

MARKET INVESTIGATION INTO PAYMENT PROTECTION INSURANCE

Provisional decision on remedies

Published: 13 November 2008

The Competition Commission has excluded from this published version of the provisional findings report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by ✂. Some numbers have been replaced by a range. These are shown in square brackets. Non-sensitive alternative wording is also indicated in square brackets.

Provisional Decision on Remedies

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Summary

1. On 7 February 2007 the Office of Fair Trading (OFT) referred to the Competition Commission (CC) the supply of all payment protection insurance (PPI) (except store card PPI) to non-business customers in the UK. On 5 June 2008 we issued a Notice of Possible Remedies (the Notice), which invited comments on the actions we might take, or recommend for implementation by others, to remedy, mitigate or prevent the adverse effect on competition (AEC), or resulting detrimental effects on customers, identified in our provisional findings of the same date.
2. This document presents our provisional decision on the package of remedies required to remedy the AEC and related customer detriment provisionally identified. This is based on our consideration of responses to the Notice, further submissions from parties, further analysis and responses to a consultation on some of this further analysis, published on 14 October. We published a separate Remedies Notice on 10 October 2008 in relation to retail PPI, and we are currently considering the responses received to that Notice.
3. We considered the remedies separately for each type of PPI policy for which an AEC was found in our provisional findings report of 5 June 2008: personal loan PPI (PLPPI), credit card PPI (CCPPI), mortgage PPI (MPPI) and second-charge mortgage (also known as secured loan) PPI (SMPPI). We concluded that the remedies package for each type of PPI policy should be the same, though the detail of some of the remedies varies according to the type of PPI policy. The remedy package includes:
 - (a) a prohibition on the active sale of PPI by a distributor to a customer within 14 days of the distributor selling credit to that customer—customers may proactively return to the distributor to initiate a purchase by telephone or online from 24 hours after the credit sale;

- (b) a requirement on all PPI providers to provide certain information and messages in PPI marketing materials, and a requirement on distributors to advertise PLPPI and SMPPI in close proximity to their respective personal loan advertisements;
- (c) a requirement on all PPI providers to provide certain information on PPI policies to the Financial Services Authority (FSA);
- (d) a recommendation to the FSA that it use the information provided under the requirement in (c) to populate its PPI price comparison tables;
- (e) a requirement on distributors to provide an annual statement for PPI customers; and
- (f) a prohibition on the selling of single-premium PPI policies.

4. We concluded that the package of remedies proposed in this paper will deal with the AEC that we have provisionally identified in a timely manner. Because the package will do this, and in doing so will address the resultant customer detriment, we do not propose to deal separately with the customer detriment of higher prices arising from the AEC that we have provisionally found, and as a result are not proposing to impose price caps.
5. We considered other remedy options, including minimum standards for PPI policies and the provision of customer credit card balances data. We conclude that these alternative options would not add to the effectiveness of the proposed remedies either on their own or as part of a package.
6. We considered whether there are any relevant customer benefits. We concluded that there are no relevant customer benefits arising from the sale of single-premium policies or the sale of PPI at the credit point of sale. We further concluded that we should not modify our remedies to preserve the relevant customer benefit of lower credit prices or credit cut-off scores when choosing our remedies, noting that we

expected our intervention would have a significant positive effect both for PPI customers and for overall consumer welfare.

7. As well as being effective, we consider that this package of remedies is proportionate to the AEC that we have provisionally found. We considered several other possible remedies and concluded, in each case, that they would not be effective to address the AEC and the resulting consumer detriment. Each of the remedies options that we are taking forward makes a significant contribution to addressing the AEC and the elements of the remedy package interact with each other to enhance the overall effectiveness of the package. The remedy package will increase overall consumer welfare, taking into account the set-up and ongoing costs of implementing the remedies as well as the loss of any benefits that customers are currently enjoying through lower credit prices. We conclude that the cost of implementing our remedies is justified by the increased competition and reduced consumer detriment that they would give rise to.
8. We expect that our remedies will include a transition period of no more than 12 months. We consider that 12 months would allow affected parties enough time to implement all the proposed remedies, though we would expect that some elements of the package, such as annual statements, could be implemented in six months.
9. The CC invites views in writing on the provisional decision and its underlying analysis by 5pm on **4 December 2008**. Interested persons should also note that we have specifically invited further representations about implementation costs and other factors regarding the detailed implementation of the remedies in paragraphs 159, 163, 178, 367, 371 and 392.

Introduction

10. The Notice, published on 5 June 2008, set out various options that we considered might be effective, alone or in combination, in addressing the AEC that we provisionally found, or in addressing the customer detriment resulting from the AEC.
11. We received 51 written responses to the Notice; non-confidential versions of these can be found on our website. In addition, we held 23 remedies hearings with main parties to the inquiry, consumer bodies, the OFT and the FSA. We also received evidence from credit reference agencies (CRAs) and others (see Appendix 1 for a complete list of parties that responded to the Notice). In addition, we commissioned a survey into customer views on price disclosure and asked the larger parties a number of additional questions about their claims profiles over the life of the single-premium policies. On 14 October, we consulted on some further analysis conducted by the CC in support of our provisional decision on remedies, to which we received 23 responses. We have considered carefully all the evidence we have received.
12. We have now come to a provisional decision as to the package of remedies we consider would be effective and proportionate in addressing the AEC and customer detriment identified. This paper sets out this proposed package of remedies and provides reasons as to why we consider that the package and the individual options will be effective. These proposals should all be regarded as provisional and will be reviewed following further representations.

The provisional findings

13. In our provisional findings, published on 5 June 2008, we concluded that features of the market, either alone or in combination with each other, prevented, restricted or

distorted competition in the supply of PPI in the UK,¹ and that these gave rise to an AEC within the meaning of section 134(2) of the Enterprise Act 2002 (the Act). These features, which are summarized in Section 8 of the provisional findings, are that:

(a) Distributors and intermediaries² fail actively to seek to win customers 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 IP policies are hindered in doing so.

Product complexity (the variations 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. 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 PPI providers or to alternative insurance products 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

¹The reference from the OFT specifies 'the supply of all payment protection insurance services except store card payment protection insurance services'. In its provisional findings published on 5 June 2008, the CC considered that the supply of payment protection insurance includes a range of products, including the provision of short-term income protection (short-term IP), the provision of CCPPI, PLPPI, SMPPI and MPPI. Retail PPI was included in the scope of that Remedies Notice, while work continued to determine the CC's provisional view on it. Following publication of the CC's provisional findings in relation to retail PPI on 10 October 2008, a Supplementary Remedies Notice relating to retail PPI was published for consultation on the same day. Overdraft PPI is excluded from the scope of this Remedies Notice as the CC has not provisionally found an AEC in relation to this type of PPI.

²For the purposes of this investigation, distributors are lenders (for example, banks, mortgage providers, credit card providers, motor finance companies) which offer PPI alongside their underlying credit products, either at the point of sale or subsequently (mostly in the case of CCPPI and retail PPI). CCPPI is predominantly sold either when the credit card is sold or when it is activated. We consider both of these times to be a point of sale for the purposes of this investigation. Lenders can also offer PPI on a stand-alone basis. An intermediary is a third party that offers services between PPI suppliers and consumers. Intermediaries means agents through whom consumers identify a suitable type of PPI policy, whether with or without an associated credit product. In this context, intermediaries are only used to purchase MPPI, to a lesser extent SMPPI, and some motor PPI. Intermediaries can distribute both credit products and PPI (and other insurance policies) or PPI alone. However, they neither underwrite the PPI policies nor finance the credit. Intermediaries make available to customers the credit products and PPI of one or more credit providers and/or underwriters. These types of insurance policies can be distributed under the brand name of the credit provider or of the underwriter. The evidence we have received indicates that intermediaries sell significant numbers of only one form of PPI, namely MPPI.

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. 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 further restricts the extent to which other PPI providers can compete effectively.

14. Section 8 of the provisional findings also identified the detrimental effects on customers which resulted from, or might be expected to result from, the AEC. Namely, we considered that prices were higher, there was less choice and possibly a lower degree of innovation than we would expect to find in a competitive market.
15. We have not, at this stage, made a final decision regarding the existence and form of the AEC and resulting customer detriment. However, for the purposes of this document, we have maintained the working assumption that the AEC and customer detriment are unchanged from that outlined in the provisional findings. Our final decisions on any AEC, and appropriate remedies, will take into account responses to our provisional findings and to this provisional decision on remedies.

Framework for the assessment of remedies and relevant customer benefits

16. Having identified a set of features of the markets for the supply of PPI in the UK that give rise to an AEC, the CC has a duty to consider what, if any, action should be taken to remedy the adverse effect and resulting customer detriment. As well as taking action itself, the CC may recommend that action be taken by others.

17. The CC is required by the Act³ 'in particular to have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition and any detrimental effects on customers so far as resulting from the adverse effect on competition'. Such detrimental effects may affect existing or future customers and must be in the form of higher prices, lower quality, less choice or less innovation in relation to goods or services in any UK market (whether or not in the market to which the feature or features concerned relate).⁴ As noted in its guidance *Market Investigation References: Competition Commission Guidelines, CC3* (paragraph 4.9): 'when deciding what is an appropriate remedy, the Commission will consider the effectiveness of different remedies and their associated costs and will have regard to the principle of proportionality'.
18. CC3 makes several general observations about factors relevant to its consideration of effectiveness (CC3, paragraph 4.13 et seq):
- (a) first, the CC will 'consider whether it is possible to devise a remedy that is both clear and not overly intrusive in its regulation of a firm's behaviour';
 - (b) secondly, in considering its effectiveness, the CC will consider the prospects of a particular remedy being implemented and complied with; and
 - (c) a third relevant consideration is the timescale within which the effects of any remedial action will occur.⁵

The CC will take full account of the OFT's functions in terms of monitoring remedies and regulating the consumer credit market (CC3, paragraph 4.15). Other factors may also be relevant to the CC's consideration of effectiveness, depending on the facts of the case.

³Section 134(6).

⁴Section 134(5).

⁵The guidance says (CC3, paragraph 4.23) that 'if the remedy is not likely to have speedy results, the Commission may choose an alternative remedy or implement additional remedies such as those to remedy the detrimental effects on customers during the interim period. Otherwise, not only might there be uncertainty as to whether the effects would ever materialise, but in the meantime customers would continue to suffer from the consequences of the adverse effects on competition.'

19. The guidance also makes the following points regarding proportionality. In considering whether a remedy is reasonable and practicable, the CC will consider the cost associated with implementing the remedy (CC3, paragraph 4.10). The CC will endeavour to minimize any ongoing compliance costs to the parties, subject to the effectiveness of the remedy not being reduced (CC3, paragraph 4.12). However, the CC will balance those costs against the benefit to the UK economy and to customers in particular. In 'choosing between two remedies which it considers would be equally effective, it will choose the remedy that imposes the least cost or that is the least restrictive' (CC3, paragraph 4.10).
20. Other relevant points in the guidance outline what remedies can address, and the likelihood of remedial action in a market in which the CC finds an AEC. The CC 'will seek to implement (or recommend) remedies that address the cause of the problem, it may also choose to address the detrimental effect on customers in addition or as an alternative' (CC3, paragraph 4.6). However, the CC is prevented from taking action to address future (rather than existing) detrimental effects on customers if it is not also remedying the AEC (section 138(6) of the Act). Although it remains an option, 'it is unlikely that the Commission, having decided that there is an AEC, will decide that there is no case for remedial action, at least before it has given attention to any relevant customer benefits that may accrue from the market features'.
21. The guidance also sets out that we may have regard to relevant customer benefits (see paragraphs 23 to 25).

Structure of this document

22. The remainder of this decision document is structured as follows:

- (a) First, we consider whether there are any relevant customer benefits arising from the current market structure and features which would be lost if we imposed remedies (paragraphs 23 to 112).
- (b) We then consider whether we should seek to ensure that we retain any such benefits by modifying remedies to maintain the benefit to customers (paragraphs 113 to 121).
- (c) Next we consider general issues regarding the market which, it has been put to us, we should consider when deciding what remedies, if any, to impose (paragraphs 122 to 141).
- (d) We then look at the remedy options we have provisionally decided should form part of the overall remedies package. For each of these we set out the original remedy option consulted on, summarize the responses received on the option, and our views on the points made, and then set out how we envisage the remedy should be formulated (paragraphs 145 to 346).
- (e) Next we set out the remedy options we do not propose to implement, summarizing the responses to the Notice received on those options and why we are not taking them forward (paragraphs 347 to 363).
- (f) We then look at the issues relating to the implementation of the proposed remedies package (paragraphs 364 to 372).
- (g) Finally, we assess the overall effectiveness and proportionality of the proposed remedies package (paragraphs 372 to 400).

Relevant customer benefits

23. 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'.⁶ Relevant customer benefits are limited to benefits to relevant customers in the form of:

- '(i) lower prices, higher quality or greater choice of goods or services in any market in the United Kingdom (whether or not the market to which the feature or features concerned relate); or
- (ii) greater innovation in relation to such goods or services.'⁷

24. A benefit is only a relevant customer benefit if the CC believes that:

- '(i) the benefit has accrued as a result (whether wholly or partly) of the feature or features concerned or may be expected to accrue within a reasonable period as a result (whether wholly or partly) of that feature or those features; and
- (ii) the benefit was, or is, unlikely to accrue without the feature or features concerned'.⁸

25. If the CC is satisfied that there are relevant customer benefits deriving from a market feature, the CC will consider whether to modify the remedy that it might otherwise have imposed or recommended. When deciding whether to modify a remedy, the CC will consider a number of factors including the size and nature of the expected benefit and how long the benefit is to be sustained (CC3, paragraph [4.39](#)).

26. We considered whether there are any relevant customer benefits which we should take account of in formulating our remedies.

