implement all the elements of the remedy package. We concluded that addressing the point-of-sale advantage was central to remedying the AEC (paragraph 10.471 of the 2009 report), that all elements of the remedy package were necessary because they interact positively with one another to enhance the overall effectiveness of the remedy package (paragraph 10.478 of the 2009 report) and that there are synergies between the applications of the remedies across different PPI sectors (paragraph 10.479 of the 2009 report).

8.35 We also considered whether the specification of each element of the package was no more onerous than necessary. For example, paragraphs 10.80 to 10.142 of the 2009 report deal with issues relating to the specification of the POSP and include for example, in paragraph 10.96, our decision that we should allow distributors to decide how much detail about PPI they should go into at the credit point of sale (rather than specifying only a general terms discussion).

8.36 We revisited the specification of the POSP in light of comments made by parties during the remittal and we also took account of comments made by parties during the consultation on the draft order prior to the remittal. Appendix N sets out our further details of how we propose to implement the POSP. With one exception, Appendix N articulates how we intend to give effect to the specification of the POSP in the 2009 report in a way that is no more onerous than necessary to achieve its aims. The one exception relates to the limited exemption to the POSP for consumer-initiated sales by telephone or over the Internet, 24 hours or more following the credit sale. In the light of further submissions about the compliance costs to business and consumer perceptions of this specification, we have decided that the exception should apply to customer-initiated sales that take place from the day after the conclusion of the credit sale, whether or not 24 hours has elapsed since the conclusion of the credit sale. Appendix N also clarifies that while sales need to be initiated by the consumer by telephone or Internet to satisfy this exemption, the transaction may be concluded in branches or other channels and that PPI sales made by a credit arranger one month or more after the conclusion of a credit sale will be treated as stand-alone sales. We concluded that these changes would reduce the costs to providers and customers of the POSP, without reducing its effectiveness.

8.37 None of the market developments caused us to change our views on the conclusion set out in the 2009 report (see paragraph 4.75).

Is the remedy package the least onerous if there is a choice?

8.38 We found in paragraph 8.33 that the remedy package was a substantially effective solution to the AEC that we found in relation to PLPPI, MPPI, CCPPI and SMPPI. We consider here whether there is a choice between equally effective measures, and if so whether the remedy package is the least onerous.

8.39 In paragraphs 10.36 and 10.37 of the 2009 report, we explained how the POSP would contribute to addressing the AEC. We said that the POSP will directly address:

- the AEC arising from the sale of PPI at the point of sale by distributors or intermediaries (ie the point-of-sale advantage); and
- barriers to search, such as customers' perception that taking PPI would increase their chance of being given credit; the bundling of PPI with credit; the limited scale of stand-alone provision of PPI; and the time taken to obtain accurate price information.[94]

8.40 During our original investigation, several alternatives to a POSP were put to us. These were set out in paragraph 10.67 of the 2009 report. Our views on them were set out in paragraphs 10.68 to 10.71 of the 2009 report. We concluded that the alternative suggestions from the parties would either be more complicated to monitor and also likely to be ineffective or would not address the AEC that we found. We saw nothing that should lead us to change this conclusion.

8.41 During the course of the remittal we received further representations about alternative remedies which we were told would be effective remedies to the AEC and would be more proportionate than a POSP. We set out below the alternative remedies put to us during the remittal and our conclusions on them. Our analysis of these different options is set out in Appendix O.

8.42 In considering these alternatives, we had regard to whether the remedy would be 'effective to achieve the legitimate aim in question'—the first limb of the test of whether a remedy is proportionate.[95] In doing so, we looked at whether the remedy will be substantially effective—the wording preferred by the Tribunal for how effective the remedy package would need to be to constitute a comprehensive solution to the AEC.[96] We also considered whether there was a material change in circumstances since our original decision on remedies, or other special reason, which should lead us to reach a new conclusion as to whether potential remedies that we had found in the 2009 report to be inadequate as a solution to the AEC would, in fact, be substantially effective (see paragraphs 1.8 to 1.10).

[94]We said that the POSP would work in conjunction with the provision of the personal PPI quote to reduce the time taken to obtain accurate price information.
[95]See paragraph 137 of the Tribunal judgment in the Tesco case, set out in paragraph 20 of the Tribunal's judgment.
[96]See paragraph 102 of the Tribunal's judgment.

Transparency remedies only

8.43 LBG, Barclays[97] and MBNA[98] told us that the remedy package's information remedies alone were sufficient to address the AEC. LBG proposed that the transparency measures could easily be strengthened and made more effective, and suggested including a PPI pricing metric in credit advertising, whilst also making clear that the PPI was optional, and recommending to the CFEB enhancements to its moneymadeclear price comparisons website.

8.44 We considered this remedy during the original investigation. Our views on it were set out in paragraphs 10.193 to 10.199 of the 2009 report. We said in paragraph 10.70 of the 2009 report: 'We concluded that a package of information remedies alone would not be sufficient and an additional structural measure would be needed to achieve a comprehensive solution to the AEC that we found'. We were similarly not convinced by LBG's analysis of why its enhanced transparency package would be substantially effective.

8.45 We did not find new evidence that would lead us to change our view that a remedy package based on information remedies alone would not be effective in addressing the point-of-sale advantage, which was an important aspect of the AEC, nor did we find a material change in circumstances, or a special reason, which should lead us to reach a new conclusion that information remedies alone would create a substantially effective remedy package.

A clear break in the sales process

8.46 In its response to our consultation on the proposed approach to reconsidering the POSP as part of its remedy package, HSBC requested that we analyse the effectiveness of alternative packages of remedies, referring to the proposals set out in the 2009 report and a proposal that, instead of imposing a POSP, we require a clear break between the sale of credit and of PPI—the credit sale would have to be concluded before the PPI sale could commence. In addition, a standard quote would be provided which the customer can either accept (with the opportunity to shop around and cancel the policy during the cooling-off period but with protection in place from the date of the credit purchase) or take away and use to shop around. The two sales could, however, be conducted by the same person within the same meeting or phone conversation.

8.47 We considered this proposal in the 2009 report in paragraph 10.69, where we concluded that:

> without a point-of-sale prohibition, providing a personal PPI quote at the point of sale, after the consumer has taken out the loan and during the sales process for a linked PPI product, would not have a sufficient effect on a consumer's searching behaviour for such a remedy package to be effective in remedying the AEC identified.

8.48 We concluded that this was not a proposal which could, with transparency remedies, form a substantially effective remedy package for PLPPI, MPPI, CCPPI or SMPPI (we consider retail PPI remedies in Section 9). In fact, we concluded that it would fall a long way short of being a comprehensive solution to the AEC. We did not believe that it would address the point-of-sale advantage held by distributors and intermed-

[97] Barclays response to the provisional decision, p11.
[98] MBNA response to the provisional decision, paragraph 2.

iaries arranging credit. It would, at best, partially address questions as to whether consumers think that taking out PPI would improve their chances of obtaining credit, though it would still be very difficult to monitor effectively whether a perception of obligation was created within a particular meeting or phone conversation.

A clear break with additional remedies

8.49 RBSG[99] said that, to the extent that the CC did not consider that the original remedy package less a POSP was sufficient to address its concerns, then a number of other remedies could be included. It suggested the following package:

(a) a requirement for a 'clear break' between the credit sale and PPI sale (see paragraphs 8.46 to 8.48);

(b) all policies to be annually renewable on an 'opt-out' basis (with an obligation on providers to contact customers reminding them that their policy was due for renewal, so as to avoid passive renewals);

(c) providers to ensure that their products could be sold on a stand-alone basis; and

(d) increased informational requirements in order to ensure that customers were made better aware of their right to cancel their PPI product in the cooling-off period. For example, there could be a requirement that firms make cancellation even easier for customers, eg by including a phone number or other contact details very prominently on all policy documents.

8.50 As set out in paragraph 8.48, we found that the 'clear break' would, at best, only partially address the point-of-sale advantage, in addressing questions as to whether consumers think that taking out PPI would improve their chances of obtaining credit. In the 2009 report, we had found that changes to the cooling-off period would not be effective because consumers seem less inclined to change policies once they have purchased them (see paragraph 10.68*(b)* of the 2009 report). The increased information requirements proposed in paragraph 8.49*(d)* did not alter our view on the effectiveness of this remedy. We saw no prospect of these two remedies which were, in our view, well short of being effective combining to be an effective solution to the point-of-sale advantage.

8.51 In terms of the opt-out remedy, we concluded in paragraph 10.68*(b)* of the 2009 report that it would not address the point-of-sale advantage directly at all, and would not be sufficient to stimulate competition to such an extent that the POSP would not be required.

8.52 We concluded that the RBSG remedy proposal would fall a long way short of being a comprehensive solution to the AEC, and hence would not be substantially effective remedy to the AEC. In particular, we concluded that it would not directly address the point-of-sale advantage, which lies at the heart of the AEC, to any material extent.

Annual renewals on an opt-in basis

8.53 During the remittal, LBG proposed that, instead of imposing a POSP, we should allow PPI sales at the credit point of sale but require that policies last no longer than one year and have an annual renewal on an opt-in basis (we refer to this as the 'opt-in remedy' as opposed to an opt-out model, proposed by Lloyds TSB during the

[99]RBSG response to the provisional decision, pp11&12.

original investigation and proposed by RBSG during the remittal—see paragraph 8.49*(b)*).