27. In our provisional findings we identified four categories of features of the supply of PPI that lead to an AEC. Parties put forward potential relevant customer benefit arguments in relation to two of these features:

⁶Enterprise Act 2002, [section 134\(7\)](#).

⁷Enterprise Act 2002, [section 134\(8\)](#).

⁸Enterprise Act 2002, [section 134\(8\)](#).

- The point-of-sale advantage—in particular, that the point-of-sale advantage may result in lower costs for distributors and therefore lower prices, higher quality and/or greater choice.
 - Switching costs—in particular, that the switching costs associated with the rebate terms for single-premium policies may result in lower costs for distributors and therefore lower prices, higher quality and/or greater choice.
28. In addition, parties put forward a potential relevant customer benefit for all credit customers; that credit prices are lower than they would be if PPI were not sold alongside credit.
29. Moreover, Lloyds TSB told us that, if we adopted remedies designed to incentivize distributors to price credit and PPI combinations more efficiently, that would be likely to result in cost savings associated with selling PPI at the point of sale being passed on, at least in substantial part, to consumers. However, whilst selling PPI at the point of sale may be more efficient for distributors, we found that any cost savings are not currently being passed on (see paragraph 5.119 of our [provisional findings](#)). There is, therefore, no relevant customer benefit to be retained.
30. We set out the relevant customers benefits put to us, and our views on them, below:
- (a) First, we consider the potential customer benefits arising in PPI markets from credit providers having a point-of-sale advantage.
 - (b) We then consider the potential benefits for PPI policy-holders relating to single-premium policies.
 - (c) We next consider whether there is a relevant customer benefit associated with credit providers knowing that a customer is taking out PPI.
 - (d) Finally, we consider the potential benefits arising in the credit market.

Potential customer benefits of the point-of-sale advantage

Lower PPI prices

31. The parties put forward a number of reasons why, all else being equal, distributors may have incentives to reduce their PPI prices when sold at the point of sale. The key reasons put forward were:
- (a) selling PPI and credit together eliminates double marginalization;⁹
 - (b) selling PPI at the point of sale enables firms to realize economies of scope and thereby reduce costs; and
 - (c) selling PPI at the point of sale increases the volume of sales allowing firms to realize economies of scale and thereby reduce costs.
32. We concluded that it was unlikely that these claimed efficiencies could constitute relevant customer benefits, within the meaning of the Act, for two reasons.
33. First, given the lack of a competitive threat in the markets for PPI, it appears to us that these benefits are not passed on to consumers in the form of lower PPI prices. In light of our analysis of profitability of PPI policies, which showed that distributors representing a substantial part of the share of supply of PPI have earned profits that were persistently and substantially in excess of the cost of capital and led us to conclude that PPI prices are higher than they would be in a well-functioning market (see paragraphs 4.79 and 4.93 of our [provisional findings](#)), we concluded that consumers were not seeing any benefit in the form of lower PPI prices.
34. Second, it does not appear that selling at the point of sale is strictly necessary to realize all of these efficiencies—some are also capable of being realized, to an appreciable level, by selling after a suitable interval.

⁹Double marginalization occurs where separate firms sell complementary products. Each firm sets prices with regard to the effect of its own prices on its own sales. However, as the products are complements, the prices that one firm sets will affect the sales of the other, as well as its own sales. When prices are by a single firm, these external effects can be taken into account, and the result is lower prices.

35. We therefore concluded that lower PPI prices arising as a result of potential cost savings at the point of sale is not a relevant customer benefit. We consider whether any benefits are passed on in the form of lower credit prices in paragraphs 82 to 112.

Increased customer choice

36. Some parties told us that remedies to address the point-of-sale advantage would reduce consumer choice as they would remove the option from customers of purchasing PPI at the point of sale.
37. We note that the relevant question, for the purposes of evaluating whether point-of-sale advantage results in a relevant customer benefit, is whether the point-of-sale advantage delivers a benefit to consumers in the form of increased choice.
38. We do not believe that the point-of-sale advantage results in increased choice for consumers. Indeed in our provisional findings we found that the reverse was true and that the point-of-sale advantage acted as a barrier to other PPI providers competing for customers of any given distributor or intermediary.¹⁰ We found that because of this lack of competition, customers had in effect only one choice, to purchase PPI from their credit supplier or to purchase no insurance at all.
39. We recognize that remedies to address the point-of-sale advantage may result in some (albeit modest) restriction in customers' purchasing freedom, in that there would be a temporary restriction in buying PPI from the credit supplier. However, we believe that, by enabling more suppliers to compete for consumers' business, these remedies will increase customer choice overall.

¹⁰Provisional findings, paragraph 5.116.

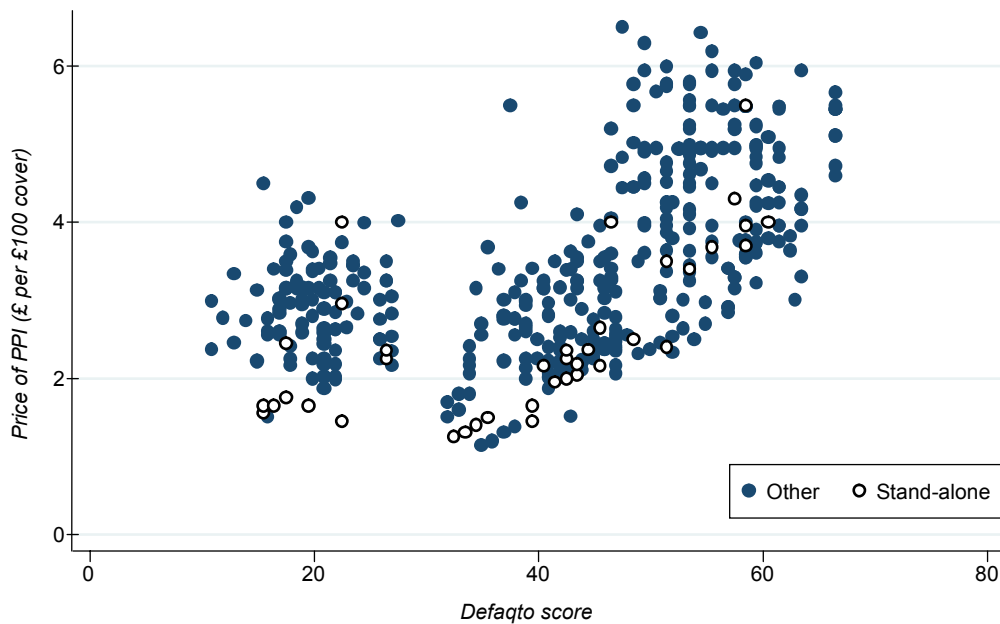
Better-quality regular-premium PPI products

40. Some parties told us that policies sold at the point of sale were generally of higher quality than those sold on a stand-alone basis. For example, Aviva told us that policies sold at the point of sale were capable of providing more exhaustive insurance cover than stand-alone policies. We considered this separately for regular-premium policies and single-premium policies (see paragraphs 46 to 60 for our analysis of whether single-premium policies result in lower-priced or higher-quality products).
41. We looked at the price and quality of PPI policies sold at the point of sale and on a stand-alone basis. Figure 1 shows the results of this analysis for MPPI policies.¹¹ We found that, once differences in price are accounted for, there is no evidence that stand-alone policies are more highly priced (for a given level of quality), or offer lower quality (for a given price) than policies offered at the point of sale. If anything, our observation of the data in Figure 1 indicates that the opposite appears to be true. We also found that stand-alone policies offer a wide range of product quality, and that some were of higher quality than most policies sold at the point of sale of the mortgage.

¹¹We chose to compare MPPI policies because both point-of-sale and stand-alone MPPI policies are charged on a regular-premium basis. Stand-alone PLPPI and point-of-sale PLPPI are more difficult to compare because point-of-sale PLPPI is typically charged as a single-premium policy whereas stand-alone PLPPI tends to be regular-premium policies.

FIGURE 1

Comparison of price and Defaqto quality scores of stand-alone and non-stand-alone MPPI policies



Source: Defaqto Aequos database.

42. Finally, and importantly, we found in our provisional findings that the point-of-sale advantage was a feature of the supply of PPI that resulted in a prevention, restriction or distortion in competition. We note that where firms are insulated from competition they face weaker incentives to offer higher-quality products for a given price.
43. We therefore conclude that the point-of-sale advantage does not lead to a relevant customer benefit in the form of higher-quality products.
44. RBSG said that we should recognize the customer benefit of the availability of high-quality products from integrated providers. However, as our remedies do not preclude sale of PPI products by distributors, we did not consider it necessary to consider whether there was a relevant customer benefit to be maintained.

Potential relevant customer benefits of a single-premium charging structure

45. We were given two reasons why a single-premium charging structure might result in relevant customer benefits. First, we were told that charging a single premium was more efficient, and that consequently distributors' costs were lower, resulting in lower prices, higher quality and greater choice for consumers. Secondly, we were told that there were advantages for customers of single-premium policies because the single-premium charging structure allowed distributors to offer a greater continuity of cover in the event of missed payments.¹²

Efficiency of charging single premiums

46. We were told that single-premium charging was more efficient than a regular-premium charging structure and that, consequently, this allowed providers to offer lower prices and/or better-quality products than would be the case under a regular-premium charging structure. A similar argument would apply to potential changes in the rebate structure for single-premium policies, for example moving to a pro-rata rebate structure.
47. The main reason put forward as to why single premiums and their associated rebate structure offer efficiency benefits, or lower costs, was because of the profile of the risk on a policy over the life of that policy. Many parties told us that the incidence and value of claims was higher in the early part of the loan and that therefore the risks covered by the policy were higher in the early months of the policy.
48. The parties told us that, given this uneven claims profile, the simplest and most logical response was to charge a single premium and provide a rebate for the unexpired cover upon early termination. This rebate is non-linear because of the

¹²HSBC said that the availability of single-premium policies did not give rise to relevant customer benefits that could not be replicated by regular-premium policies. It told us that HFC had just launched a regular-premium PLPPI policy sold at the point of sale.

uneven risk profile, so the value of the cover provided in the earlier months of the policy is greater than the value of cover provided in later months.

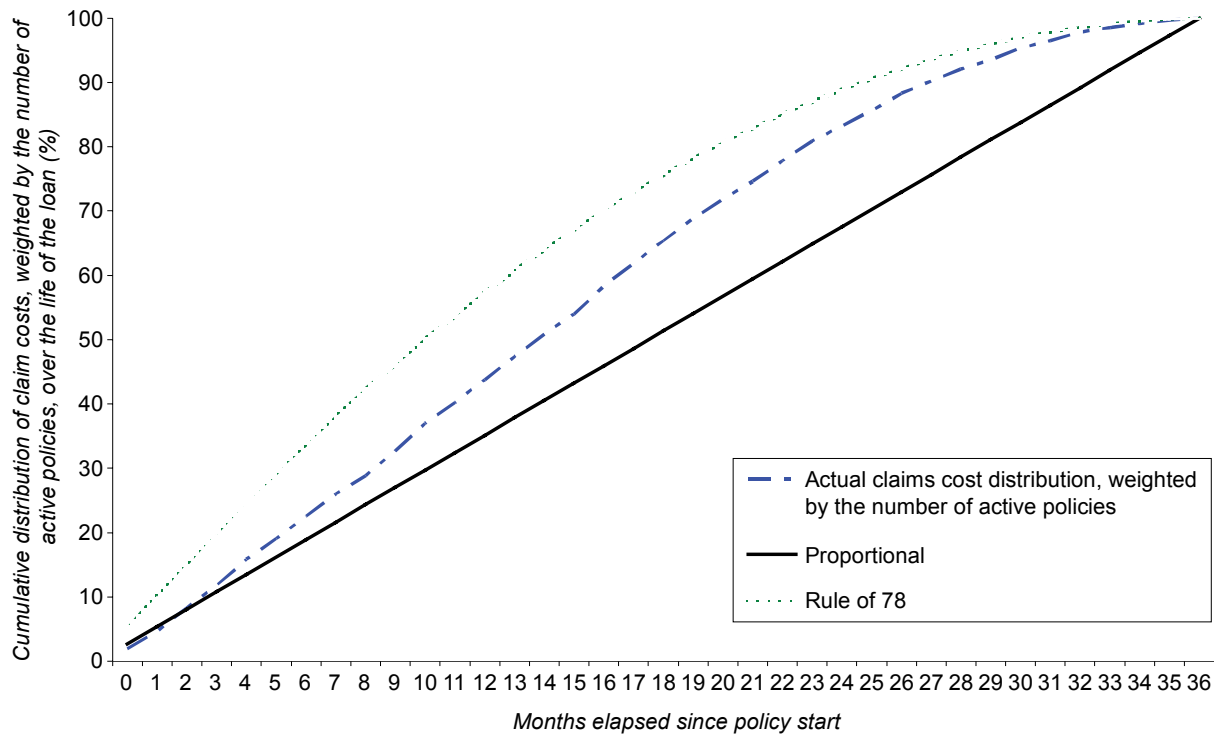
49. Under a regular-premium structure, or with pro-rata rebates, those terminating the policy early would receive greater cover, in proportion to the premium they had paid, than those holding the policy for longer. The only way to reduce the impact of this, we were told, would be to reduce the benefits on offer to try and ‘flatten’ the risk profile to make it more like a pro-rata rebate profile. RBSG said that the premium could be amortized, so that the premium varied across the life of the loan (starting higher and falling). Everydayloans told us that it sold a monthly premium product whereby the premium was calculated as a percentage per month of the balance outstanding on a fixed-term regular-repayment unsecured loan. This would generate a reducing premium through the life of the loan. However, other parties told us that charging a reducing premium for regular-premium PPI was not a suitable approach. Aviva said that one of its partners had launched a product that had had a reducing premium. However, it had stopped because it was too complex, in terms of administration and systems, and there had been a lot of problems around sales processes and explaining the premium to customers. HBOS said that the point when customers borrowed money was not the most propitious moment to charge larger premiums, and that it did not seem terribly customer friendly.
50. We analysed the data on claims. Details of this analysis are set out in Appendix 2. We obtained claims profile data for 36- and 60-month single-premium policies from five large distributors.
51. We noted first that claims costs make up a small proportion of the overall income earned on single-premium policies. In our [provisional findings](#) (paragraph 4.49) we found that, based on data from the six largest underwriters, the average claims ratio

over the five-year period 2002 to 2006 for PLPPI was 15 per cent. Any cost efficiencies associated with the claims profile on single premiums are therefore likely to be small relative to the current prices of single-premium PPI policies.

52. Our analysis of the profile of claims on these single-premium policies showed that there is evidence that there are more claims in the early part of a policy (an effect which was more pronounced for the 60-month loans than the 36-month loans). There was a more pronounced skew in the *value* of claims in the earlier months of a policy than there was in the *incidence* of claims. However, since a substantial proportion of loans are settled early, we would expect more claims to occur in the early part of the original loan period, in any case, even if there were no difference in risk profile.
53. We therefore weighted the distribution of claims costs by the number of policies that were still active at different points in the loan, by dividing the total lifetime cost of claims occurring in each month by the number of policies which were active in that month. We compared the weighted claims profiles of the five large distributors to the rule of 78, which is used for assessing risk by many distributors for calculating refunds (others use actuarial calculations which give very similar profiles—see paragraph 5.67 of our [provisional findings](#)) and to a ‘proportional’ distribution in which the profile of claims is not affected by the length of time that the customer has held the loan. The results are shown in Figures 2 and 3.

FIGURE 2

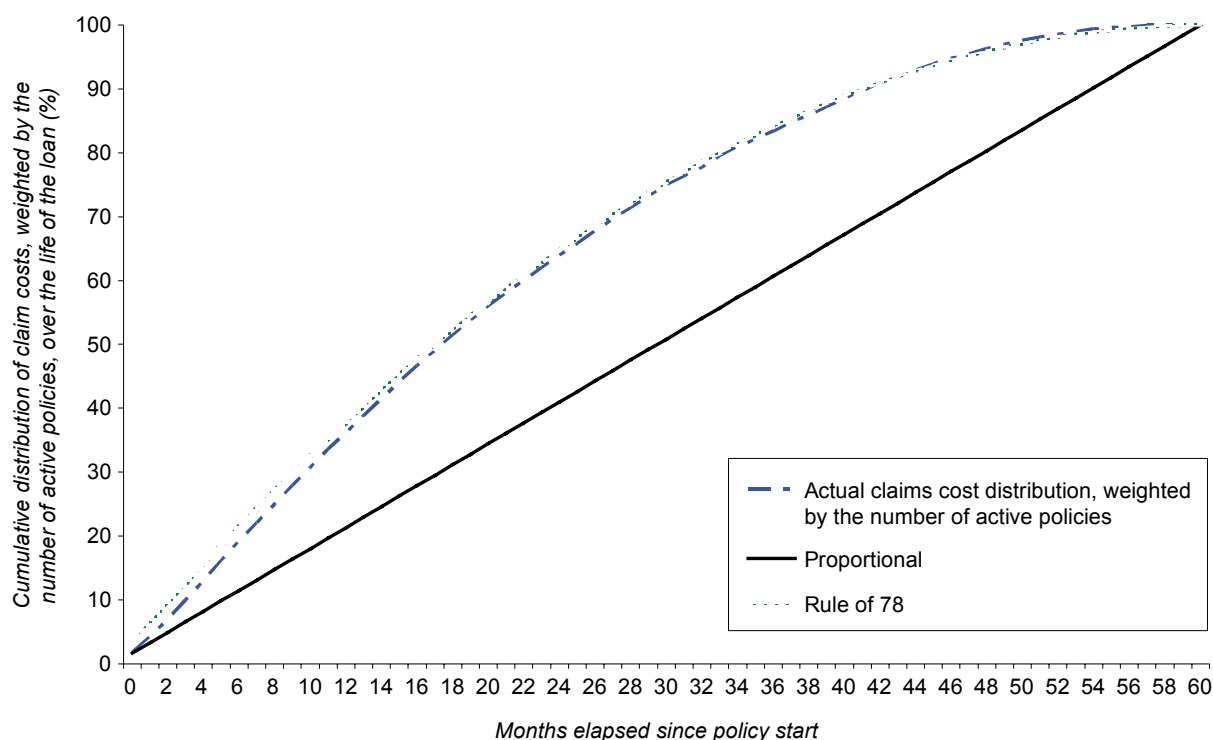
Cumulative distribution of claim costs, weighted by the number of active policies, across the life of the loan: combined sample of 36-month PLPPI policies



Source: CC analysis of data provided by the large distributors.

FIGURE 3

Cumulative distribution of claim costs, weighted by the number of active policies, across the life of the loan: combined sample of 60-month PLPPI policies



Source: CC analysis of data provided by the large distributors.

54. We found that the claims profile for 36-month PLPPI policies was between a straight-line profile and the rule-of-78 profile—that is to say, while skewed towards earlier in the loan term, the asymmetry in claims was not as pronounced as implied by a rule-of-78 rebate for these policies. For 60-month PLPPI policies we found that the rule of 78 was a reasonable reflection of the claims profile over the loan term. We also analysed some data for 60-month SMPPI policies, and concluded that the distribution of claims costs over the length of the loan most likely lay somewhere between that implied by a proportional distribution of claims and that implied by the rule of 78 (see paragraphs 19 to 24 of Appendix 2). Finally, we found that the claims profile for personal loans offered by two large non-standard lenders ([X] and [X]) displayed a similar degree of asymmetry to standard personal loans, although in one case ([X] 36-month PLPPI policies taken out in 2004) the claims profile skew was more

accentuated than that allowed for by the rule of 78 (see paragraphs 25 to 30 of Appendix 2).

55. This indicated to us that offering a rebate on single-premium policies based on the rule of 78 was overly generous to underwriters as an allocation of claims costs over time for shorter-term policies (36 months), but was a reasonable approximation of the profile of claims for longer-term policies (60 months).
56. To evaluate the scale of any cost efficiencies associated with single-premium policies, we considered how much claims costs and prices might increase if single premiums were replaced with regular premiums or if pro-rata rebates were given. Our analysis took into account both the claims profiles we found, and our observation that claims costs make up a small proportion of the overall income earned on single-premium policies (see paragraph 51). We found that the monthly average of the lifetime value of claims costs per active policy in the first year of the loan was about 24 per cent higher than the monthly average of the lifetime value of claims over the entire term for 36-month PLPPI policies, and just over 70 per cent higher for 60-month PLPPI policies. Our analysis suggested that the differential could be slightly greater for non-standard lenders—[>75] per cent for [X] 36-month PLPPI. This would seem to represent the maximum extent to which claims costs could increase as a result of a move to a regular-premium, or pro-rata rebate, structure, corresponding to the unlikely situation in which all customers switched within the first 12 months of a loan.
57. We calculated an upper bound to the extent to which prices to consumers might rise as a result of any cost increase as a result of increased claims costs. This was calculated assuming that a switch to regular-premium charging or a pro-rata rebate would lead to an extreme result whereby all customers switched within a year of

taking out their policy, that all of the additional cost from claims as a consequence was passed on to consumers and that there was no downward pressure on PPI prices as a result of increased competition. We regard these assumptions as extremely unrealistic and in practice we would expect much lower levels of switching, a smaller increase in claims costs and an increase in competitive pressure.

58. We found that even under these extreme assumptions the price effect was likely to be modest. Our calculations showed that this could represent a maximum price increase of less than 6 per cent for 60-month PLPPI, and slightly above this (up to 7.5 per cent) for non-standard lenders.
59. We were also told that single-premium policies were able to offer enhanced cover compared with regular-premium policies, such as accident and sickness cover which lasts for the duration of the policy rather than for a maximum of 12 months. However, we concluded, and were told by one party (Lloyds TSB¹³), that if these different offers were valuable to consumers, it would be possible to find a way of pricing regular-premium policies that would allow them to be offered as part of a regular-premium policy.
60. We therefore concluded that the limited cost efficiencies that arose as a result of single premiums did not constitute a relevant customer benefit within the meaning of the Act. Without a competitive threat to distributors when selling PPI to their own credit customers, there would seem to be little incentive for distributors to pass these benefits on to consumers. To the extent that any cost efficiencies are currently passed on to customers, this is more likely to appear as lower credit prices, which we consider in paragraphs 82 to 112.

¹³See also comments in footnote 12.

Continuity of cover for single and regular premiums

61. We considered whether there was a relevant customer benefit associated with continuity of cover guaranteed by having a single premium.
62. We asked distributors to tell us the proportion of regular-premium customers that missed a regular-premium payment. We found that there was a relatively wide range in estimates of the incidence of missed payments between types of PPI and between distributors. Estimates of the proportion of MPPI customers that had missed one or more MPPI payments in 2007 were between 2.3 per cent ([redacted]) and 17.5 per cent ([redacted]). For CCPPI, estimates were generally higher, with, for example, [redacted] and [redacted] reporting that around 30 per cent of their customers had missed one or more payments in 2007.
63. We also found a wide variation between distributors in their approach to customers' cover in the event of missed payments. [redacted], [redacted] and [redacted] told us that they cancelled or suspended cover either immediately or within seven days of either the missed payment or the second request for that payment. Other distributors continued cover for longer. For example, [redacted] will cancel MPPI cover after a period of around five weeks from the missed payment. [redacted], [redacted], [redacted], [redacted] and [redacted] said that their cover would continue from between 30 and 90 days from the first missed payment. Finally, [redacted] told us that, for MPPI, it treated missed premium payments as arrears, that it did not cancel or suspend cover and that missed premiums would not prevent the customer from making a claim.
64. As noted in paragraph 2.76 of our [provisional findings](#), the Financial Ombudsman Service (FOS) told us that it would have doubts about whether it would be fair or reasonable to cancel a policy immediately if only one or two payments were missed.

65. It was also suggested to us that single-premium policies prevented companies from withdrawing cover. For example, London General Insurance noted that in unstable economic times the insurer remained bound by the terms of the agreed policy and was unable to withdraw cover, unlike regular-premium policies. We were told that there had recently been some changes in regular-premium policies because of changing economic circumstances. Aviva told us that, in light of a significant increase in sales of a Paymentsshield unemployment-only PPI by British Insurance following the turmoil in the financial markets from mid-September 2008, it had withdrawn that policy from the market, and it was considering what to do about the significant number of ASU policies being sold by British Insurance since the unemployment-only policy was withdrawn. British Insurance told us that it had been able to source a new underwriter. Aviva told us that it thought that a significant proportion of consumers buying these policies were doing so in response to a specific trigger event, and would be at risk of making a claim. More generally, Cattles referred to us some media articles which it told us showed the benefits of single-premium policies over regular-premium ones.
66. With increased competition, we would expect the general level of quality of PPI policies to increase, as firms seek to win and retain customers by offering better terms and better prices. We see no reason why this should not also include the nature of terms such as the continuation of cover in the event of missed payments. Given this, the evidence that many providers already offer a significant grace period if a payment is missed, and the views of the FOS, we concluded that there was not a relevant customer benefit associated with continuity of cover offered by single-premium policies.
67. We noted the views expressed on the ability of regular-premium providers to withdraw cover. We agreed that single-premium policies lock the underwriter in to

providing the cover sold, even when there is a change in economic circumstances, and noted that the underwriter charges a premium taking account of this. However, if this guaranteed cover were something to which consumers attached significant importance, we saw no reason why suitably-priced regular-premium policies could not be designed with clauses guaranteeing cover for the duration of the policy.

Knowledge by credit providers that a customer will take out PPI

68. It was put to us that customers who take out PPI are, even with PPI, more likely to go into arrears or default on credit repayments than those who do not take out PPI. We were told that this could be used to help determine parties' lending strategies.
69. [X] told us that its insured portfolio is inherently more risky than its non-insured portfolio. The net loss rate for [X] insured credit card book is projected to be 8.7 per cent, whilst it is only projected to be 3.5 per cent for its uninsured book. It told us that any changes to its PPI income or portfolio would impact on its overall business and lending strategy.
70. HSBC said that an important benefit of selling PPI at the credit point of sale was the additional information that take-up of PPI provided in identifying higher-credit-risk customers, allowing customers to benefit from access to affordable protected credit, which may not otherwise have been available. It said that PPI customers incurred significantly higher bad debt than non-PPI customers despite their PPI cover, and that its analysis showed that take-up of PPI was a powerful independent indicator of bad debt propensity. It told us that, in the absence of being able to sell PPI at the point of sale, lenders would be substantially less able to identify different risk categories, leading to the inability to supply credit to higher-risk customers at all.

71. Finally, Capital One said that PPI revenue was integrated into its pricing methodology when calculating rates of return. Although this resulted in lower credit prices to all customers, it said that it typically observed higher losses for customers with PPI than those without, and that this would need to be taken into account in examining whether ultimately there was a material cross-subsidy between these two groups.
72. Two potential efficiency gains associated with this difference in credit risk might arise, related to providers' ability to identify which credit customers intend to purchase PPI, and to charge these individuals higher prices in order to account for the extra risk they present. First, the extra information about a customer's risk of default which lenders are able to infer from their decision to purchase PPI could allow differentiated prices to be charged to those credit customers who intend to purchase PPI, and those who do not. If so, these prices could be more efficient, better reflecting the costs associated with providing credit to the two groups. Secondly, the extra information could serve to offset an asymmetry in the information available to lenders and borrowers, reducing an adverse selection effect in the credit market and allowing the lender to provide credit to a greater number of customers.
73. We consider these issues in more detail in our working paper 'The impairment experience of insured and non-insured credit customers and the use of this data'. For the purposes of our provisional decision on remedies, we focus here on whether credit or PPI prices are at their current levels because distributors are reflecting the additional risk associated with PPI customers in higher credit or PPI prices, and, if so, whether this should constitute a relevant customer benefit.
74. We looked first at whether PPI customers are at higher risk of default on credit repayments than credit customers who do not take out PPI. For personal loans, we found that customers who took out PPI were more at risk of going into arrears or

defaulting on credit repayments than non-PPI customers. This difference in impairment experience was largely confined to credit customers with higher risk scores.