8.54 LBG said that an opt-in annual renewal did not wholly address the point-of-sale advantage but would in its view substantially diminish it.[100] The point-of-sale advantage would, LBG said, be reduced to a unique advantage in selling PPI to a consumer for one year, and a limited incumbency advantage in offering a renewal at the first anniversary.

8.55 We found that the LBG package would not deal directly with the point-of-sale advantage or the adverse effects on competition arising from it. We also found that the removal of the POSP from the remedy package was likely to reduce the effectiveness of the informational remedies in reducing barriers to search. This failure to deal directly with important features of the AEC—including the point-of-sale advantage, which we believe lies at the heart of the AEC (as acknowledged by the Tribunal[101])—and their adverse effects on competition led us to be concerned that the LBG package would not be effective in remedying the AEC.

8.56 We recognized that the LBG package might still be substantially effective in addressing the AEC if the opt-in remedy resulted in a competitive switching market in relation to existing customers, and if the competition for consumers at the point of renewal had beneficial feedback effects that increased competition or improved outcomes for consumers at the initial point of sale. However, we concluded that, while the opt-in remedy would increase opportunities for competition to attract existing consumers, there was a risk that these opportunities would not be sufficiently taken up by either providers or consumers, if the remedy package did not also contain effective measures to promote competition at the initial point of sale. Further, we did not find a reliable mechanism by which competition for switching customers would feed back to competition prior to the point of sale of credit.

8.57 We concluded that the LBG package does not deal directly with important elements of the AEC. We considered whether it could nonetheless be effective in addressing the AEC through indirect mechanisms, but we were not satisfied that the necessary conditions for this would hold in practice. We therefore concluded that the LBG package would fall a long way short of being a comprehensive solution to the AEC and would therefore not be substantially effective in remedying the AEC that we had found.

Menu regulation

8.58 Following the publication of our provisional decision, Barclays[102] proposed a new remedy, which it called ‘menu regulation’, where a consumer can buy PPI at the same time as credit but those who prefer to wait are not artificially discouraged from doing so (eg by biased information, undue pressure, etc). It said that in practice, a minimum arrangement might involve offering the customer simultaneously three different options: a default which involves being contacted in a week; another which allows for PPI (including in the form of a short-term IP product) to be taken out immediately; and a third which says that the customer does not want to be contacted in relation to those products.

[100] LBG response to the provisional decision, paragraph 1.3.
[101] See paragraph 119 of the Tribunal’s judgment.
[102] Barclays response to provisional decision, p12 and Annex 1, paragraphs 9–18.

8.59 We did not consider that the proposal would adequately address the point-of-sale advantage. This was because we had serious concerns about its impact and enforceability. In our judgement, the main shortcomings of this proposals were that:

- Customers would not have sufficient information at the credit point of sale to know whether it was worth shopping around, reducing the incentive to do so.

- The alternatives would need to be given equal weighting in their presentation to customers for this proposal to provide customers with a clear choice, but the incentives on distributors, and their sales staff, would be strongly to encourage purchase at the point of sale.

- The monitoring of this proposal for distributors and the OFT would be very difficult, given the likely volume of sales and as there would be no bright line as to what constituted a compliant sale and what did not. We did not think that this remedy could be effectively monitored.

8.60 Given these shortcomings, we concluded that a remedy package based around Barclays' menu regulation proposal would fall a long way short of being a comprehensive solution to the AEC and would therefore not be substantially effective in remedying the AEC that we had found.

Conclusion on whether the remedy package is the least onerous if there is a choice

8.61 We concluded that none of the alternative remedy packages put to us would be substantially effective—or close to substantially effective—in remedying the AEC that we had found in relation to PLPPI, MPPI, CCPPI or SMPPI. We therefore concluded that the remedy package was the least onerous remedy package that was also substantially effective.

Does the remedy package produce adverse effects which are disproportionate to the aim?

8.62 We looked at whether the remedy package would produce adverse effects disproportionate to its aim of remedying the AEC found in PPI markets. We focused on the following factors:

- the extent of customer detriment resulting from the AEC;

- the benefits of intervention;

- relevant customer benefits;

- the quantification of benefits, taking account of the loss of convenience and the loss of relevant customer benefits;

- the time frame over which the remedy package would become effective; and

- other economic risks.

The extent of customer detriment

8.63 We looked at the extent of the gross customer detriment (ie the extent of customer detriment before consideration of relevant customer benefits) that was associated with the high PPI prices caused by the AEC. We took this to be the average annual pre-tax excess profits earned by distributors over the period 2005 to 2009. We calculated this using the same methodology used in the 2009 report, as shown in Appendix A. The extent of annual gross customer detriment is set out in Table 8.1.

TABLE 8.1 **Gross customer detriment per year**

Product	*Extent of customer detriment per year £m*
PLPPI	826.4
MPPI	130.8
CCPPI	428.6
SMPPI	114.3

Source: Average excess profits 2005–2009, CC calculations based on information provided by the parties.

8.64 The data shows that for all four of the products the annual detriment is extremely high. We noted that for PLPPI in particular the average was brought down by the 2009 profitability, which we considered to be an anomalous number because of what happened in the PLPPI market in 2009 (see paragraph 4.57). If we had used an average of the years 2005 to 2008 instead, the extent of gross customer detriment would have been in excess of £1 billion per year.

Benefits of intervention

8.65 We set out customer detriments being addressed by the remedy package in paragraphs 10.493 to 10.495 of the 2009 report. There are three categories of customer detriments that we aim to address through the remedy package, and as we expect the remedy package to be substantially effective these will be benefits arising from the implementation of the remedy package.

- First, we expect competition to eliminate the 'static' harm to customers associated with current high PPI prices, including the economic inefficiencies associated with high PPI prices and low credit prices (ie the 'deadweight losses' that stem from people not buying PPI at high prices who would buy it at competitive prices and, similarly, people being offered credit at lower prices than would be the case if PPI profits were not being used to fund the sale of credit).

- Secondly, we expect the remedy package to eliminate a further static source of detriment, namely that high PPI prices were likely to have resulted in adverse selection in the markets for PPI, resulting in increased claims costs on PPI policies and increased impairment costs on credit sold to PPI customers, compared with the levels that would arise given the lower PPI price levels that we would expect in a well-functioning market. A further detriment to consumers as a result of high PPI prices was therefore the increased costs of supplying PPI at high prices due to adverse selection.

- Thirdly, we expect the remedy package, by introducing competition into PPI markets, to deliver a large category of further dynamic benefits. As set out in paragraph 7.12, we thought there were at least three categories of dynamic benefits the remedy package would deliver: first, arresting any decline in the size of the PPI sector that results from the current lack of competition, for example negative publicity associated with high prices and issues around sales quality; second, increases in advertising and awareness of PPI; and third, a combination of product innovation and selection pressure. We expect that the remedies would produce large dynamic benefits to consumers because of increased competition in the provision of PPI.

Relevant customer benefits

8.66 In paragraph 10.460 of the 2009 report we concluded that the features that we had identified as giving rise to the AEC in PPI markets resulted in a relevant customer benefit within the meaning of the Act, namely lower credit prices for personal loans (unsecured and secured), mortgages and credit cards. The only credit products on which we thought that such a waterbed effect might result in an appreciable reduction in credit prices were unsecured and secured personal loans.

8.67 In the 2009 report, we considered whether to retain the relevant customer benefit of lower credit prices for PLPPI, MPPI, CCPPI and SMPPI by altering the remedies in some way. We noted in paragraph 10.482 of the 2009 report that a distortion in credit prices is not intrinsically beneficial, and that nobody suggested to us that the cross-subsidy from PPI affects the competitive intensity of credit markets; parties which discussed this issue with us told us that the credit market would not be less competitive if the cross-subsidy were removed, but that credit prices and credit cut-off scores would reach a new equilibrium based on the competitive conditions in credit markets at that time. We saw no reason to change our conclusions on this point.

Quantification of net effect on consumer welfare , taking account of the loss of convenience and other relevant considerations

8.68 In the 2009 report we conducted some modelling to inform our judgement as to whether introducing the remedy package might be expected to have a positive or negative impact on total consumer welfare after taking account of the loss of any relevant customer benefits in credit markets.

8.69 We refined this modelling exercise looking at the net impact on consumer welfare of introducing the remedy package after taking account of the impact of a waterbed effect at the same time as looking at the effects of accounting for a loss of convenience, the ongoing costs of the remedies and the other matters which the Tribunal had invited us to reconsider. This analysis was set out in Section 7. Below we summarize the key conclusions from this analysis, as they relate to the issue of whether the remedy package gives rise to adverse effects that are disproportionate to its aim in relation to PLPPI, MPPI, CCPPI and SMPPI.

- *PLPPI*

8.70 For PLPPI, we concluded that the remedies would be substantially effective (paragraph 8.33) and that it was therefore reasonable to conclude that the detriment to be remedied would be equivalent to the benefits of implementing the remedy package. The gross detriment identified for PLPPI was £826.4 million per year (Table 8.1). We found in our base case that introducing the remedy package created a net customer welfare benefit of £100 million per year (paragraph 7.73) even before dynamic benefits of the remedies were taken into account. We found that the net effect on consumer welfare remained significantly positive, both allowing for the remedy package to take up to three years to become substantially effective and taking account of the one-off costs of implementation (Table 8.2).