75. For mortgages, we were only able to obtain a small sample (most providers were unable to tell us which of their mortgage customers had PPI), but analysis of this sample showed that those mortgage-holders with PPI were also more likely to go into arrears or have their mortgages written off than non-PPI customers.
76. For credit cards, we again found that customers with PPI were more likely to go into arrears or default on repayments than non-PPI customers, with the value of protected credit card balances being written off approximately twice as high as the value of unprotected credit card balances written off, even after controlling for the difference in risk already observed, captured in credit risk scores.
77. We concluded, therefore, that PPI credit consumers—and those with higher risk scores in particular—were more likely to enter into arrears or default on credit repayments than credit consumers without PPI.
78. We considered whether this higher risk was reflected in credit pricing. Nearly all distributors we spoke to told us that whether a customer was going to take out PPI had no impact on the credit decision,¹⁴ and those distributors which did factor the decision to take out PPI into the credit-approval decision said that it was a minor factor. We noted that if the approval of credit was contingent on taking out PPI, the APR offered would have to be based on the cost of both credit interest and PPI, and that no providers currently offer credit contingent on taking out PPI. We concluded,

¹⁴There were some exceptions to this. [§] has recently introduced whether or not a customer requests PPI when signing up for their credit card as a variable in assigning their risk score. [§] told us that the intention to take out PPI affected whether a customer would be accepted for credit. One distributor ([§]) provided us with a presentation that showed that it had modelled the probability of default on loans with and without PPI and had considered reflecting this in the pricing of personal loans.

therefore, that the higher risk associated with PPI customers was not generally reflected in individualized higher credit pricing for those customers.

79. We also considered whether PPI prices are higher than they need to be to cover costs of supplying PPI because distributors reflect the increased risk of credit default among PPI customers in the price set for PPI.
80. We received no clear evidence to suggest that the impairment experience of insured versus uninsured customers was taken into account when providers made their decision about what PPI price to set.¹⁵ Indeed, even [§]—which out of the three parties that raised the potential issue of impairments spelt out the argument in most detail—said that it ‘wouldn’t be right ... to say that we explicitly allowed for [the extra bad debt offered by protected customers] in the pricing of PPI’ when we asked it if it priced PPI to take account of default risk. Because of this, there would seem little reason to believe that current PPI prices have explicitly been set at the level associated with the extra impairment risk presented by these individuals.
81. Whilst we found that taking out PPI can indicate an increased likelihood of defaulting on credit repayments, especially for customers in higher risk bands, we did not find evidence that this information was consciously used by distributors to set either credit or PPI prices more efficiently, by charging these customers higher prices either for credit or PPI. We concluded, therefore, that, as this information was not used, there was no relevant customer benefit being lost if distributors would not find out when selling credit whether or not a consumer would take out PPI.

¹⁵One credit card provider ([§]) told us that one factor taken into account when setting the price of PPI was the overall economics of credit cards.

Lower credit prices

82. Many parties put to us that prices for credit were lower than they would otherwise be because profits made on PPI policies were competed away in the form of lower credit prices. Where firms make profits in secondary markets, and prices in the primary market affect sales of secondary products, firms have an incentive to discount the price of their primary market products in order to increase sales of the secondary product. This is sometimes referred to as a 'waterbed effect'. A similar argument was put to us regarding availability of credit; the sale of PPI allows distributors to offer credit to (higher-risk) customers to whom they would not otherwise offer credit.
83. We considered whether credit prices took account of profits made in the sale of PPI, and if so what the likely scale of the price reduction in credit might be. We expected that, if a waterbed effect existed, it would have a larger impact on personal loan prices (in particular, unsecured personal loans) because the price of PPI is often larger than the interest payable on the loan (see paragraph 2.68 of our [provisional findings](#)) and a higher proportion of credit sales have PPI attached than for mortgages and credit cards.
84. We considered evidence from a range of sources: the views of distributors, their internal documents, what their financial models predicted if PPI incomes were reduced, an analysis of the profitability of the bundle of credit and PPI, and econometric analysis of distributors' sales data to see if credit prices were affected by changes in PPI income.

The views of distributors

85. Distributors told us that a reduction in PPI income would result in major changes to distributors' (secured and unsecured) personal loan businesses (in terms of higher prices and/or higher credit score cut-offs); for other forms of credit, we were told that

PPI generated a much smaller proportion of overall revenue and so would not result in such major changes. Details of their views are set out in Appendix 3.

Distributors' internal documentation

86. As noted in paragraph 4.85 of our [provisional findings](#), some distributors' internal documents showed that PPI income has influenced pricing decisions for personal loans, has influenced lenders' determinations of credit score cut-offs, and that some segments of customers within low credit score bands would be unprofitable were it not for PPI income earned within that segment.

Distributors' financial models

87. The majority of distributors told us that they used financial models either in setting their credit prices or in a higher level evaluation of the profitability of their credit businesses. Where distributors said that PPI income affected their credit pricing, we asked them to undertake a modelling exercise, using their existing models to assess the impact of reductions in PPI income.
88. We asked the distributors to estimate, for a given reduction in PPI income, the extent to which their non-PPI income would need to increase in order to achieve the same rate of return as they had achieved absent that reduction in PPI income (see Appendix 3 for more details).
89. Under a full waterbed scenario, where all of the distributors' PPI profits are competed away in the credit market, we would expect distributors' overall system profits to be the same regardless of the level of PPI income. The modelling exercise therefore gives an estimate of the upper bound of the scale of any distortion of credit prices:

- Estimates of the increases in APRs necessary to compensate for a 100 per cent reduction in PPI income, across the personal loans portfolio,¹⁶ ranged between two percentage points ([REDACTED]) and five percentage points ([REDACTED]).¹⁷ Estimates of the extent to which non-PPI personal loan income would need to rise to achieve the same level of profitability, given a 100 per cent reduction in PPI income, ranged from 13 per cent ([REDACTED]) to 93 per cent ([REDACTED]).
- For credit cards, the estimates of the increase in non-PPI income that would be required to achieve the same level of profitability were much lower. Estimates of the increase necessary to compensate for a 100 per cent reduction in PPI income ranged from 1 per cent ([REDACTED]) to 22 per cent ([REDACTED]). In all cases, distributors gave a lower figure for credit cards than for personal loans in their responses.
- Only three distributors were able to provide a response relating to second-charge mortgages—[REDACTED], [REDACTED] and [REDACTED]. [REDACTED] estimated that a 100 per cent reduction in PPI income would necessitate an increase in its typical APR from of between six and nine percentage points above current levels. This estimate was smaller than its projected increase for unsecured personal loans. [REDACTED] estimated that a 100 per cent reduction in PPI income would necessitate a proportionate increase in its APR of 8 per cent. This was lower than its estimate for personal loans (13 per cent). Finally, [REDACTED] estimated that, for [REDACTED], a 100 per cent reduction in PPI income could necessitate an increase in second-charge mortgage APRs of up to 49 per cent over current levels.
- Most distributors did not contend that a reduction in PPI income would have a significant effect on the pricing of their first-charge mortgage products. For example, [REDACTED] estimated that non-PPI income would need to increase by 4.7 per cent to recover lost PPI income, equivalent to a 0.03 per cent increase in the APR.

¹⁶We were told that some customers, closest to the credit cut-off point, would face higher increases in APR than the reported figures for the portfolio as a whole.

¹⁷[REDACTED] told us that it did not consider this modelling exercise to be realistic or informative.

90. There are several limitations to this approach which mean that this evidence needs to be interpreted with care. These figures are based on the price-setting models in place at the time we asked firms to carry out this exercise, and we noted that firms may alter their price-setting models or their overall strategy in the event of a major market wide change.
91. It may also be the case that there is a less than 100 per cent pass-through of PPI profits to customers in the form of lower credit prices, in which case the effect of any intervention in the markets for PPI on credit prices would be mitigated to an extent by reduced distributor profits.

System profitability

92. We created models of market profitability, one for personal loans and one for credit cards. The models provide a high-level assessment of the profitability of the personal loan and credit card markets over the last five years (2003 to 2007) using publicly available information.
93. We looked at the personal loans and credit card markets only and did not look at the mortgages market; we noted that MPPI made up less than 10 per cent of the total 'price' of the bundle of MPPI and credit and that MPPI is sold on only approximately 15 per cent of mortgages sold by the large distributors. PPI income is therefore a very small part of the total revenue earned on mortgages. We estimated that MPPI profits make up less than 1 per cent of the total revenue earned on mortgages excluding MPPI, and therefore that the scale of any effect on credit prices from a reduction in PPI income is likely to be very small.
94. We used the models to identify trends in profitability in the two credit markets and the relative importance of PPI revenues to that profitability. We looked at contribution as

a measure of profitability, which is a function of interest income, funding costs, PPI income, other income, direct costs and impairment charges, but does not include indirect costs or a cost of capital.

95. In both market models the output was consistent with our previous findings:
- In the personal loans market, we saw declining profitability in recent years to the extent that there was a negative contribution in 2007. We noted that the decline in profits was due to a squeeze in net interest margins and an increase in impairment costs. We also saw that PPI income appeared to be a relatively small factor contributing to the decline in profitability.
 - In the credit card market, we saw that the sector was profitable over the last five years even before taking into account income from PPI.
96. We cannot infer anything about the extent of the waterbed effect from this analysis. Although the negative contribution from credit appears to be driven primarily by impairments, we do not know the extent to which PPI profits were passed through to customers as a result of competition. We summarize our findings below.

Personal loans

97. Contribution declined from £4.1 billion to £1.3 billion between 2003 and 2007. This decline in profitability coincided with a period of growth in terms of total debt outstanding. Without PLPPI income, contribution was only marginally positive in 2005 and 2006 and negative in 2007.
98. The key drivers behind the observed decline in profitability are as follows:
- Net interest income margin declined markedly over the period (from 59 to 36 per cent). Base rates increased over the period from 3.7 per cent in 2003 to 5.5 per cent in 2007 (peaking in August 2007 at 5.75 per cent). This was not reflected in

an increase in APRs: the effective interest rates received on balances outstanding fell slightly over the period, as did average APRs (which did, however, increase during 2007 from 2006).¹⁸

- Impairment costs. Impairment charges increased from £1.9 billion in 2003 to £3.5 billion in 2007, an increase of 81 per cent. Thus impairments can be seen to be the single most important reason for the decline in profitability observed over the period. Up to 2005 there were historically low levels of bad debt indicators such as unemployment, records of mortgage arrears and repossessions, and county court judgments (CCJs). However, the level of consumer indebtedness increased and consumers started to take out individual voluntary arrangements (IVAs) and declared bankruptcy in significant numbers as they became unable to service their higher debt commitments: the number of IVAs taken out rose from 10,752 in 2004 to 44,332 in 2006—an increase of over 300 per cent—and to 64,480 in 2007.

99. In comparison, PLPPI income appears to be a relatively minor contributor to the decline in profitability over the period. PLPPI income declined from £1.8 billion in 2003 to £1.4 billion in 2007. On average, PLPPI income made up roughly one-quarter of total net income over the period.

Credit cards

100. The credit card market has been profitable in all years and has not experienced the same sharp decline as the unsecured personal loans market. Contribution rose from £2.9 billion in 2003 to £3.6 billion in 2005, but decreased to £2.7 billion in 2007.

¹⁸By reference to the Bank of England data, the average effective interest rate received on outstanding credit balances decreased between 2003 and 2007 from 9 to 8.7 per cent, reaching a low of 8.5 per cent in 2006.

101. Whilst outstanding balances have increased across the period—£46 billion in 2003 to £54 billion in 2007—as per the personal loans market, the credit card sector has suffered from increased funding and impairment costs.
102. Impairment costs for credit cards more than doubled over the period from £1.5 billion to £3.1 billion and can be seen to be the single most important factor impacting on profitability.
103. Funding costs increased markedly during the period, by 76 per cent, although outstanding balances only increased by 18 per cent. This was the main driver in the decline in the net interest margin (from 67 to 54 per cent).
104. Although CCPPI income has fallen, this is a relatively immaterial income stream in the credit card market. There was little movement in CCPPI income between 2003 and 2007 and PPI income is a less important stream of income in the credit card market compared with the personal loans market. On average, CCPPI income made up only 11 per cent of total net income. Credit cards have greater reliance on income from other fees and charges as an income stream, which increased in the period primarily due to a material increase in balance transfer fees.

Econometric evidence

105. We undertook an assessment of the distributors' sales data in order to assess whether there was any evidence that credit prices were affected by changes in PPI income. It is difficult to draw firm conclusions from this evidence as there may be other factors, which we cannot control for, affecting the observed correlations (or lack thereof) between credit prices and factors affecting PPI income.
106. We looked at the correlation between personal loan APRs and PPI prices.

107. We found that there was a negative correlation over time between PPI prices and credit prices for personal loans. This means that for an individual product we observe that as PPI prices rise (fall) the credit price is lower (higher). This would be consistent with a waterbed effect.
108. However, this was a weak result, as there may be other circumstances and trends that could lead to lower credit prices and higher PPI prices over time. We also have a large range in size of products and these results could therefore be driven by very small products. To overcome these potential problems, we included monthly dummy variables to represent wider trends and weighted observations by their volume of sales. Doing this we found no significant correlation.
109. A fuller discussion of our econometric analysis is provided at Appendix 4.

Conclusions on lower credit prices

110. The evidence we saw led us to conclude that credit prices, and credit cut-off scores, are lower than they otherwise would be because of PPI income generated at the credit point of sale. For mortgages, the effect is very small. We concluded that credit card prices were not significantly affected by PPI income.
111. We concluded that these lower prices were a direct result of the distributors' anticipation of high profit margins on PPI. Lower credit prices are therefore a direct result of the features of the sale of PPI that lead to an AEC in the markets for PPI.
112. We conclude, therefore, that there is a relevant customer benefit of 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. We note that the incentive to discount credit prices is due, in part, to the intensity of competition in the credit market. There is some uncertainty over the intensity of competition for credit customers going forward, for example given recent events in the credit markets involving the proposed consolidations of some credit providers and, at least in one case, the running down of some business lines. In this respect Cardiff Pinnacle told us that in the current economic situation banks had made significant changes to their credit policies, that this had already had an effect on credit prices, and hence the waterbed effect might not be as marked as our research suggested. We note that, although levels of indebtedness in the credit markets have increased, new gross lending advances have contracted, with credit providers now more focused on their existing customer base and the quality of their lending book; rising bad debt levels have forced some providers to review their customer acquisition strategies by focusing on quality lending, increasing APRs, and lending only to customers with whom they have a shared knowledge of credit history. The 'credit crunch' has accentuated this trend. As a result, we could not be confident that the scale of the relevant customer benefit that we observed in the period up to December 2006 would persist at that level in the future.

Intervention in the PPI markets

113. We considered whether we should exercise our discretion with regard to relevant customer benefits.
114. We noted that all our remedies are aimed at increasing competition, and that we expect that a successful intervention would bring PPI prices down. If profits from PPI prices are passed through to consumers as lower credit prices, the imposition of any remedy would impact on credit prices. If we imposed remedies, PPI consumers may be expected to benefit but credit and PPI consumers would face higher prices for

their credit products; if we did not intervene, PPI consumers would continue to face high PPI prices.

115. We noted that a distortion in credit prices is not intrinsically beneficial. That credit prices are lower as a result of a distortion in the PPI market may be considered to be a benefit to some customers; however, we noted that where credit prices are below their marginal cost, this will result in inefficiency.¹⁹ Moreover, we noted 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.
116. However, PPI is a secondary product, and there is therefore a potential for waterbed effects on the primary market for credit which could affect the welfare of credit consumers. Our analysis of the effects on consumers of the features we have found in the markets for PPI and of any remedies to address them is therefore necessarily more complex. This is different from a standard monopoly context where the effects on consumers of market features, and remedies to address them, is more straightforward. In particular, economic theory does not give unambiguous results as to whether the effect of remedies to address market features giving rise to a secondary market monopoly on consumers as a whole is positive or negative.
117. We therefore considered whether our remedies might be expected to have a positive or negative impact on total consumer welfare. To do this, we considered two different examples: a remedy which increased information such that all consumers were able to search effectively for both credit and PPI before arriving at the point of sale of

¹⁹This is because distorted credit prices induce overconsumption of credit.

credit, and a remedy where PPI prices were reduced but there was no increase at all in the amount of searching for PPI before the credit point of sale. These two examples represent the two ends of a spectrum in terms of the potential impact of remedies on customer search. Our analysis of this is set out in Appendices 5, 6 and 7.

118. We tested the sensitivity of our results to different assumptions regarding three key parameters of the models. We found that for MPPI and SMPPI, under any reasonable set of assumptions for the value of these parameters, any effective intervention in the PPI market that brought PPI prices down towards competitive levels always had a positive net consumer welfare effect (taking both PPI and credit market effects into account). We would expect similar effects for CCPPI and credit cards, because PPI income on credit cards forms a small percentage of overall income for credit card providers.
119. For PLPPI, we found that a remedy which increased search resulted in a positive net consumer welfare under any reasonable set of assumptions. For a remedy which reduced prices towards competitive levels but did not increase the extent of customer search at all, we found that, under certain sets of assumptions, such a remedy could have a negative overall impact on net consumer welfare. However, under other, more realistic, assumptions it would be likely to have a positive effect.
120. We noted that none of our remedies were aimed at reducing PPI prices without improving the ability to search for PPI price at the same time as credit price—we were confident that the point-of-sale ban would give providers an incentive to increase advertising of their stand-alone products (and in some cases to introduce stand-alone products to the market). The remedies package as a whole also includes additional items aimed at increasing PPI advertising and improving the ability of

consumers to shop around for PPI. We were confident, therefore, that we would not be in a situation of imposing an effective remedy which had no impact on search.

121. The results of our analysis led us to conclude first that, for MPPI and SMPPI, we should not modify our remedies to maintain the relevant customer benefit of lower credit prices or cut-off scores, as any effective intervention would have an overall positive effect (and, as noted in paragraph 110, for MPPI at least the scale of the relevant customer benefit is very small). We inferred from our results that we should reach the same conclusion for CCPPI. For PLPPI, we noted that under some circumstances (where a number of fairly extreme assumptions combine)²⁰ intervention might not be welfare enhancing. However, we consider the circumstances giving rise to a negative net consumer detriment to be very unlikely to occur, and we were confident that our remedies would increase both search and the extent to which distributors and intermediaries actively seek to win customers using price as a competitive variable. We therefore concluded that we should not modify our remedies to preserve the relevant customer benefit of lower credit prices or cut-off scores when choosing our remedies for PLPPI.

General issues

122. A number of general issues have been put to us in the course of the remedies process. These related to:
- (a) the likely impact of Insurance Conduct of Business sourcebook (ICOBS)²¹ regulation on competition;
 - (b) the impact of the economic downturn;
 - (c) the impact of any remedies on the 'protection gap' and default rates on credit;

²⁰There are PPI price reductions but no increased search by consumers prior to the credit point of sale; all profits from PPI are passed through to credit customers; the price of PPI relative to the price of the protected credit is estimated conservatively; and the market elasticity of credit demand is estimated generously.

²¹See the provisional findings [Appendix 2.5](#), paragraphs 28 to 31.

- (d) the impact of any remedies on adverse selection and the viability of supplying PPI;
- (e) comparison with remedies put in place following other market investigations; and
- (f) recent competitive developments in PPI markets.

Impact of ICOBS regulation

123. Many parties told us that the revised ICOBS regulation would make a significant impact on the sales process of PPI and as a result would change the market. It was suggested to us by some parties that we should allow the changes introduced by ICOBS to ‘bed down’ before we considered whether remedies were required. Others suggested that the changes to how insurance is sold introduced by ICOBS were in themselves sufficient to remedy some or all of the adverse effects we found. We noted that we have to publish our final report on this investigation by February 2009, and are therefore unable to wait and see what changes in the market result from ICOBS. However, the FSA told us that it was fairly convinced that the kind of information and disclosure remedies that it typically deployed were unlikely significantly to affect structural problems seen in this market.
124. We do not believe that the measures introduced by the FSA, such as increased cooling-off periods and a greater provision of non-price information—which are intended to increase customer protection rather than to address competition problems in the market—would be nearly sufficient by themselves to remedy the AEC that we have identified in PPI markets. For our analysis regarding cooling-off periods and the provision of non-price information, see paragraphs 149, 248 and 249.

The impact of the economic downturn

125. Several parties told us that the prevailing economic conditions had led to a significant increase in claims on PPI policies, particularly for unemployment. The ABI provided evidence that the number of new claims because of unemployment was 69 per cent higher in September 2008 compared with September 2007. [REDACTED], [REDACTED] and [REDACTED] also told us that unemployment claims had increased. A large distributor ([REDACTED]) provided us with evidence that the number of involuntary unemployment claims was significantly higher in September 2008 than in September 2007, and that involuntary unemployment claims represented a significantly greater proportion of all claims. [REDACTED] evidence also showed that, whilst involuntary unemployment claims had increased, the overall number of claims in September 2008 had decreased by 11 per cent on the levels of September 2007. Aviva told us that its analysis of the impact of the recession of the early 1990s showed that the average annual cost to a scheme for unemployment per person covered increased by [300–500] per cent over three years (from 1989 to 1992). For sickness and disability, the corresponding increase was [0–200] per cent. This was as a result of increases in both the frequency and the duration of claims. Further, as set out in paragraph 65, we were told that some changes to policies had occurred recently. More generally, we were told that some distributors had stopped selling PPI policies (though we were *not* told that these decisions were related to the current economic downturn). Sterling Insurance told us that some providers had stopped selling new PPI policies since September 2006, citing, among others, Virgin and M&S Money.
126. It was put to us, in this context, that we could place little weight either on the results of our analysis of claims profiles for single-premium policies in Appendix 2 or our analysis of waterbed effects in Appendices 3 to 7, primarily because the likely effect of the economic downturn would be to raise claims costs, in particular those associated with unemployment.

127. The current downturn has not yet run its course, and neither we nor the parties are able to predict reliably what will happen. The previous economic downturn started nearly 20 years ago. Even if the PPI and credit data needed to conduct the analysis of waterbed effects were available for that period, because it was so long ago, we do not think we could place much weight on the results as an indicator of what is likely to happen in the current downturn.
128. We were not persuaded that the current economic downturn would clearly result in a sufficiently different outcome from our analyses in Appendices 2 to 7 to warrant a change in our approach to remedies. In Appendix 2, we found that claims costs were relatively small relative to the price that consumers pay for PPI. Whilst claims costs may increase in an economic downturn, many other factors affecting the size of claims costs relative to the price that consumers pay may also change—for example, the prices that consumers pay for PPI, or the level of demand for PPI.
129. Our analysis of potential waterbed effects in Appendices 3 to 7 was based in part on assumptions regarding the profitability of PPI, the intensity of competition for credit customers and the responsiveness of credit demand (at a market level) to changes in average credit prices.
130. As noted in paragraph 127, whilst claims costs may be affected by an economic downturn, many other factors affecting PPI prices and the profitability of PPI distribution may also change. Therefore it was not clear to us that PPI profitability would reduce significantly in an economic downturn. We noted in paragraph 112 that there was some uncertainty regarding the intensity of competition for credit customers going forward, and that consequently we were not confident that the scale of the relevant customer benefit we observed in the period up to December 2006 would persist at this level in the future. One third party ([REDACTED]) told us that the sensitivity of

credit customers to changes in average credit prices could increase substantially as the economy entered recession and consumers tightened their expenditures and their budgets. However, given that there are likely to be many factors affecting credit demand in an economic downturn, we felt that we could make no clear prediction regarding its effect on the responsiveness of credit demand to changes in average credit prices.

131. Finally, we were told that we should take a cautious approach to remedies in light of the economic outlook. As set out in paragraph 129, we see no clear reasons why an economic downturn would necessarily diminish the adverse effects on consumers of the monopoly that distributors enjoy over sales of PPI to their own credit customers. As set out in paragraph 112, there is some uncertainty over whether the relevant customer benefits in the form of low credit prices would persist at the levels observed up to December 2006, which would increase the case for intervention. If anything, in an economic downturn the case for intervention to address a competition problem in PPI could be seen to be more pressing, since the current high prices discourage PPI uptake and could result in customers being uncovered at a time of increased risk. We concluded that we should not change our approach to remedies, in the light of the current economic outlook.

Impact on the 'protection gap'

132. We were told that any measure that reduced the uptake of PPI would increase the protection gap,²² which, given the economic downturn, they told us would be particularly unfortunate. In addition, we were told that a reduction in the proportion of loans for which customers had taken out PPI could increase default rates to a significant degree.

²²The ABI defined 'protection gap' in its report as existing when households do not have sufficient insurance or other coping strategies in place to match the loss of income resulting from unemployment, illness or loss of life. We concentrate on 'debt' and 'essential' expenditure, since 'lifestyle' expenditure can be reduced. Source: *Coping with crises: household protection needs*, ABI Insurance Market Study No 5, 2008.

133. Our analysis of PPI price elasticities indicated that the current high price of PPI deters some borrowers, who would take it out if it were competitively priced, from taking out PPI policies. Measures which increase competition are likely to bring down the price of PPI policies, which, in turn, is likely to make PPI more attractive to consumers, increasing the likelihood of consumers taking out PPI policies. We also noted that, in times of economic downturn, consumers are more likely to think about the possible consequences of taking on debt. We concluded that our remedy package, which is designed to increase competition between PPI providers and reduce the cost of PPI policies to consumers, would not be detrimental to consumers during an economic downturn.

Increased risk of adverse selection

134. We were also told²³ that some of the proposed remedies (in particular, the proposed ban on selling PPI at the credit point of sale) could result in the PPI market disappearing altogether. For example, Aviva said that any initial fall in sales completed at the point of sale of credit could lead to increased adverse selection, which in turn would lead to reduced customer choice, higher prices and a further fall in sales. This in turn would lead to PPI providers and underwriters exiting the market, and that in turn would lead to further reduced customer choice, higher prices and a further fall in sales. We were told that it was important for insurers to get a suitable balance of high- and low-risk customers in sufficient volumes in order to sustain a commercially viable PPI product that is available to a broad range of consumers with minimal exclusions.²⁴

135. However, there are likely to be a number of conflicting factors affecting the balance of low-risk and high-risk customers. In particular, we would expect our remedies to have

²³HSBC response to Remedies Notice, p12.

²⁴Aviva response to provisional findings, paragraph 2.3.

a significant impact on PPI prices. It is a generally accepted economic principle that adverse selection problems are exacerbated by high prices. This is because high prices discourage low-risk customers more than they discourage high-risk customers. Given the scale of distributor margins, we would expect our remedies to deliver a large reduction in PPI prices and therefore a significant improvement in the average risk profile of PPI customers.