8.71 We did find that in some sensitivity checks our modelling predicted a negative consumer welfare outcome, before taking account of the dynamic benefits associated with the remedy package. However, we concluded that the scenarios in which this would occur were unlikely individually and even more unlikely to occur at the same time (see paragraphs 7.80 and 7.95). Further, the model included some conservative assumptions and we needed only partially to relax one of these, our conservative assumption on customer myopia, in order for the model to predict that consumer welfare would increase even in these scenarios.

- *MPPI*

8.72 For MPPI, we concluded that the remedies would be substantially effective (paragraph 8.33) and that it was therefore reasonable to conclude that the detriment to be remedied would be equivalent to the benefits of implementing the remedy package. The gross detriment identified for MPPI was £131 million per year (Table 8.1). We found in our base case that introducing the remedy package created a net consumer welfare benefit of £56 million per year (paragraph 7.73) even before dynamic benefits of the remedies were taken into account. We found that the net effect on consumer welfare remained significantly positive, both allowing for the remedy package taking to take up to three years to become substantially effective for all policies and taking account of the one-off costs of implementation (Table 8.2).

8.73 We did find that in one sensitivity check our modelling predicted a negative consumer welfare outcome, before taking account of the dynamic benefits associated with the remedy package. However, we concluded that this scenario was unlikely to occur (see paragraph 7.86). Further, the model included some conservative assumptions and we needed only partially to relax one of these, our conservative assumption on customer myopia, in order for the model to predict that consumer welfare would increase even in this scenarios.[103]

- *CCPPI*

8.74 For CCPPI, we concluded that the remedies would be substantially effective (paragraph 8.33) and that it was therefore reasonable to conclude that the detriment to be remedied would be equivalent to the benefits of implementing the remedy package. The gross detriment identified for CCPPI was £429 million per year (Table 8.1). We found in our base case that the remedies created a net consumer welfare benefit of £77 million per year (paragraph 7.73) even before dynamic benefits of the remedies were taken into account. We found that the net effect on consumer welfare remained significantly positive, both allowing for the remedy package to take up to three years to become substantially effective and taking account of the one-off costs of implementation (Table 8.2).

8.75 We did find that in some sensitivity checks our modelling predicted a negative consumer welfare outcome, before taking account of the dynamic benefits associated with the remedy package. However, we concluded that the scenarios in which this would occur were unlikely individually and even more unlikely to occur at the same time (see paragraphs 7.88 and 7.95). Further, the model included some conservative assumptions and we needed only partially to relax one of these, our conservative assumption on customer myopia, in order for the model to predict that consumer welfare would increase even in these scenarios.

[103] In response to our provisional decision, Legal & General (Legal & General response to provisional decision, pp1–2) said that we should consider whether it was proportionate to apply the same remedies to the sale of MPPI as to the sale of PLPPI and CCPPI given that the scale of detriment was significantly lower than for MPPI (see Table 8.1). In our view, whilst it is true that the scale of the detriment is lower than for other types of PPI, it is still a significant figure and therefore the benefits for intervention with the remedy package for MPPI customers are both significant and likely to outweigh any adverse effects.

- *SMPPI*

8.76 For SMPPI, we concluded that the remedies would be substantially effective (paragraph 8.33) and that it was therefore reasonable to conclude that the detriment to be remedied would be equivalent to the benefits of implementing the remedy package. The gross detriment identified for SMPPI was £114 million per year (Table 8.1). We found in our base case that the remedies created a net consumer welfare benefit of £17 million per year (paragraph 7.73) even before dynamic benefits of the remedies were taken into account. We found that the benefit remained significantly positive, both allowing for the remedy package taking up to three years to become substantially effective for all policies and taking account of the one-off costs of implementation (Table 8.2).

8.77 We did find that in some sensitivity checks our modelling predicted a negative consumer welfare outcome, before taking account of the dynamic benefits associated with the remedy package. However, we concluded that the scenarios in which this would occur were unlikely individually and even more unlikely to occur at the same time (see paragraphs 7.92 and 7.95). Further, the model included some conservative assumptions and we needed only partially to relax one of these, our conservative assumption on customer myopia, in order for the model to predict that consumer welfare would increase even in these scenarios. We did find that in some sensitivity checks our modelling predicted a negative welfare outcome, before taking account of the dynamic benefits associated with the remedy package. However, we concluded that the scenarios in which this would occur were unlikely individually and even more unlikely to occur at the same time (see paragraphs 7.92 and 7.95).

Time frame for remedies to come into effect

8.78 The Tribunal asked us to address the timescale over which the remedies would be effective in more detail in the remittal (see paragraph 1.5). We looked at the likely timescales over which the various elements of the remedy package would have effect. Our analysis is set out in Appendix M.

8.79 As in the 2009 report, our intention is to implement the remedy package (except for the recommendation to CFEB) by means of an Order. The provision of information in marketing materials and the provision of information to third parties would then be implemented within six months of the entry into force of the Order and all other parts of the remedy package, including the POSP, would be introduced within 12 months of entry into force of the Order. So far as possible we will aim to make use of the two common commencement dates each year for new legislation and regulations of 6 April and 1 October. We concluded that the remedy package will only have a limited effect on competition before the point at which all elements of the package are implemented (which we expect to be the second quarter of 2012). We concluded this primarily because we believe that the POSP, which is in the second tranche of measures that we are introducing, forms an integral part of the remedy package, without which the remaining remedies will only be partially effective.

8.80 The remedy package may be expected to have a substantial and immediate effect on competition for new sales from the date on which all elements of the remedy package come into force. Competition for new sales is likely to develop and grow from this point on.

8.81 We concluded this for three main reasons:

- First, the POSP, in combination with the informational remedies, will immediately change the context in which consumer decisions about PPI are made. By removing the main barriers to search and providing all consumers with the opportunity to search the market away from the credit point of sale, we would expect consumer search activity to increase substantially from the date on which the POSP comes into effect.

- Second, by changing the context in which consumer decisions about PPI are made, the POSP, in combination with the information remedies, generates an immediate change to the incentives facing credit arrangers. The lead-in period to the introduction of the POSP provides an opportunity for credit arrangers to develop their product offering in ways that make their products more attractive to consumers in this new environment.

- Third, the POSP in combination with the information remedies generates immediate new opportunities for stand-alone providers, including credit providers offering PPI on a stand-alone basis. The lead-in period provides an opportunity for stand-alone providers to develop new products and propositions that will be attractive to PPI consumers that can be in place as soon as the remedies have come fully into force.

8.82 We would also expect the remedy package to have a substantial effect on competition for existing PPI policies within two to three years of all elements of the remedy package coming into force. There are two main mechanisms by which we expect the remedy package to increase competitive pressure in relation to existing PPI consumers:

- The development of a larger, more dynamic stand-alone sector—resulting from the effect of our remedies on both new and existing customers—is likely to generate greater awareness of alternatives among existing customers, both when they receive an annual review and at other times during the year. We expect stand-alone providers to respond to these opportunities by increasing the visibility and attractiveness of their products, eg through marketing, to attract new consumers, and we have found that several large distributors have already been developing policies that can be sold to their non-credit customers, and to customers with whom they do not currently have an existing relationship. We would expect the annual review and single-premium prohibition—in conjunction with the measures to facilitate search—to increase substantially the competitive constraint posed by stand-alone PPI in relation to all types of PPI, within one to two years of all elements of the remedy package coming into force, though this impact is likely to evolve and develop as the stand-alone sector grows and matures.

- The obligation to provide an annual review will prompt existing consumers to review their current cover and to consider alternatives. We believe that the impact of the annual review will be felt when customers receive their first annual review—which is within two years of making an Order for the majority of customers.

8.83 Furthermore, the single-premium prohibition will remove and prevent the reintroduction of the switching barrier associated with single-premium PPI. This was the main financial cost of switching for PLPPI and SMPPI that we found in the 2009 report. We believe there will be only a very limited number of single-premium policies still in place when the remedies come into force (see paragraph 10.331 of the 2009 report), so that the removal of this barrier to switching—and the prevention of its future return—will have immediate effect, albeit on a small number of policies.

8.84 We also considered the timescale over which we expect the remedy package to deliver dynamic benefits. We thought that there would be three types of identifiable dynamic benefits accruing (see paragraph 8.65). First, the remedy package will contribute to arresting any decline in the size of the PPI sector that results from the current lack of competition. Aside from the time taken for the remedy package to improve outcomes for consumers, we thought that this would be impacted by the time taken for those improved outcomes to feed into an improved perception of the value for money offered by PPI and the quality of PPI sales. As a matter of judgement, we thought that we would see material reputational benefits to be seen within the first five years of all elements of the remedy package coming into force.

8.85 An increase in advertising and awareness of PPI was the second category of dynamic benefits we expected. We would expect these to be stimulated by the informational remedies and the increased opportunities for stand-alone provision, and would therefore expect benefits to begin to be realized immediately with substantial dynamic benefits from this source to be realized within the first one to two years of the remedies coming into force.

8.86 The third category of dynamic benefits is a combination of product innovation and selection pressure. We expect there to be an immediate beneficial impact on product innovation as providers seek to develop new products to be in place by the time the remedy package comes into force. Subsequently, in the presence of competition, those products and providers that best meet the needs of consumers will tend to survive better than those which offer poor value for money. We therefore expect further beneficial effects of selection pressure to be realized as consumers start to make choices within the new market structure and as suppliers respond to customer demand to win business and retain market share. We would expect substantial beneficial effects arising from product innovation and selection pressure to occur within the first two to three years of the remedies coming into force and for the evolution of better products available to customers to continue to be driven by this dynamic process of rivalry.