136. In addition, we consider that the package will decrease adverse selection risks in the stand-alone market. A point-of-sale ban would lead, in our view, to more consumers searching for PPI, increasing the number of consumers considering stand-alone PPI policies. The increase in consumers looking at stand-alone policies when taking out credit would, in our view, reduce overall adverse selection risks for stand-alone providers.
137. We note that there may be some increases in credit prices for PL and SM due to so-called waterbed effects. However, we would expect that price effects in the credit markets will be smaller in magnitude than the effects on PPI prices. Credit suppliers can also protect themselves from credit risk to an extent using their credit-scoring systems. In our view, any increase in adverse selection in the markets for credit is likely to be modest.
138. As regards distributors, it is possible that adverse selection for some might increase, if their penetration rates were to fall. We consider this unlikely in the context of falling prices for PPI. However, we note that current claims ratios would have to rise, in some cases by more than six times, to reflect other insurance markets. Moreover we were told that adverse selection and moral hazard risks in the PPI market were different from those in the motor or household insurance market, as the risks were less affected by customer behaviour and a customer's risk in terms of their

unemployment and health tended to be of public record, allowing firms to underwrite that customer based on known medical conditions or exclusions. We consider that these differences make the potential for adverse selection to be a problem for distributors lower, and easier for them to mitigate by using pre-existing condition clauses in the contracts, if this were necessary. But it was not clear that the risk profile of customers choosing to buy from the credit provider would change dramatically to the disadvantage of that provider if there were a point-of-sale ban. We were content that if adverse selection did increase for some distributors, it would not do so to a level which would lead to a significant reduction in the number of providers of PPI.

139. We therefore disagree with the parties that our package of remedies will lead to a reduction in the number of different PPI policies being offered. We expect that stand-alone sales should increase significantly and the number of providers of stand-alone PPI should increase. Sales by individual distributors may decline, but we did not think that the balance of high- and low-risk customers buying their products would change dramatically, nor that there would be a significant reduction in the number of providers of PPI.

Comparison with extended warranties and store cards

140. Some parties referred us to the CC's remedies²⁵ in Store Cards²⁶ and Extended Warranties²⁷ and said that the CC had not proposed such extensive remedies in these cases. However, we are not bound by the remedies that have been introduced in inquiries into other markets; each reference market needs to be assessed individually on its merits and appropriate remedies put in place where adverse effects are identified.

²⁵ Genworth referred to Extended Warranties at pp7–8 of its response to the Remedies Notice.

²⁶ *Store Cards*, TSO, March 2006.

²⁷ *Extended warranties on domestic electrical goods*, TSO, December 2003.

Recent competitive developments

141. Some parties told us that competitive developments had taken place in the PPI market that were not fully reflected in our provisional findings, or had taken place after publication of our provisional findings. The FLA,²⁸ citing a survey of its members it was conducting, told us that 80 per cent of those surveyed had improved terms and conditions in some way in the last year, and that 36 per cent of its members which had responded to its survey had reduced PPI prices, for reasons including to increase take-up rates and market share, and (in one case) as part of its 'treating customers fairly' review. We have also been made aware of price rises which have occurred during the course of our inquiry. For example, between June 2006 and June 2007 moneyfacts.co.uk reported that some providers, including Alliance & Leicester, Direct Line, Lloyds TSB and, Liverpool Victoria, had increased PPI prices (it also noted that some had reduced prices).²⁹ We noted this evidence, but we concluded that these price changes and other developments that have been brought to our attention did not represent a decisive shift in nature of competition in PPI markets.

An assessment of the options in the Notice

142. This section of the paper discusses the different remedy options set out in the Notice published on 5 June 2008 and those that have subsequently been put to us. For each option, we set out: the initial proposal consulted upon in the Notice; a summary of the responses to the Notice; and our provisional decision on how the remedy should be implemented.
143. We start by considering the options we are taking forward as our remedy package, options 1, 3, 4, 6 and 7(a) (pre-sale marketing, additional information for comparison, a point-of-sale ban, annual statements and a ban on single-premium policies). After

²⁸FLA response to Remedies Notice, p5.

²⁹Moneyfacts.co.uk press release, 18 June 2007.

that, we consider the remedies that we do not propose to take forward. In some cases we have revised the options we are taking forward to take into account aspects of the options we are not considering taking forward. For example, as the point-of-sale ban (option 4) requires certain information to be given to the customer, it incorporates many of the characteristics of option 2 (information at the point of sale), and as the annual statement requires some information on customer claims, it incorporates parts of option 9 (the obligation to share information about customer claims).

144. We considered the remedies separately for each type of PPI policy for which an AEC was found in our provisional findings. On this occasion we concluded that the remedies packages for each type of PPI policy should be the same though the individual options do reflect different characteristics of the different types of PPI and the underlying credit.

The options we are proposing to take forward

Option 1: Standard disclosure of cost to the customer of PPI and credit and requirement to provide a statement of 'key messages' in marketing materials

A summary of the proposal from the Notice

145. In the Notice, we proposed a requirement that distributors which offer PPI and credit products (we also asked if stand-alone providers should be covered by this option to the extent that they could be) provide the following in marketing materials:
- (a) the annual cost to the customer of the interest and charges payable on the credit product;
 - (b) the annual cost to the customer of taking the PPI product;
 - (c) the annual cost to the customer of the combination of the credit product with the PPI product; and
 - (d) a short statement of key messages (the 'key messages') alerting customers:
 - (i) to the existence of alternative PPI products (including stand-alone PPI);

- (ii) to the existence of the FSA comparative tables and possibly other sources of information about the cost of PPI and of insured credit (eg other price comparison sites); and
- (iii) that purchasing PPI is optional and does not increase the likelihood of obtaining credit.

146. We have provisionally found that a customer's ability to compare products is reduced by an absence of information provided in a way that would help them compare PPI policies. We also found that few distributors actively seek to win credit and/or PPI business, by using the price (or non-price characteristics) of their PPI policies. In particular, we found that the time taken to obtain accurate price information is a barrier in relation to the provision of PLPPI, MPPI and SMPPI. This option would make it easier for customers 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 customers, it would also help address the distributors' failure to compete actively on the price of their PPI products.

Responses to the Notice and our views on the issues raised

147. In general terms, all parties were in favour of increased transparency and making it easier for customers to compare PPI policies.
148. However, there was a wider range of views about the benefits of this remedy option as a means of increasing transparency. Some parties were concerned that any changes in regulations might make advertisements more difficult to understand and

hence less effective at attracting customers.³⁰ In addition, some parties³¹ told us that ICOBS already addressed many or all of the informational issues that we noted in our provisional findings and that there would be no benefit from additional information. Others told us that this remedy option could distort competition by focusing consumers' attention on the price of PPI (rather than looking at both price and quality), giving distributors an incentive to reduce both the level of cover and innovation.

149. We consider that the information currently provided regarding the price of PPI does not encourage customers to shop around and is not sufficient to enable customers easily to compare products.³² In our view, the form and content of the price information required under ICOBS is useful for the customer when considering whether a particular product is affordable and suits their needs, but we do not consider that it provides a sufficient basis to enable customers to compare products across different providers. We note that ICOBS already requires a substantial amount of disclosure of the features of a PPI product, such as a policy's significant benefits, significant exclusions and limitations, duration, as well as price information, and we do not believe that further disclosure of non-price features of the product is necessary. We do consider, however, that more needs to be done on price disclosure to enable customers to use this to shop around and compare products.
150. We received views on the following issues relating to the detail of this remedy option:
- (a) where PPI messages should be published;
 - (b) issues regarding the current and future credit regulations;
 - (c) what price metric should be used; and

³⁰AFB response to Remedies Notice p3, AIFA/AMI response to Remedies Notice p2, Aviva response to Remedies Notice p4, Barclays response to Remedies Notice p5, Cattles response to Remedies Notice p7.

³¹Abbey response to Remedies Notice p6, Banque PSA response to Remedies Notice p3, Genworth response to Remedies Notice p4.

³²Under ICOBS, PPI providers have to provide a document that outlines prices in a durable medium—before the conclusion of a contract in a non-distance sale or immediately after the conclusion in a distance sale: <http://fsahandbook.info/FSA/handbook/ICOBS/6/4.pdf>. Under ICOBS rules, firms are required to give price information to customers in a way calculated to enable the customer to relate it to a regular budget and total premium payable.

(d) issues regarding the combination of options 1 and 4.

- *Where PPI messages should be published*

151. There was a broad consensus that pricing and other information should be included in marketing materials specifically related to PPI products. Views were mixed on whether credit providers should be required to provide information about PPI in their credit advertisements.
152. The FSA and Which? told us that just putting messages into PPI marketing materials would not be effective. Abbey told us that putting additional information into PPI marketing materials may confuse customers. These three parties noted that distributors did not generally market PPI and hence the impact on competition of a remedy that affected only PPI marketing would be small. However, most parties, including stand-alone providers such as the Post Office, considered that mandatory provision of information about PPI could be helpful on direct PPI marketing materials and on the Internet.
153. Parties were split over the effectiveness of requiring key messages and information about the price of PPI on credit advertising. Those parties which were in favour of requiring more PPI information to be included in credit advertising told us that all advertising and marketing material that carried an illustration of the cost of credit should also show the same illustration in relation to the credit and PPI bundle, as this would encourage customers to shop around for cheaper PPI and/or the cheapest combination of credit with PPI.

154. Abbey and RBSG³³ were concerned that any combined disclosure could have unintended consequences in the credit market and on their ability to cross-sell non-PPI products at the credit point of sale. Capital One said that having a combined disclosure (such as a combined APR) could cause both customer detriment and a distortion to competition in the credit market because:
- (a) combining marketing materials in situations where PPI is not relevant risks consumer alienation or confusion;
 - (b) the additional complexity to prospective customers of a combined disclosure could potentially mislead the customer regarding the cost of the underlying credit; and
 - (c) a combined APR would not impact all PPI providers equally causing a competitive distortion.
155. The Post Office said that having PPI advertising on credit advertisements should not be implemented, favouring instead a de-linking of credit and PPI.³⁴ Barclays³⁵ said that, depending on how the cost of credit and PPI was presented, it may lead to a belief on the customer's part that the PPI was not optional.
156. Other parties questioned whether it would be appropriate to require the disclosure of the cost of PPI on credit advertisements in those situations where a credit provider offered a number of products that could be bought alongside the loan—such as household insurance (when selling a mortgage) or fraud insurance. We were told that it could be misleading to consumers for providers to be required to provide an illustration of combined cost of credit plus PPI, but not to provide a similar illustration of the cost of other products also offered alongside the credit product.

³³Abbey response to Remedies Notice p4, RBSG response to Remedies Notice pp3,5.

³⁴Post Office Financial Services response to the Notice, p2.

³⁵Barclays, response to Remedies Notice, p7.

157. The FSA said that, if we were satisfied that the benefits of option 1 were proportionate to the costs, then it would seem appropriate that a distributor which intended to sell PPI at the point of sale should be required to provide the information specified in this option when advertising their credit product and in other marketing material.
158. We recognize that requiring additional content in PPI marketing materials³⁶ might have a limited effect, by itself, given the current low degree of PPI-specific marketing. However, we consider that having additional information on the PPI price available in a comparable form would be effective as a supporting measure to other options (notably the provision of personal quotes in option 4 and annual statements in option 6) which would reduce the point-of-sale advantage and make it easier and cheaper for customers to switch suppliers. In a more competitive PPI market, we would expect more marketing of suppliers' PPI offerings than we currently observe. We note that many providers have Internet sites which currently highlight their PPI offerings and that customers using these sites would benefit from this option.
159. We propose that the key messages and disclosure of price be provided in all PPI marketing materials, including both direct marketing materials (such as statement inserts, emails and direct mail) and non-direct marketing material (such as newspaper advertisements, telephone directories and radio advertisements). We invite views as to whether there are any specific forms of PPI marketing material that should not be required to contain this information.
160. We noted the concerns that the parties have raised in relation to including PPI content in credit advertisements (in paragraphs 154 to 156). We consider that these concerns have most force where very few customers of a particular type of policy take out PPI. In these circumstances, there is a risk that requiring provision of

³⁶For the purposes of this document, marketing materials includes advertising and direct mail.

information about PPI in credit advertisements could confuse customers and/or decrease the effectiveness of the credit advertisements by providing additional and, for many consumers, irrelevant information. We also noted that requiring PPI content to be put into certain credit advertisements could be considered to be in conflict with the consumer credit directive (CCD)—see paragraphs 164 and 165.

161. However, for PPI policies and credit providers with high penetration rates of PPI, we found these concerns to carry much less weight. We provisionally found that the time taken to obtain accurate price information about PPI was a barrier to effective search. Requiring information to be provided about PPI in advertisements that were in close proximity³⁷ to credit advertisements would reduce the costs to customers of obtaining accurate price information for PPI by making this information more widely available to customers before the credit point of sale. In addition, by requiring separate advertisements, we will reduce the risk that customers become overwhelmed and confused by the amount of information in the credit advertisement or that they could conclude that PPI is compulsory.
162. In light of the above considerations, we looked at penetration rates to inform our view of which credit products and credit providers should be required to include messages about PPI in close proximity to their credit advertisements. Penetration rates for all main forms of PPI had fallen since 2002. In 2006, PLPPI and SMPPI had the highest penetration rates, of 43 and 65 per cent respectively. The penetration rate for CCPPI was 20 per cent and that for MPPI was 12 per cent. This suggested that there was a strong case for requiring PPI advertisements in close proximity to personal loan and second-charge mortgage advertisements. Based on current penetration rates, such

³⁷For the purposes of this document, we consider close proximity to mean sufficiently close that an ordinary credit customer would be likely to see or hear it. For example, for a radio advertisement it could mean within the same time slot or directly after the credit advertisement; for a press advertisement it could mean on the same page or on the facing page, for a direct mail campaign it could mean a leaflet in the same envelope and for a website it could mean a link from the credit advertisement.

additional information would be of interest and relevance to a substantial proportion of credit customers—a majority of customers in the case of SMPPI.

163. We concluded therefore that the requirement to provide PPI advertisements in close proximity to credit advertisements should apply to all suppliers of PLPPI and SMPPI, for all forms of advertisements. We invite views on any implementation issues that might arise for different advertising media.

- *Issues regarding the current and future credit regulations*

164. Some parties³⁸ highlighted potential issues with credit regulations. A number of parties referred to the new ICOBS rules relating to PPI which came into force in January 2008,³⁹ and others⁴⁰ highlighted concerns about the interaction of option 1 and the CCD.⁴¹ Cattles also said that there were some general issues in defining advertising and marketing materials.
165. The CCD will regulate the form and content of credit advertising from 2010. Implementation is under way and we continue to work with other government departments regarding how our remedies can fit with current and future regulation. Our current view is that the CCD sets out the boundaries of national regulation of the content of advertisements for unsecured personal credit including unsecured personal loans and credit cards but does not address the content of PPI advertisements. We consider that our remedy—to require advertisement of PPI in close proximity to every credit advertisement—would be compatible with the CCD.

³⁸ABI response to Remedies Notice p3, AFB response to Remedies Notice p2, Sterling Insurance response to Remedies Notice p3.

³⁹ICOBS 6 sets out product information requirements and 6.4 deals with the pre- and post-contractual requirements for protection policies.

⁴⁰ABI response to Remedies Notice p3, Banque PSA response to Remedies Notice p3.

⁴¹2008/48/EC.

166. We consider that all our remedies are compatible with ICOBS and we will continue to work with the FSA to ensure that the detail of the advertising requirements that we put in place are compatible with the financial promotion rules in ICOBS.

- *What price metric should be used*

167. A number of parties had views on the best way to advertise price to customers. However, there was no overall consensus, apart from the need to be clear and succinct.

168. As a general principle, HBOS said that developing a 'common currency' in which to express the price of PPI would have huge value prior to point of sale. It considered that this common currency would help to drive customer searching. Lloyds TSB said that it would be necessary to take into account the different characteristics of PLPPI, MPPI and CCPPI when looking at price. Citizens Advice suggested that, in addition to disclosing information about the price of PPI, distributors should also disclose their commission in cash terms. It said that this would concentrate the mind of a consumer to consider the cost, and that a cash amount could be more explicit than a percentage.

169. In addition to these general points, we received comments on a range of ways of presenting PPI prices and the price of combinations of credit and PPI, both in marketing materials and in material presented to customers at the point of sale. The price measures we considered included:

- (a) the annual or monthly cost of PPI presented as a cash amount in relation to a particular scenario or quote;
- (b) the cost of PPI per £100 of monthly benefit. This metric compares the monthly premium paid by customers with the monthly benefits received if the customer

makes a valid ASU claim. This metric is already commonly used for MPPI and short-term IP and in the FSA tables for credit cards;

(c) a 'combined APR' incorporating both the cost of the credit and that of the PPI calculated using the standard approach for measuring APRs; and

(d) a 'stand-alone APR' for PPI, calculated as the difference between the combined APR and the APR on the credit only.

170. Many parties⁴² considered that monthly costs were useful for customers, particularly when assessing their budgets and overall affordability; however, Which?, Cardif Pinnacle and Cattles said that annual costs should also be provided.

171. Citizens Advice and Which? did not consider that APRs were a useful indicator of price in this market, and Which? said that they might make it harder to compare products. Abbey told us that APRs would not give customers any indication of the quality of cover. Nationwide said that a combined APR could apply only to distributors, which would be unfair to the stand-alone market and could be a barrier to entry for stand-alone providers. The FSA told us that it was generally understood that, though people did not know what the APR meant, it was useful for customers in comparing products, because people did understand the basic information that a higher number was more expensive than a lower number. However, it was important that the level of cover was also taken into account, something which the APR did not do.

172. Some parties⁴³ suggested that monthly cost per £100 of monthly benefit was a good measure of the price for PPI, which could be used by stand-alone providers and credit providers alike and could increase pressure on pricing. It would be argued that

⁴²AFB response to Remedies Notice p3, FLA response to Remedies Notice p12, Genworth response to Remedies Notice p5, HSBC response to Remedies Notice p10, Nationwide response to Remedies Notice p6, Sterling Insurance response to Remedies Notice p2.

⁴³Defaqto response to Remedies Notice p8, Post Office response to Remedies Notice p1.

use of this measure would remove the current confusion and increase price transparency across lending products that had led to the current wide variation in prices.⁴⁴ Others supported the use of cost per £100 monthly cover.^{45,46} RBSG proposed, as an alternative metric for single-premium policies, the monthly cost of PPI per £1,000 borrowed. However, RBSG said that a move to this measure would also require some simplification of the current PPI pricing structure, as it recognized that currently the measure varied significantly, for example according to the period of the loan.

173. We undertook some qualitative research with PPI customers⁴⁷ to assess their understanding of the various elements of credit and PPI pricing and to investigate which ways of presenting price information were most easily understood by consumers.
174. The research found that consumers were not comfortable working with percentages, and, whilst they could compare two different percentages (such as two APRs) and understand which one related to the cheaper product, they were unsure what an APR actually represented or what the actual cost to them would be. The research also found that consumers were uncomfortable with large numbers, generally preferring to think in terms of monthly costs; however, it was suggested that whilst large numbers such as lifetime costs made customers uncomfortable, the simple effect of making them uncomfortable might in fact encourage them to consider the cost more carefully and search around more.

⁴⁴See POFS response to the Remedies Notice, paragraph 14(b).

⁴⁵Cost per monthly cover is equivalent to monthly cost per monthly benefit for some products, such as MPPI, though not for variable premium products such as CCPPI.

⁴⁶Abbey response to Remedies Notice p4, Coventry Building Society response to Remedies Notice p3, HBOS response to Remedies Notice p3, Council of Mortgage Lenders response to Remedies Notice pp2–3, Nationwide response to Remedies Notice pp7,10.

⁴⁷Qualitative research comprising of 24 in-depth interviews. These interviews were undertaken with a range of recent PPI customer types (MPPI, CCPPI, PLPPI and SMPPI) and socio-economic groups.

175. Given the findings from our research and the responses to the Notice, we consider that price information needs to be made explicit in a standardized format in order for customers to be able more easily to compare the price PPI policies. We therefore consider that pre-sale marketing materials should include a disclosure of price using a standardized metric in an easily understandable format.
176. We agreed with HBOS and others (including the Post Office) that the beneficial effect of price disclosure on competition would be maximized if it enabled the development of a 'common currency' for use in comparisons.
177. An ideal pricing metric for use in marketing materials would be one that any consumer who saw the material could use to compare accurately the price of two competing products. We noted that the monthly cost/£100 monthly benefit was already in use for MPPI and short-term IP (and is used on the FSA tables for CCPPI) and that this metric had the desirable property for regular-premium policies that it was unaffected by factors that varied across customers, such as the size or term of the underlying loan, or the APR on the credit. Whilst the monthly cost/£100 monthly benefit may differ across consumers where risk-based pricing is used, we considered that this was a useful headline indicator that could be used to compare policies offered both by distributors and on a stand-alone basis.
178. We noted that some providers will offer more than one type of PPI policy to customers. In particular, some providers already offer customers a choice of different levels of cover (eg LASU, ASU, AS and U). In these circumstances, it may not be possible to use a single price to communicate the cost of PPI to every customer who

sees the advertisement. However, we note that ICOBS⁴⁸ includes rules regarding financial promotions⁴⁹ and we consider that these rules adequately address the issue of how variations in product offers could best be accommodated. We also note that providers will have incentives to advertise aspects of their PPI product characteristics that customers are likely to find attractive. Nonetheless we invite views as to whether interested parties consider that the ICOBS rules are adequate or whether we should require further disclosure of the core product characteristics for any product, whose price is disclosed (for example, the level of cover offered or the duration of ASU cover).

179. We took the view that the monthly cost/£100 monthly benefit should be used as a common metric for quoting PPI prices in marketing materials for all forms of PPI, that the disclosure of price according to this metric should be quoted in all PPI marketing materials (see paragraph 159) and should be featured prominently within them.⁵⁰
- This approach would maximize comparability of the prices of PPI products, including PPI offered on a stand-alone basis. We noted that one risk of using this metric was that providers could reduce the number of months for which their products offered cover, in order to appear to offer better value for money. We therefore propose to require PPI marketing materials to give a clear notice to customers if benefits on the product advertised pay out for less than 12 months.

⁴⁸ICOBS 2.2.4:

(1) This guidance applies in relation to a financial promotion that makes pricing claims, including financial promotions that indicate or imply that a firm can reduce the premium, provide the cheapest premium or reduce a customer's costs.

(2) Such a financial promotion should:

(a) be consistent with the result reasonably expected to be achieved by the majority of customers who respond, unless the proportion of those customers who are likely to achieve the pricing claims is stated prominently; (b) state prominently the basis for any claimed benefits and any significant limitations; and (c) comply with other relevant legislative requirements, including The Control of Misleading Advertisements Regulations 1988.

⁴⁹A financial promotion, with regard to PPI, is an invitation or inducement to engage in investment activity that is communicated in the course of business.

⁵⁰We have not specified a particular definition of prominence and note that this is likely to vary across media. We consider that the disclosure of monthly cost/monthly benefit should be sufficiently prominent that an ordinary PPI customer would notice it, when looking at/listening to the marketing material concerned and it should be of equal prominence to other descriptions of price and/or product features.

180. We also noted that, in the case of CCPPI, a different metric—the price per £100 outstanding balance—was already well established. We considered that this form of price disclosure was complementary to the disclosure of monthly cost/£100 of monthly benefit—in that it provided an indication of the way in which charges to a customer are calculated, whereas the monthly cost/£100 of monthly benefit provides an indication of value for money and provides a point of comparison with other providers, including stand-alone PPI. We therefore propose that, for CCPPI only, price should be disclosed on both bases. We note that providers may wish to include a wider range of pricing and other information in their marketing material to help promote their PPI product or bundle of credit with PPI. Such information may reflect the information in the annual statement (see option 6) and the personal quote (see option 4) as well as details of the non-price characteristics of their products. We do not propose any restrictions on other information provided in marketing material, beyond the existing ICOBS rules.

181. We do not consider that the provision of data on distributors' commission would be effective, as many providers are vertically integrated, making the disclosure of commission meaningless to customers.

- *Issues regarding the combination of options 1 and 4*

182. Several parties⁵¹ said that requiring PPI advertisements in credit advertising seemed inconsistent with a point-of-sale ban. Genworth said that it would be confusing to customers, who would be unable to buy the products they had received marketing and advertising information for at the credit point of sale. RBSG said that a combined (PPI + credit) APR would send mixed messages to customers, who might assume that the PPI had to be bought with the credit product.

⁵¹Abbey response to Remedies Notice p10, Genworth response to Remedies Notice p5, RBSG response to Remedies Notice p11.

183. We do not consider that the implementation of option 1 in the format set out below is incompatible with a point-of-sale ban. The point-of-sale ban is designed in such a way as to maximize consumer search, which should significantly increase sales of stand-alone PPI and encourage consumers to consider switching credit provider if they find a better combined offer of PPI and credit. However, it also allows consumers who want to buy PPI from their credit provider to buy that PPI, on a proactive basis, quickly, and allows distributors to contact consumers to offer them PPI only two weeks after the credit sale. Our remedy package aims to increase competition from stand-alone providers and competition on the combination of PPI and credit. We consider that the advertising of the price of PPI in close proximity to the credit advertisement, as well as letting customers know that it is available elsewhere and is not a condition of taking out credit, will result in better-informed customers with enhanced access to more easily comparable information.

Provisional decision on implementation of remedy

184. We concluded that there is information that should be provided to consumers in PPI marketing materials, which would better enable them to understand the price of PPI and search more effectively for the best-value stand-alone policy or combination of credit and PPI. We also concluded that pricing information should be provided in a standardized way. We concluded therefore that we should implement this option. Further, we decided that PPI price and other information should be provided in close proximity to credit advertisements for all PLPPI and SMPPI credit providers. These measures would allow customers to compare PPI price more easily.
185. The remedies proposal builds on option 1 in the Notice and requires that additional information regarding PPI is added to PPI marketing material and that all such material should be easy to understand (see paragraph 370 on monitoring of this).

FIGURE 4

Remedy proposal for information provision in marketing materials

All PPI providers must provide the following information in all PPI marketing material:

1. The monthly cost of PPI per £100 of monthly benefit.*†
2. That PPI is optional‡ and available from other firms (without specifying those other firms).
3. That information on PPI, alternative providers and other forms of protection products can be found on the FSA's moneymadeclear website.

All PLPPI and SMPPI distributors must advertise their PPI products in close proximity to their personal loan advertisements.

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

†CCPPI providers must also show the cost of PPI per £100 of outstanding balance.

‡If the PPI provider is a stand-alone provider, they do not have to include the information that the PPI is optional in their marketing material.

186. An obligation to advertise PPI prices would have the greatest impact and be most effective if:

- (a) PPI providers increase advertising and marketing for PPI and distributors do not decrease advertising for SMPPI and PLPPI;
- (b) pricing structures become more standardized and hence easier to compare across the market; and
- (c) customers use the opportunity to shop for alternative protection products.

187. We consider that the option above would work best in conjunction with other options aimed at increasing customers' understanding of prices and making it easier for customers to compare PPI products.