8.87 Overall, we expect our remedies to be substantially effective in remedying the AEC within a timescale of around two to three years of all elements of the remedy package coming into force. We expect the remedy package to generate substantial benefits—both in terms of the eradication of the static consumer detriment associated with high prices and dynamic benefits of competitive markets—over a similar period, though we note that the dynamic benefits, in particular, will continue to grow as the market evolves.

The results of the modelling taking account of the time frame for effectiveness

8.88 We looked at the results of our modelling (see paragraph 7.73), taking into account the time frame over which remedies would be become substantially effective for all types of policies, and also taking account of the one-off costs of implementation. To take into account the time frame over which remedies would become substantially effective, we assumed that benefits would be realized in relation to new sales only in the first year. In the second year, we assumed that benefits would be realized in relation to new sales in the second year as well as the new sales from the previous year. From Year 3 onwards, we assumed that the static benefits would be realized on all existing PPI policies.

8.89 The results are shown in Table 8.2. The table shows that, even allowing both for the remedies to take time to take full effect, and for the one-off costs of implementation, there are significant positive benefits of intervention for PLPPI, MPPI, CCPPI and SMPPI within three years of the remedies coming into force. We noted that the positive results are robust to the assumptions made on time frame—the benefits of intervention are significantly greater than the one-off costs of implementation under any reasonable set of assumptions about timescale over which the remedies would become substantially effective.

TABLE 8.2 **Results of modelling, taking account of the one-off costs of implementation and the time frame for the remedies to be substantially effective**

	£ million per year				
	One-off costs	*Year 1 benefit**	*Year 2 benefit**	*Year 3+ benefit*	*NPV of costs and benefits over ten years†*
PLPPI	–33	+33	+67	+100	+703
SMPPI	–2	+5	+11	+17	+122
MPPI	–9	+7	+14	+56	+370
CCPPI	–26	+13	+26	+77	+505

Source: CC analysis.

*To calculate Year 1 benefits, we used the data in Table 1 of Appendix M, according to which, for PLPPI and SMPPI, about one-third of existing policies in a year are new policies; for MPPI, about 13 per cent of existing policies are new policies, and for CCPPI, about 17 per cent of existing policies are new policies.
†To calculate the NPV of benefits and costs, we assumed that one-off costs were incurred immediately. We discounted benefits by applying a discount rate of 3.5 per cent, in line with the figure specified by HM Treasury in its guidance on economic assessments as the Social Time Preference Rate.

8.90 We also looked at the net benefits of the remedies to consumers under different assumptions; we first calculated the benefits to consumers if the full effect of the remedies took five years to materialize (rather than three years), and we also calculated benefits if the full benefits of the remedies took five years to materialize and were only half of our base case estimate. The results are shown in Table 8.3. We found that, even if the remedies only brought about half of the net benefits that we had estimated, and took five years to be fully realized, the net present value of the flow of costs and benefits over ten years, taking into account the one-off costs of implementation, remained very highly positive.

TABLE 8.3 **Net present value calculations for five-year glidepath for the remedies to become fully effective, with different assumptions on the value of the benefits**

	One-off costs	*Year 1 benefits*	*Year 2 benefits*	*Year 3 benefits*	*Year 4 benefits*	*Year 5 benefits*	*Annual benefits year 6 & onwards*	*NPV of costs/benefits over 10 years*
Five-year glidepath								
PLPPI	–33	20	40	60	80	100	100	612
SMPPI	–2	3.4	6.8	10.2	13.6	17	17	108
MPPI	–9	11.2	22.4	33.6	44.8	56	56	352
CCPPI	–26	15.4	30.8	46.2	61.6	77	77	471
Five-year glidepath and benefits only half of the ones we estimated in our base case								
PLPPI	–33	10	20	30	40	50	50	289
SMPPI	–2	1.7	3.4	5.1	6.8	8.5	8.5	53
MPPI	–9	5.6	11.2	16.8	22.4	28	28	172
CCPPI	–26	7.7	15.4	23.1	30.8	38.5	38.5	222

Source: CC analysis.

Other economic risks

8.91 In paragraphs 10.39 to 10.79 of the 2009 report, we considered other economic risks that might arise with the implementation of a POSP. These were risks put to us by parties to the investigation.

8.92 In paragraphs 10.40 to 10.45 of the 2009 report, we dealt with concerns regarding whether the POSP addressed all aspects of the point-of-sale advantage and whether it would be effective at promoting search among customers. We were content at the time that the remedy package would deal with these issues sufficiently to form a substantially effective remedy package, and we found that nothing has changed since the 2009 report was published to alter that analysis in any way.

8.93 In paragraphs 10.46 to 10.52 of the 2009 report, we covered issues relating to a reduced take-up of PPI, due to a loss of convenience or an inability to recontact customers after the credit point of sale. We covered this in Section 5, and took account of our conclusions on cost of loss of convenience in our modelling (see Section 7).

8.94 In paragraphs 10.53 to 10.57 of the 2009 report, we looked at whether the POSP would result in a reduction in consumer choice, and concluded that it would not. We found in paragraphs 6.14 to 6.17 that in fact there was not going to be a loss of choice resulting from market exit—we expected nearly all large distributors to continue selling PPI (or equivalent short-term IP—a form of PPI—products) to their credit customers, and moreover, to start offering stand-alone policies in competition with one another.

8.95 In paragraphs 10.58 and 10.59 of the 2009 report, we covered concerns that the introduction of a POSP would lead to lower-quality products, on the basis that stand-alone products then in the market were of lower quality than products sold alongside credit. We found at that time that stand-alone products were not necessarily of lower quality and we did not expect the remedies to lead to lower-quality products. Nothing has happened since the 2009 report to suggest that the POSP would result in lower-quality products. Indeed, the opposite may be true, as several distributors have conducted consumer research to find out what customers want from PPI and have been developing new products (see Tables 5.1 and 5.3), many of which are aimed not just at their credit customers but for non-credit customers and possibly the open market. In our judgement, it is more likely that with the remedy package in place there will be a greater variety of stand-alone PPI products available, and some of those are likely to be responding directly to consumer research as to what customers would like from such policies.

8.96 In paragraphs 10.60 to 10.62 of the 2009 report, we looked at whether the remedies would result in higher costs for distributors. We input the ongoing costs of implementing remedies, and the costs of marketing, into our modelling, as requested by the Tribunal (see Section 7) and found that the static benefits of intervention through introducing the remedy package including a POSP for PLPPI, MPPI, CCPPI and SMPPI more than outweighed the costs of the loss of convenience and implementation, and any adverse effects associated with the loss of a relevant customer benefit of lower credit prices (see paragraph 7.96).

8.97 In paragraphs 10.63 and 10.64 of the 2009 report, we covered the question of whether the remedies would have different impacts on different providers—in particular, whether point-of-sale providers would be disadvantaged compared with stand-alone providers. We acknowledged that some disadvantage might accrue, but considered it necessary in order to remedy the AEC, and introduced the option for consumers to call back proactively after 24 hours to complete the transaction in order to mitigate the level of disadvantage felt by distributors; as noted in paragraph 14***(a)*** of Appendix N, we have decided to amend this so a call-back can be made the next day, in order to avoid issues of when the 24-hour period expires within a working day. Nothing has changed since the 2009 report to suggest that this is more of an issue than it was when we considered it in the 2009 report. Moreover, during the remittal we have seen parties' consumer research aimed at developing more tailored products for consumers, many of which would be available to at least some consumers on a stand-alone basis. We found in paragraphs 6.14 to 6.17 that with the remedy package in place nearly all large distributors will continue marketing PPI at the same time as credit, and moreover, will start offering stand-alone policies in competition with one another, and hence the boundary between point-of-sale and stand-alone providers will be blurred, further reducing the different impact on different providers.

8.98 In paragraphs 10.65 and 10.66 of the 2009 report, we covered one party's suggestion that the imposition of a POSP would amount to a restriction of the right of freedom of establishment under EU law, and our response to that. Nothing has changed since the 2009 report to alter our analysis of this point.

8.99 In paragraphs 10.67 to 10.69 of the 2009 report, we considered alternatives to a POSP put to us by other parties. We have covered those alternatives, and alternatives put to us since then, in paragraphs 8.40 to 8.61.

Conclusion on whether remedy package produces adverse effects that are disproportionate to the aim

8.100 We concluded that the remedy package was unlikely to produce adverse effects that were disproportionate its aim in relation to PLPPI, MPPI, CCPPI and SMPPI markets.

8.101 Despite the market developments that have taken place since our 2009 report, the AEC in these markets continues to give rise to very substantial consumer detriment and economic inefficiency associated with high PPI prices and an absence of the dynamic benefits that are associated with competitive markets. We expect the remedy package to eliminate the static detriment associated with high PPI prices within a period of around two to three years of all elements of the remedy package coming into place and to deliver substantial dynamic benefits within a period of around five years.

8.102 We have used an economic model to inform our judgement about the overall impact of introducing the remedy package, looking at both beneficial and adverse effects. We concluded that for PLPPI, MPPI, CCPPI and SMPPI, our modelling exercise indicated that the beneficial impacts of the remedy package were likely substantially to outweigh any adverse effects, even before taking into account the dynamic benefits associated with more competitive PPI markets. While there were some scenarios in relation to PLPPI, CCPPI and SMPPI in which this was not the case, we concluded that these were unlikely to occur in practice. Taking into account both the time for the remedies to take full effect and for the one-off costs of implementation, our modelling showed that there would be significant positive benefits of intervention for PLPPI, MPPI, CCPPI and SMPPI within three years of the remedies coming into force.

8.103 In our judgement, the dynamic benefits of greater competition, which are likely to be substantial, strongly reinforce the conclusion from our modelling exercise that the overall effect of introducing the remedy package will be beneficial.

8.104 As in the 2009 report, we reviewed various other economic risks that parties had told us were associated with the POSP and concluded that there was no new evidence that would lead us to change our view about the materiality of these risks.

8.105 Taking account of all the evidence, both quantitative and qualitative, we were confident that the remedy package would not produce adverse effects which were disproportionate to the aim in PLPPI, MPPI, CCPPI and SMPPI.

Conclusion on effectiveness and proportionality of the remedy package

8.106 Based on the analysis set out in paragraphs 8.22 to 8.105, looking at both quantitative and qualitative evidence, we conclude that the remedy package is a substantially effective and proportionate solution to the AEC found in PLPPI, MPPI, CCPPI and SMPPI markets. It is effective in achieving its aim. It is no more onerous than necessary and is the least onerous solution to the AEC that is also substantially effective. It does not produce adverse effects that are disproportionate to its aim. In reaching these conclusions, we have modelled what is in effect a 'worst case' outcome, in that there are dynamic customer benefits which we have not sought to model and which cannot readily be quantified, but which we expect to flow from the remedy package and the growth of competition.

Implications for need to carry out comparative analysis

8.107 We considered whether we should perform an additional modelling exercise comparing the remedy package with alternative remedy packages, and in particular the extent to which we needed to consider LBG's comparative modelling of the remedy package and its alternative remedy package (see paragraph 3.12). Given that we found the remedy package was substantially effective for PLPPI, MPPI, CCPPI and SMPPI, and also proportionate for these four products, and we did not find any alternative remedy package which was substantially effective, we decided not to conduct a comparative modelling exercise for these products. For retail PPI, we did not conclude that the remedy package was substantially effective, so we did consider alternative packages (see Section 9).

Conclusions on the imposition of a remedy package including the POSP

8.108 We conclude that the following remedy package (including the POSP) would be a substantially effective remedy package, and would be a proportionate remedy package, for the PLPPI, MPPI, CCPPI and SMPPI markets. In our judgement, the remedy package represents a comprehensive solution to the AEC in these markets that is both reasonable and practicable:

(a) A prohibition on selling PPI at the credit point of sale. PPI cannot be sold by the credit arranger (or any business covered by the prohibition—see paragraph 10.127 of the 2009 report) at the same time as the credit product, nor within seven days of the conclusion of the credit sale period, or the provision of a personal PPI quote, if one were not provided during the credit sale period. As a limited exception to this point-of-sale prohibition, the distributor or intermediary arranging the credit (or any business covered by the prohibition) may sell PPI to the consumer the day after the conclusion of the credit sale provided that the consumer has initiated the transaction over the Internet or by telephone and the consumer has confirmed that they have seen the personal PPI quote.

(b) Provision of a personal PPI quote. All credit arrangers must provide a personal PPI quote to the consumer in a durable medium, if the credit arranger provides information about PPI to the consumer during the credit sale. If the credit arranger does not provide a personal PPI quote during the credit sale period, but subsequently contacts the consumer to offer PPI, a personal PPI quote must be provided at that time. Stand-alone providers are required to provide a personal PPI quote to the consumer in a durable medium if the consumer asks the provider about the cost and/or features of a stand-alone PPI policy, including short-term IP, sold by that provider.

(c) Information provision in marketing materials. All PPI providers must disclose prominently the following information in any PPI marketing materials that include pricing claims or cost information, any indication of the benefits of the PPI product or its main characteristics: the monthly cost of PPI per £100 of monthly benefit[104] (CCPPI providers must also show the cost of PPI per £100 of outstanding balance); that PPI is optional (stand-alone providers do not have to include this statement) and available from other providers (without specifying those other providers); and that information on PPI, alternative providers and other forms of protection can be found on the CFEB's moneymadeclear website.

(d) Provision of information to third parties. All PPI providers must provide comparative data to the CFEB, as specified by, and in the format requested by, the CFEB. In addition to the information that the OFT may request from time to time for the purposes of monitoring and reviewing the operation of the remedies package, all PPI providers that meet a specified threshold must provide the following information to the OFT on an annual basis: annual GWP, split by product type; distributor penetration rates, split by product type; and aggregate claims ratios for each provider, split by product type. In addition, all PPI providers must provide to any person on request aggregate claims ratios, split by product type, for the previous year. These can be provided in the form of a range to be specified by the CC.

(e) Recommendation to use information for price comparison tables. The CC should recommend to the CFEB that it use the information provided to it pursuant to this remedies package to populate its PPI price-comparison tables with data on all PPI and short-term IP products.

(f) A prohibition on the selling of single-premium PPI policies. PPI cannot be charged on a single-premium basis. Subject to the prohibition on charging PPI on a single-premium basis, premiums can be charged monthly or annually. Where an annual premium is paid by a consumer, then a rebate must be paid to consumers on a pro-rata basis if the consumer terminates the policy during the year. No separate charges can be levied on a customer for administration or for the set-up or early termination of a PPI policy.

(g) Annual reviews. PPI providers must provide an annual review for PPI customers. Provision of this annual review will be the responsibility of the company that sold the PPI policy to the consumer, other than for sales made by intermediaries where provision of this annual review will be the responsibility of the company with whom the consumer has an ongoing relationship.

(h) Compliance reporting requirements to support the above elements, as summarized in paragraph 10.566 of the 2009 report.

8.109 In our judgement, this combination of measures, by opening up the market to competition and directly addressing search and switching costs, will comprehensively address the AEC that we have found and which results in consumer detriment. It will encourage consumers to search by removing many of the barriers to searching that we identified, including the point-of-sale advantage. It will improve the transparency and comparability of price information, will offer consumers a clearer understanding of the cost of PPI (and hence the benefits to searching) and will remove some of the persistent consumer misconceptions that previously discouraged shopping around. An increase in the level of searching will contribute to the development of greater price competition among PPI providers. By decreasing the point-of-sale advantage,

[104] If the benefit pays out for less than 12 months, notice of this fact must also be clearly disclosed to consumers alongside the cost of the policy.

the remedy package will also provide more opportunities for stand-alone providers to compete for PPI consumers. By prohibiting single-premium PPI, the package will also remove and prevent the re-emergence of the most significant switching cost for PLPPI and SMPPI found in the 2009 report and an important source of product complexity in pricing structures.

8.110 Moreover, the elements in the remedy package interact positively with one another to enhance its overall effectiveness. Each element of the package, when considered separately, contributes to addressing the AEC, as well as addressing specific features that we found gave rise to the AEC. Taken together, they will have a greater effect in increasing competition than if they were implemented individually and we consider that this combined effect is required in order to effectively address the AEC that we identified. For example, we consider that requiring a similar format for personal PPI quotes and annual statements will increase the impact of both. The point-of-sale prohibition and personal PPI quote are similarly complementary in that the prohibition provides consumers with the opportunity to search for a competitive PPI policy having concluded the credit agreement and the personal PPI quote provides the consumer with information that will assist in carrying out such search. We also believe that there are synergies between the application of our remedies across different PPI sectors. In particular, we expect that one effect of our remedies across all PPI sectors will be to increase substantially the competitive constraint posed by stand-alone PPI in relation to all types of PPI. The specific measures that we are proposing to put in place in relation to each form of PPI will enable consumers in that sector to benefit from this increased constraint and the greater number of alternatives available to them. While recognizing differences between products, where relevant, we have taken a broadly similar approach to remedies for all forms of PPI. This will maximize the scope for comparability which will enhance the competitive impact of the remedies package.

8.111 We conclude that we should require the introduction of the remedy package set out in paragraph 8.2 for PLPPI, MPPI, CCPPI and SMPPI.

9. The remedy package for retail PPI

9.1. This section sets out the package of remedies we have decided to implement to remedy the AEC and related customer detriment identified in relation to retail PPI. This is based on our consideration of responses to the Notice of possible remedies for retail PPI published on 14 May 2010 (the Retail Remedies Notice), responses to the provisional decision on retail PPI remedies published on 29 July 2010 (the retail provisional decision) and further analysis in light of these responses.

9.2. In the section we also discuss relevant customer benefits (paragraphs 9.27 to 9.30), issues around the implementation of the remedies (paragraphs 9.31 to 9.33), and the effectiveness and proportionality of the remedies (paragraphs 9.34 to 9.57).

The remedy package for retail PPI

9.3. The measures that form our remedy package for retail PPI are:

(a) an obligation to offer PPI separately from merchandise cover if both are offered as a bundled product (unbundling retail PPI from merchandise cover);

(b) an obligation to provide information about the cost of PPI and 'key messages' in marketing materials (information provision in marketing materials);

(c) an obligation to provide information to CFEB for publication and to provide information about claims ratios to any party on request (provision of information to third parties);

(d) a recommendation to CFEB that it uses the information provided to it under the above obligation to populate its PPI price comparisons table (recommendation to CFEB);

(e) an obligation to provide a personal PPI quote to customers before the end of the cooling-off period (personal PPI quote);

(f) an obligation to provide customers who have spent more than £50 on retail PPI premiums in the preceding 12 months with a written annual review of PPI costs including a reminder of the customer's right to cancel (annual review);

(g) an obligation to remind all active customers of their cancellation rights and of key messages on an annual basis (annual reminder); and

(h) a prohibition on selling single-premium PPI policies and on charges which have a similar economic effect (single-premium prohibition).

9.4. Key points on each of the constituent parts of the remedy package are set out in paragraphs 9.5 to 9.25 and details of parties' comments and our views are set out in Appendix P.

Unbundling retail PPI from merchandise cover

9.5. This element of the remedy package was summarized in Figure 10.6 of the 2009 report, reproduced in Figure 9.1.

FIGURE 9.1

Specification of this measure in the 2009 report

Where distributors of retail PPI offer an insurance package containing PPI and merchandise cover, they must also offer, as a separate item, PPI cover alone.

9.6. Paragraph 10.280 of the 2009 report sets out our reasoning on how this measure addresses the AEC. By separating retail PPI cover from the merchandise cover offered by retail credit providers, this element of the remedy package helps address the barriers to search in retail PPI, making it easier for customers to compare PPI products offered by different retail credit providers and to search for alternative PPI offers, including stand-alone PPI and short-term IP. By increasing pricing transparency, it helps address the failure of distributors to compete on price.

9.7. We have decided to require those retail PPI providers who offer a PPI product bundled with merchandise cover also to offer an unbundled retail PPI product, excluding merchandise cover. We expect the unbundled product to be promoted with equal prominence as the bundled product, for example in retail PPI providers' catalogues and on their websites. Retail PPI providers will not be required to offer the unbundled product proactively to every customer over the telephone but retail PPI providers will be expected to sell the unbundled product to customers on request through any distribution channel where they offer the bundled product.

Information provision in marketing materials

9.8. This element of the remedy package was summarized in Figure 10.3 of the 2009 report, reproduced in Figure 9.2.

FIGURE 9.2

Specification of this measure in the 2009 report

All PPI providers must prominently disclose the following information in any PPI marketing materials, which include pricing claims or cost information, any indication of the benefits of the PPI product or its main characteristics:

1. the monthly cost of PPI for every £100 of monthly benefit;*†
2. that PPI is optional‡ and available from other providers (without specifying those other providers); and
3. that information on PPI, alternative providers and other forms of protection products can be found on CFEB's§ moneymadeclear website.

*If the benefit pays out for less than 12 months, notice of this fact must also be clearly disclosed to consumers alongside the cost of the policy.
†CCPPI and retail PPI providers must also show the cost of PPI per £100 of outstanding balance.
‡If the PPI provider is a stand-alone provider, it does not have to include the information that the PPI is optional in their marketing material.
§Since the 2009 report, responsibility for operating the moneymadeclear website and the comparative tables has passed from the FSA to CFEB.

9.9. Our reasoning for how this measure addresses the AEC was set out in paragraphs 10.182 to 10.184 of the 2009 report. We decided that certain standard information should be provided to consumers in relevant PPI marketing materials to help them understand the price of PPI and search more effectively for the best-value stand-alone policy or combination of credit and PPI. This element of the original remedy package would make it easier for consumers to compare PPI products offered by different providers and to search for alternative PPI offers, including stand-alone PPI and short-term IP policies. By increasing the prominence of PPI prices within the information provided to consumers, the remedy would help to address the failure of distributors to compete actively on the price of their PPI products. This requirement would complement and enhance other measures that address barriers to search and complement and support measures to facilitate switching.

9.10. We have decided to implement this remedy as specified in the 2009 report in relation to marketing materials. In doing so, we concluded that it was practicable to apply the monthly cost for every £100 monthly benefit pricing metric, used for other forms of PPI, to retail PPI (see paragraph 31 of Appendix P and Appendix Q). We have also decided to require retail PPI providers to state during sales conversations that PPI is optional, that alternative products are available from other providers (without specifying those other providers) and that information on PPI, alternative providers and other forms of protection products can be found on CFEB's moneymadeclear website, but not to require retail PPI providers to state the price of PPI using any particular metric during sales calls.

Provision of information to third parties

9.11. This element of the remedy package was summarized in Figure 10.4 of the 2009 report, reproduced in Figure 9.3.[105]

FIGURE 9.3

Specification of this measure in the 2009 report

All PPI providers must provide comparative data to CFEB§, as specified by, and in the format requested by, CFEB. We also recommend to CFEB that it uses the information provided to it under this obligation to populate its PPI price-comparison tables. All PPI providers should provide to any person, on request, aggregate claims ratios, split by product type, for the previous year. These can be provided in the form of a range to be specified by the CC. §Since the 2009 report, responsibility for operating the moneymadeclear website and the comparative tables has passed from the FSA to CFEB.

9.12. The rationale for this remedy was set out in paragraphs 10.223 and 10.224 of the 2009 report. We said we had found that a consumer's ability to compare products was reduced by an absence of information provided in a way that would help them, and that few distributors actively sought to win credit and/or PPI business by using the price (or non-price characteristics) of their PPI policies as a competitive variable.

9.13. Paragraph 10.225 of the 2009 report explained how we expected the remedy to address the AEC. We expected that this requirement would make information available which would help consumers to compare the cost of PPI and would help consumers to search for the best-value policy. By facilitating search and switching, this requirement would complement and enhance other measures including the provision of a personal PPI quote, the provision of information in marketing material and the annual review.

9.14. We concluded that an obligation on retail PPI providers to provide information to CFEB for use in its price comparison tables, when combined with a recommendation to CFEB to develop its website to incorporate retail PPI, would make an important contribution towards addressing the AEC in retail PPI. It would help those retail PPI customers who were motivated to search and switch to do so, by helping them compare retail PPI policies against one another and against other PPI products including stand-alone PPI, short-term IP and CCPPI. We also concluded that the obligation to make claims ratios publicly available was necessary for the reasons set out in paragraphs 10.240 of the 2009 report. We therefore decided to implement this remedy as specified in paragraph 10.240 of the 2009 report.

Obligation to provide a personal PPI quote during the cooling-off period

9.15. In the 2009 report, we concluded that a personal PPI quote was necessary, in conjunction with the POSP, to help customers search. The personal PPI quote would contain information about the consumer, the credit product that is being insured (where this is relevant) and the PPI policy. We have decided not to impose the POSP (see paragraph 9.26(a) and Appendix P) but have explored with parties whether the personal PPI quote might instead be adapted to provide information about retail PPI during the cooling-off period.

[105]Figure 10.4 of the 2009 report also included a requirement to disclose information to the OFT to facilitate its monitoring of the remedies. These monitoring requirements are discussed in Appendix T.

9.16. The purpose of this measure is to encourage customers to review their recent PPI purchase during the cooling-off period and to provide them with information that would enable those customers who were interested in doing so to compare the PPI policy they have recently taken out against alternatives. This measure would contribute towards addressing the AEC by encouraging search and would act with the remedies requiring the provision of information in marketing materials and the supply of information to CFEB for publication on its price comparisons website.

9.17. We decided that retail PPI providers should provide a personal PPI quote during the cooling-off period, no later than 14 days after the conclusion of the contract. This should use the template at Appendix R. Retail PPI providers will be permitted to provide the personal PPI quote with policy documentation to those customers that have taken out PPI, and we expect that retail PPI providers will do so. The personal PPI quote may be provided, if appropriate, by electronic means.

Obligations to provide annual reviews[106] and annual reminders

9.18. The obligation to provide an annual review in the original remedy package was summarized in paragraph 10.302 and Figure 10.7 of the 2009 report, reproduced in Figure 9.4.

FIGURE 9.4

Specification of annual review in the 2009 report

All PPI providers will provide an annual review to all their PPI consumers (detailed in Appendix 10.2 of the 2009 report).*
Provision of this annual review will be the responsibility of the company which sold the PPI policy to the consumer (ie the distributor or the stand-alone provider), other than for sales made by intermediaries where provision of this statement will be the responsibility of the underwriter (or distributor or stand-alone provider) with which the consumer has an ongoing relationship.
The annual review must be provided separately to any information on a credit product held by the consumer but might be included with other information relating to the PPI policy.

*PPI consumers in this context do not include those PPI consumers who have not paid any PPI premium on that policy in the previous year.

9.19. In paragraph 10.302 of the 2009 report, we said the annual review should include information similar to that provided in a personal PPI quote and information about consumers' rights to cancel the policy. Paragraph 10.303 of the 2009 report explained that by raising consumer awareness of their ability to switch PPI provider, this remedy would encourage consumers periodically to consider whether their PPI policy still represented their best-value option. The specification of the annual review was designed to complement the requirements to provide a personal PPI quote, to pricing information in marketing materials and information to CFEB for publication on its website. This would help consumers prompted by the annual review to consider alternatives to their current PPI policy and make comparisons with other products.

9.20. In the Retail Remedies Notice, we also consulted on an alternative measure, to send some or all customers an annual reminder of their cancellation rights and of key messages (see Figure 9.5). This would contain some of the generic elements of the

[106] In the 2009 report, we referred to this element of the remedy package as an annual statement. Following consumer testing in April 2009, we decided that this document should be referred to as an 'annual review' as consumers felt that this more accurately described its purpose.

annual review but would not include specific information about a customer's PPI policy or its use of that policy during the past 12 months. We also consulted on whether the annual review should be targeted at consumers who have paid retail PPI premiums over the past year above a certain threshold (we consulted on a £50 threshold—see paragraph 9.22), since these customers are most likely to perceive benefits from searching and switching than other customers, with lower-spending consumers receiving the annual reminder.

FIGURE 9.5

Specification of annual reminder in the Retail Remedies Notice

Retail PPI providers should be required to remind, on an annual basis, those customers who do not receive an annual review of their cancellation rights and of the key messages that PPI is optional and available from other providers, and that information is available on the CFEB's moneymadeclear website.

9.21. The aim of this measure is similar to that of the annual review, to encourage consumers periodically to consider whether their retail PPI product is right for them and to consider searching the market for alternatives.

9.22. We have decided that we should include the obligation to provide an annual review, as specified in the 2009 report, to those customers who have spent more than £50 (a group we thought were most likely to search the market and consider switching given their level of PPI spend) in the period to which the annual review relates. The template to be used for the annual review is at Appendix R. We have also decided that retail PPI providers should be required to provide an annual reminder of the information in paragraph 72 of Appendix P to other customers that have an active balance on their retail credit account, on the date when, if their spending in the past year had been greater, they would have been due to receive an annual review.

Single-premium prohibition

9.23. This element of the remedy package was summarized in Figure 10.5 of the 2009 report, reproduced in Figure 9.6.

FIGURE 9.6

Specification of this measure in the 2009 report

No PPI provider can charge for PPI on a single-premium basis. The only charge that can be levied on a PPI policy is a regular premium, paid monthly or annually by a consumer. If an annual premium is paid by a consumer, then a rebate must be paid to consumers on a pro-rata basis, if the consumer terminates the policy during the year. No separate charges for administration or for the set-up or early termination of a PPI policy shall be payable by the consumer.

9.24. Paragraph 10.245 of the 2009 report explained that this remedy would fully address the switching barrier caused by the terms on which single-premium policies were terminated and was the only option which would do so effectively. The element of the remedy package would also reduce barriers to search associated with complex pricing structures. It therefore complemented and enhanced the other elements of the remedy package aimed at facilitating consumer search, addressing the point-of-sale advantage and encouraging switching.

9.25. None of the parties has expressed concern about this remedy because it does not have any immediate practical implications for their business. We consider that it would be appropriate to retain this remedy for retail PPI as a preventative measure—to prevent the emergence of cancellation fees or other forms of pricing complexity—and note that in practice its implementation would not impose any costs on retail PPI providers. We have therefore decided to include this measure in the remedy package for retail PPI.

Options we are not taking forward

9.26. There were a number of options set out in the Retail Remedies Notice or suggested to us by parties which we are not proposing to take forward. These are:

(a) the point-of-sale prohibition;

(b) obligation to renew retail PPI policies annually on an opt-in basis; and

(c) price caps.

Our reasoning on why we have decided not to take forward these remedies is provided in Appendix P.

Relevant customer benefits

9.27. In deciding the question of remedies, the CC may 'in particular have regard to the effect of any action on any relevant customer benefits of the feature or features of the market concerned'.[107] Appendix S details our framework for the assessment of relevant customer benefits.

9.28. We considered whether there are any relevant customer benefits which we should have regard to in deciding on our remedy package for the retail PPI market. SDGFS submitted analysis by the economic consultancy Oxera, including internal documents, which it said demonstrated the existence of a waterbed effect[108] in relation to the price of retail PPI and the price of goods and credit. SDGFS submitted that this was a relevant customer benefit that would be lost if the CC were to impose a price cap. Another retail credit provider (FGH) submitted that there was a waterbed effect, but did not produce further evidence or analysis to support this view.

9.29. We considered these further submissions carefully. While we acknowledge, in principle, that a waterbed effect might exist in relation to retail PPI, the further analysis and internal documents submitted by SDGFS did not persuade us that such an effect existed in this market, or if it did, that it was material. In particular, the evidence submitted did not establish any direct link between the price of PPI and the price of other products offered by SDGFS. At most, the evidence from SDGFS suggested to us that SDGFS looked at the profitability of its business 'in the round', and that if income from PPI were to fall for any reason, it might seek to recover profits from elsewhere.[109] In response, SDGFS said that the decision not to impose a price cap meant that the CC's findings on relevant customer benefits were not as important as they would otherwise have been, but that it still disagreed with the CC's views. It said

[107] Section 134(7) of the Act.
[108] A waterbed effect, if it existed, would mean that high retail PPI prices result in lower prices for goods or credit than would otherwise be the case.
[109] The Oxera report came to the similar conclusion: 'All these documents are consistent with an overall finding that retail PPI is not considered in isolation from other products offered by SDG, and hence it would be expected that any excess profits would not be ring-fenced and could have a bearing on Group-level commercial decisions regarding other parts of SDG'.

that, in its view the evidence demonstrated that low margins on the embedded product offering were supported by margins in financial services, including PPI. However, it said that the direct link sought by the CC was only difficult to establish because the margin support provided by PPI was spread thinly across the revenue from the sale of goods, but it said that nevertheless there was margin support.

9.30. In our judgement, this still fell some way short of establishing that there were relevant customer benefits that were sufficiently material, or well evidenced, for us to take into account in deciding what remedial action to take in relation to retail PPI. We also noted SDGFS's submissions that a waterbed effect was most likely to materialize if we were to require a price cap, which is not one of the remedies that we are taking forward. We concluded that it was unlikely that any material relevant customer benefits would be lost as a result of introducing the remedy package and we therefore decided not to modify our remedy package to take account of relevant customer benefits.

Implementation of remedies

9.31. We have decided that the remedies should be implemented by Order and that all elements of the remedy package should come into force within 12 months of the implementing Order, with the exception of the provision of information to third parties and the provision of information in marketing material, which should come into force within six months of the implementing Order (see Appendix T).

9.32. We propose to make one recommendation to CFEB, that it use the information provided to it to populate its PPI price comparison tables. CFEB told us that it did not object to this proposal and that it would need to undertake some work with providers and others to explore the feasibility of this recommendation. JD Williams also suggested that the CFEB could work directly with the PPI providers to agree the content and format of the information required. CFEB told us that it would liaise with providers in its development of the tables and it would probably issue a communication that would set out the questions it is proposing to ask and the information it is likely to display. CFEB would also want to undertake a cost-benefit analysis. The CC will provide CFEB with the necessary assistance to help it carry out this further work.

9.33. We have also decided that the monitoring and enforcement regime set out in paragraph 10.566 of the 2009 report and in Appendix T should also apply to retail PPI, apart from those reporting requirements which relate specifically to the POSP.[110] Following publication of our retail provisional decision, JD Williams queried one element of this regime, namely the requirement for the compliance reports produced by distributors whose GWP exceeds a threshold of £10 million a year to be verified by an independent third party. In our judgement, this requirement remains necessary to ensure effective monitoring of the remedies as this will reduce the need for the OFT to verify that the information being provided by parties is correct. We acknowledge that this requirement will add to the cost of the remedy package—JD Williams estimated that the additional cost might be 'tens of thousands' of pounds. However, we did not consider that this additional cost was disproportionate, given the importance of effective monitoring to delivering the benefits that we expect our remedies to deliver.

[110]All retail PPI providers will be required to appoint a compliance officer. The OFT will have the ability to obtain from any relevant person, from time to time, any information and documents reasonably required for the purposes of enabling the OFT to monitor and review the operation of the remedies Order or any provision of the Order. There are additional compliance reporting requirements in relation to those retail PPI providers with GWP above £10 million.

The effectiveness and proportionality of our proposed remedy package

9.34. The decisions set out above give rise to a package of measures:

(a) an obligation to offer PPI separately from merchandise cover if both are offered as a bundled product (unbundling retail PPI from merchandise cover—paragraphs 9.5 to 9.7);

(b) an obligation to provide information about the cost of PPI and 'key messages' in marketing materials (information provision in marketing materials—paragraphs 9.8 to 9.10);

(c) an obligation to provide information to CFEB for publication and to provide information about claims ratios to any party on request (provision of information to third parties—paragraphs 9.11 to 9.14);

(d) a recommendation to CFEB that it uses the information provided to it under the above obligation to populate its PPI price comparisons table (recommendation to CFEB);

(e) an obligation to provide a personal PPI quote to customers before the end of the cooling-off period (personal PPI quote—paragraphs 9.15 to 9.17);

(f) an obligation to provide customers who have spent more than £50 on retail PPI premiums in the preceding 12 months with a written annual review of PPI costs including a reminder of the customer's right to cancel (annual review—paragraphs 9.18 to 9.22);

(g) an obligation to remind all active customers of their cancellation rights and of key messages on an annual basis (annual reminder—paragraphs 9.18 to 9.22); and

(h) a prohibition on selling of single-premium PPI policies and on charges which have a similar economic effect (single-premium prohibition—paragraphs 9.23 to 9.25).

How the proposed remedy package addresses the AEC

9.35. We expect that these remedies will mitigate the AEC and the resulting consumer detriment that we have identified in the following ways.

9.36. We expect the informational remedies in paragraph 9.34(a) to 9.34(e) to encourage some retail PPI customers to search by removing some of the barriers to searching that we identified in our 2009 report, including the bundling of retail PPI and merchandise cover. These measures will increase consumers' awareness of the existence of alternatives and improve the transparency and comparability of price information, offering consumers a clearer understanding of the cost of retail PPI and hence the potential benefits to searching.

9.37. We acknowledge that the increase in customer search may be limited, in particular because the typical monthly premium paid by many retail PPI customers is low, and because there is no measure that directly addresses the point-of-sale advantage from this package. However, we expect any increase in the level of searching to contribute to greater price competition among retail PPI providers and to provide additional opportunities for stand-alone providers to compete for retail PPI customers.

9.38. The obligations to provide annual reviews and annual reminders (paragraph 9.34*(f)* and 9.34*(g)*) to existing customers will also increase competitive pressure on retail PPI providers, particularly in relation to the retention of the higher-spending customers of retail PPI, who we would expect to have the greatest financial motivation to search and switch. The prohibition on single premiums and other pricing structures with similar economic effects in paragraph 9.34*(h)* will ensure that the improvements in transparency that we expect our remedy package to deliver will not be eroded by changes to future pricing structures.

9.39. Our proposed remedies will interact positively with one another to enhance the overall effectiveness of the remedy package. Each element of the package contributes to addressing the AEC, and when they are combined they will have a greater effect in increasing competition than they would individually.

9.40. The remedies that we are proposing for retail PPI also interact positively with the remedies that we are proposing for other types of PPI. We expect that one effect of our remedies across all PPI markets will be to increase substantially the competitive constraint posed by stand-alone PPI in relation to all types of PPI, including retail PPI. The specific measures that we are proposing to put in place in relation to retail PPI will enable retail credit customers to benefit from this increased constraint and the greater number of alternatives that we expect will be available to them. In Table 6.2 we noted that mail order customers had, on average, relationships with four financial institutions, and we expect that the measures we are adopting in retail PPI, together with the measures in other markets, mean that competition for retail PPI customers should increase.

9.41. While recognizing differences between products, where relevant, we have taken a broadly similar approach to the informational remedies that we are putting in place for retail PPI as for other forms of PPI. This will maximize the scope for comparability, which will enhance the competitive impact of the remedy package.

9.42. We consider that this combination of measures, by opening up the market to competition and directly addressing search and switching costs, will mitigate the AEC that we have found and as a result will also reduce the consumer detriment that flows from the AEC. We expect this remedy package, when combined with the introduction of remedies in other PPI markets, to produce appreciable beneficial effects to consumers over a timescale of two to three years from the remedies coming into force (see Appendix U for further discussion of this issue).

The cost of the remedy package

9.43. The cost estimates from SDGFS and JD Williams for the remedies in the form we have adopted are summarized in Appendix V. Based on these figures, the annual cost to these parties of complying with the remedy package could be the region of £0.8 million a year, with a one-off implementation cost in the region of £1.0 million. In light of our discussion of relevant customer benefits at paragraphs 9.27 to 9.30, we did not consider it likely that any material relevant customer benefits would be lost as a result of introducing this package of measures.

Evaluation of proportionality

9.44. We have concluded that the package of remedies proposed in this document will mitigate the AEC and will produce beneficial effects within a timescale of around two to three years of coming into force (see paragraph 9.42).

9.45. We now consider whether this package would be a proportionate response to the problems that we have identified, by considering the following four key questions:

(a) Is the remedy package effective in achieving its aim?

(b) Is the remedy package no more onerous than necessary to achieve its aim?

(c) Is the remedy package the least onerous if there is a choice?

(d) Does the remedy package produce adverse effects which are disproportionate to the aim?

Effective in achieving its aim

9.46. We have concluded that the remedy package will mitigate the AEC by addressing some of the barriers to search and reminding existing customers of the opportunities to switch (see paragraphs 9.35 to 9.42). We considered other remedies (see paragraphs 9.26 to 9.30 and Appendix P) but concluded that the remedy package selected was the most proportionate remedy package that was both reasonable and practicable. We note that the single-premium prohibition is a preventative measure but does not impose any costs.

No more onerous than necessary

9.47. We have designed the remedy package to be no more onerous than necessary. This consideration has informed decisions about the choice of remedies—in particular, the exclusion from the remedy package of those measures, including the POSP, which we did not consider would make a sufficient contribution to addressing the AEC to justify their costs of implementation and compliance. It has also informed our consideration of the design of individual remedies—for example, our decision to require annual reviews to be sent only to those retail PPI customers who have spent more than £50 in retail PPI premiums over the past year.

9.48. We concluded that each of the remedies we have decided to include in our remedy package makes a significant contribution to addressing the AEC without being more onerous than is necessary to achieve that aim, and the elements of the remedy package interact with each other to enhance the overall effectiveness of the package.

Least onerous if there is a choice

9.49. We considered other remedy options, as set out in paragraphs 9.26 to 9.30 and Appendix P, that we decided not to implement. Each of the other options was either less effective than elements in this remedy package that we are taking forward having the same aim, more onerous, or both. In the case of remedies (or alternative specifications of remedies) that were less onerous than the remedies that we were taking forward, we found that these would make the remedy package less effective and that the additional costs involved by taking our preferred approach were justified by the impact on the effectiveness of the package.

Does not impose costs which are disproportionate to the aim

9.50. Based on the evidence from providers, we expect the package to give rise to implementation costs in the region of £1.0 million and ongoing costs of around £0.8 million a year (see paragraph 9.43).

9.51. We looked at the extent of the gross customer detriment (ie the extent of customer detriment before consideration of relevant customer benefits) that was associated with the high PPI prices caused by the AEC. We took this to be the average annual pre-tax excess profits earned by distributors over the period 2005 to 2009. We calculated this using the same methodology used in the 2009 report, as shown in Appendix A. We estimated the static consumer detriment arising from the AEC over the past five years to have been £13.5 million a year. This figure was somewhat lower in 2008 and 2009 than in previous years, though we found it difficult to establish whether this recent reduction, which appeared to be driven primarily by falling GWP rather than lower prices, was likely to continue into the future. We noted the submissions by SDGFS and FGH (see paragraph 9.28) that there were waterbed effects, such that customers were benefiting from lower prices for credit and/or goods as a result of the AEC, but we did not find strong evidence that such effects were material or would be lost as a result of our remedies. We concluded that £13.5 million was a reasonable estimate of the static consumer detriment that could be avoided each year by the introduction of a substantially effective remedy package.

9.52. In addition, we considered that there would be other dynamic benefits to consumers that we would expect to arise from increased competition in the provision of retail PPI beyond those reflected in the calculation of static consumer detriment. For example, we might expect some customers to benefit from switching to alternative forms of PPI and for increased competitive pressure to drive retail PPI providers to develop their products to respond to customer demand.

9.53. As we thought that our remedy package would mitigate the AEC and resulting consumer detriment, we expect the remedy package to have a static consumer benefit of less than the full static consumer detriment of £13.5 million. Therefore we explored the level of annual benefits the remedies would need to generate to justify the costs. It was not possible precisely to quantify the benefits that we expected to result from the remedy package. However, we decided that it was reasonable to expect that the remedy package, in conjunction with the introduction of remedies in other PPI markets, would generate static annual consumer benefits equivalent to at least 20 per cent of the static consumer detriment that we had identified in retail PPI, within a period of two to three years of coming into force. In forming this view, we took into account the following:

(a) the assessment in paragraphs 9.35 to 9.42 about how the remedy package addresses the AEC and resulting consumer detriment;

(b) the analysis in Appendix P indicating that around three-quarters of retail PPI premiums each year are accounted for by customers who spend more than £50 a year on retail PPI and who we consider are most likely to respond to our remedies by searching and switching; and

(c) our assessment in paragraph 9.42 and Appendix U of the timescale over which we expect our remedies to take effect.

9.54. To inform our judgement, we calculated an illustrative scenario of the potential net benefits of our remedies on the assumption that the remedies would generate annual static consumer benefits equivalent to 20 per cent of the static consumer detriment within three years of the remedies coming into force and that the remedy package would result in one-third of this level of benefit in the first year of operation and two-thirds in the second year. Table 9.1 shows the one-off costs and the net consumer benefits—after taking account of ongoing costs—based on these assumptions.

TABLE 9.1 **Illustrative scenario of costs and net benefits of remedies**

				£ million
	One-off costs	*Year 1 net benefits*	*Year 2 net benefits*	*Year 3 net benefits*
Retail PPI	–1.0	0.1	1.0	1.9

Source: CC analysis based on information provided by parties.

9.55. We also expect (see paragraph 9.52) that the remedy package is likely to generate dynamic benefits in addition to the static benefits associated with lower retail PPI prices.

9.56. Based on the assessment in paragraphs 9.50 to 9.55, we concluded that the benefits of introducing this remedy package for retail PPI were likely to outweigh the relevant costs within a period of around three years. We concluded that the remedy package would not impose costs that were disproportionate to the aim of mitigating the AEC that we found in relation to retail PPI.

Conclusion on proportionality of remedy package for retail PPI

9.57. Based on the assessment in paragraphs 9.45 to 9.55, we have concluded that the remedy package as set out in this section represents a proportionate approach to mitigating the AEC and resulting consumer detriment that we found in retail PPI. We concluded that we should introduce this remedy package for retail PPI.

Conclusion

9.58. For retail PPI we decided not to impose a POSP as part of the remedy package. New evidence about customer behaviour meant that we could not be confident that such a remedy package would be substantially effective for retail PPI. In the light of this new evidence and taking into account its likely costs, we concluded that introducing a POSP was unlikely to generate a sufficient increase in competition to justify its inclusion in the remedy package for retail PPI. We decided instead to impose a remedy package which would represent a proportionate approach to mitigating the AEC and resulting consumer detriment that we found in retail PPI markets.