188. We consider that if we took this remedy forward, it could be implemented within six months of any CC Order and could be monitored by the OFT (supported by suitably comprehensive compliance reporting requirements on the parties). We also note that by requiring all PPI marketing materials to contain information on price, we are, in effect, making all PPI marketing materials financial promotions under ICOBS rules.

Option 3: Obligation to provide information about PPI and credit products to third party providers of comparative information for publication

A summary of the proposal from the Notice

189. In the Notice, we proposed a requirement that distributors provide information, in an appropriate format, about their PPI and credit products to third parties (including operators of comparative websites, market research companies and publishers of 'best buy' tables), for its use by those third parties in published comparative information.
190. We have provisionally found that a customer's ability to compare products is reduced by an absence of information provided in a way that would help them, and that few distributors actively seek to win credit and/or PPI business by using the price (or non-price characteristics) of their PPI policies as a competitive variable. This option would make information available which would better enable customers to compare the cost of PPI and credit with PPI.

Responses to the Notice and our views on the issues raised

191. Most parties⁵² were in favour of increasing transparency and making it easier for customers to compare PPI policies. Some parties⁵³ said that more comparable information would act as an encouragement for customers to shop around as it would give them the ability to compare PPI sold alongside credit with stand-alone PPI. However, others⁵⁴ believed that there was a risk that providing additional information would just increase complexity and could lead to a focus on price rather than on the appropriateness of the product.

⁵²Assurant response to Remedies Notice p2, Axa response to Remedies Notice p4, BBA response to Remedies Notice p3, Barclays response to Remedies Notice p13, Citizens' Advice response to Remedies Notice p8, Capital One response to Remedies Notice p4, Cassidy Davis response to Remedies Notice p1, Genworth response to Remedies Notice p2, HBOS response to Remedies Notice p5, IMLA response to Remedies Notice p3, Lloyds response to Remedies Notice p14, Nationwide response to Remedies Notice p9, RBSG response to Remedies Notice p8.

⁵³Axa response to Remedies Notice p4.

⁵⁴Abbey response to Remedies Notice pp8,9, Aviva response to Remedies Notice p12.

- *Comparative tables*

192. Many parties⁵⁵ noted that the FSA tables provided customers with comparable PPI information. In general, these tables were considered to be a positive step forward, a good concept and a useful resource for customers.⁵⁶ However, some parties⁵⁷ were concerned that the tables as presently published were difficult for customers to understand as the information was presented in a complex way. For example, Abbey said that its initial impression of the FSA comparison tables was that product information was not particularly clear and the interpretation of product quality was left to the consumer.
193. However, given that the FSA comparison tables are available to consumers, nearly all parties⁵⁸ considered that it would be more proportionate to make the provision of information to the FSA for use in these tables compulsory, even if they were not ideal, rather than to set up an additional independent website. In addition, a few parties (Aviva, Cattles and Lloyds TSB, for example) said that care should be taken in creating an obligation to supply sensitive data to third party commercial service providers as they may seek to leverage their role as the operative of comparative tables with commercial objectives.
194. Citizens Advice noted that, though it would support the proposal to get better PPI information on to comparative websites, PPI consumers were more likely to come from socio-economic groups D and E who may not have access to broadband

⁵⁵ Abbey response to Remedies Notice p9, ABI response to Remedies Notice p5, Axa response to Remedies Notice p4, Barclays response to Remedies Notice p13, BBA response to Remedies Notice p3, Cassidy Davis response to Remedies Notice p2, Council of Mortgage Lenders response to Remedies Notice p4, Coventry Building Society response to Remedies Notice pp6–7, FLA response to Remedies Notice p18, Genworth response to Remedies Notice p6, HBOS response to Remedies Notice p5, IMLA response to Remedies Notice p3, Nationwide response to Remedies Notice p9, Post Office response to Remedies Notice p4, RBSG response to Remedies Notice p8, Sterling Insurance response to Remedies Notice p6.

⁵⁶ BBA response to Remedies Notice p3, Barclays response to Remedies Notice p13, Coventry Building Society response to Remedies Notice p6, Nationwide response to Remedies Notice p9.

⁵⁷ Abbey response to Remedies Notice p9, BBA response to Remedies Notice p3.

⁵⁸ ABI response to Remedies Notice p6, Axa response to Remedies Notice p5, Cattles response to Remedies Notice p24, Coventry Building Society response to Remedies Notice p7, Nationwide response to Remedies Notice p10, Post Office response to Remedies Notice p4, RBSG response to Remedies Notice p8.

Internet at home. Though access is rising strongly, the effectiveness of this option may be limited by home broadband take-up levels among consumers in key socio-economic groups. However, we consider that any comparative pricing table would be most effective if it is in a central location such as the FSA website, that was easy to monitor, had comprehensive coverage and available when the customer wanted it.

195. Most parties⁵⁹ considered that stand-alone providers should be included in any obligation to provide information for use in comparative tables, as the tables should be used by customers to compare stand-alone products with products sold alongside credit.
196. We agree with the parties that, given that the FSA tables are available, it would be more effective and proportionate to add to them rather than create an additional table. We consider that, for these tables to be most effective, they need to provide a comprehensive view of the market, and as such need to include data about all PPI policies, including stand-alone policies and short-term IP policies (which, we concluded in paragraph 2.14 of our provisional findings, can be a form of PPI). We also note the parties' concerns regarding the complexity of the tables but consider that this issue might be the same for any new comparative website and that the FSA has considerable resources to enhance the website to make it more consumer friendly where this is necessary. We also note that the FSA will be doing some further evaluation of the PPI comparative tables, probably in a few months' time.
197. We also noted Citizens Advice's concerns about access to the Internet. However, our consumer research, which involved interviews of PLPPI, SMPPI, MPPI and CCPPI

⁵⁹Abbey response to Remedies Notice p9, Aviva response to Remedies Notice p13, Axa response to Remedies Notice p5, BBA response to Remedies Notice p4, Barclays response to Remedies Notice p13, Cassidy Davis response to Remedies Notice p2, Cattles response to Remedies Notice p15, Coventry Building Society response to Remedies Notice p6, FLA response to Remedies Notice p18, FSA response to Remedies Notice p13, Genworth response to Remedies Notice p6, Lloyds TSB response to Remedies Notice p14, Nationwide response to Remedies Notice p10.

customers, found that nearly 90 per cent of those customers had access to the Internet either at home or at work. Between 50 and 75 per cent of those asked for each product had income of less than £25,000 per year.⁶⁰ This evidence gave us confidence that, whilst Citizens Advice makes a valid point about home Internet access, enough low-income PPI consumers were able to access the Internet to make this remedy option worthwhile.

- *Claims ratios*

198. As part of the consultation on this remedy option, we asked whether claims ratios should also be provided. Most parties⁶¹ said that they should not be provided for a number of reasons, including: a perception that customers would not understand them (and indeed might be put off from taking out PPI by them);⁶² that they would change over time (and relate to the past rather than the present);⁶³ that they were not important at an individual level as they said nothing about the amount of money someone would receive upon making a successful claim and did not indicate whether an individual's claim would be accepted or not;⁶⁴ that they were commercially sensitive; and that new entrants into the market would not have claims ratios to provide.⁶⁵

199. Both Which? and Defaqto said that they would find claims ratios helpful when comparing products, as they were an important indicator of how much an insurer

⁶⁰BMRB Report—Telephone survey of PPI customers, February 2008, pp8&10.

⁶¹Abbey response to Remedies Notice p9, ABI response to Remedies Notice p5, Axa response to Remedies Notice p5, BBA response to Remedies Notice pp3–4, Banque PSA response to Remedies Notice p5, Barclays response to Remedies Notice p13, Coventry Building Society response to Remedies Notice p6, Defaqto response to Remedies Notice p10, FLA response to Remedies Notice p19, FSA response to Remedies Notice pp9–10, Genworth response to Remedies Notice p6, GMAC response to Remedies Notice pp1–2, HBOS response to Remedies Notice p5, HSBC response to Remedies Notice p11, Lloyds TSB response to Remedies Notice p14, Nationwide response to Remedies Notice p10, Openwork (noted this for MPPI only) response to Remedies Notice p1, Post Office response to Remedies Notice p4, RBSG, response to Remedies Notice p9, Sterling Insurance response to Remedies Notice p6.

⁶²ABI response to Remedies Notice p5, Banque PSA response to Remedies Notice p5, Barclays response to Remedies Notice p13, Coventry Building Society response to Remedies Notice p6, Post Office response to Remedies Notice p6.

⁶³Barclays response to Remedies Notice p13, Defaqto response to Remedies Notice p11, Genworth response to Remedies Notice p6, Lloyds TSB response to Remedies Notice pp14–15, Post Office response to Remedies Notice p6.

⁶⁴ABI response to Remedies Notice p5, FLA response to Remedies Notice p19, Genworth response to Remedies Notice p6, Nationwide response to Remedies Notice p10.

⁶⁵Post Office response to Remedies Notice p4.

would be able or willing to pay out in claims, and a good indication of value for money. Capital One said that it did not object to the publication of claims ratios as long as a consistent method was used to calculate them; however, it shared some of the concerns raised in paragraph 198.

200. Some parties⁶⁶ suggested that, as an alternative to the provision of data on claims ratios, we should require provision of information on the percentage of claims that are accepted. These parties said that it was more important to customers to know the probability of their claim being turned down than for them to know claim ratios.
201. We consider that claims ratios are an important measure of both absolute and comparative value for money. We noted that both Defaqto and Which? consider that claims ratios are an important indicator of value for money and that having this data would help them assess the relative merits of different PPI products. In addition, we noted the FSA's view that claims ratios could be a useful general guide for consumer groups, though it did not think that claims ratios would be useful for consumers.⁶⁷ However, we are also aware that consumers may find claims ratios confusing if published along with a number of other indicators. Hence, although we consider that claims ratios should be available to anyone or any organization who wants them, we do not consider that it is appropriate for them to be required to be published on a consumer website.
202. Though we have noted the parties' concerns regarding the logistics of calculating claims ratios, such as for new products and what should be included, these issues are not insurmountable. For example, we note that the parties have been able to provide claims ratios to us in the same format and that Datamonitor publishes claim

⁶⁶ Abbey response to Remedies Notice p9, Nationwide response to Remedies Notice p10, RBSG response to Remedies Notice p9.

⁶⁷ FSA response to the Remedies Notice, p11.

ratios of the top 10 UK insurers across five major lines of business: accident and health, liability, motor, pecuniary loss and property insurance, which is based on data from the FSA.⁶⁸ In relation to new products, we have been told that the underwriter must assess what the claims ratio will be ([X] told us that it could predict these to within a couple of percentage points of the actual in a benign economic period), and as a result a forward-looking claims ratio estimate could be available and meaningful in these circumstances. However, we concluded that it would not be necessary for new providers to provide information about expected claims ratios, as this would not add appreciably to the OFT's ability to monitor the market and could put new entrants at a competitive disadvantage to established players, who would not have to publish their forecasts. We propose that new providers should be required to publish actual claims ratios, as they start to build up a claims history.

203. We thought that information on the percentage of claims accepted might give consumers a feel for the quality of a distributor's sales process (a lower percentage might give some indication about the proportion of customers who have bought policies on which they cannot claim). However, we did not think that it would help consumers to search for the best-value policy for them in any material respect.

Provisional decision on implementation of remedy

204. We concluded that the mandatory provision of key information on PPI and short-term IP policies to the FSA, for use in comparative tables, would help consumers to search for the best-value policy. We concluded therefore that we should implement this option.
205. The remedy proposal builds on option 3 in the Notice. It makes the FSA tables as comprehensive as possible and provides a conduit for claims data, including claims

⁶⁸www.datamonitor.com/products/free/Report/DMFS2163/020dmfs2163.htm.

ratios, to be provided to third parties. In addition, we consider that the provision on GWP, penetration rates, price data and claims data to the OFT will assist them in monitoring the ongoing success of the remedies package. The remedies package would also include standard wording requiring parties to provide to the OFT any information and documents that it reasonably requires to enable it to monitor and review the operation of the remedies package. We propose to recommend to the FSA that it uses information provided to populate its comparative tables.

FIGURE 5

Remedy proposal for information provision to third parties

All PPI providers must provide comparative data to the FSA, as specified by, and in the format requested by, the FSA.

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 must provide the following information to the OFT on an annual basis— where indicated below, this information should also be available from the provider to any person on request:

1. Annual GWP, split by product type.
2. Distributor penetration rates, split by product type.
3. Aggregate claims ratios for each provider, split by product type, for one year, three years and five years (this should be available to any person on request).

206. This option works in combination with the annual statements and the personal PPI quote that is to be provided at the point of the credit sale. In these other remedies, we are proposing to require distributors to mention the FSA tables and as a result these remedies will be more effective if the tables are comprehensive. We therefore also recommend to the FSA that it uses the information provided to it under this requirement to populate its PPI price comparison tables.

207. We consider that the GWP and penetration rates, as well as the claims ratios, will be essential to the OFT when monitoring the effectiveness and impact of the remedies. We note that in a more competitive market for PPI we would expect to see claims ratios and penetration rates increase.

208. We consider that if we took this remedy forward it could be implemented within six months of any CC Order.

Option 4: Prohibition on selling PPI at the credit point of sale and within a fixed time period of the credit sale (the 'point-of-sale ban')

A summary of the proposal from the Notice

209. In the Notice, we proposed a requirement mandating that PPI could not be sold at the same time as the credit product, nor within a fixed time period of the credit sale (and/or in the case of CCPPI, when the credit product was activated). This option could directly address the point-of-sale advantage enjoyed by distributors, and would provide a greater incentive and opportunity for customers to search for PPI after the credit sale and for stand-alone providers to enter PPI markets.
210. We provisionally found that a credit provider enjoys significant advantages over other PPI providers, when selling credit and then PPI to their credit customers at the credit point of sale. We provisionally concluded that the sale of PPI at the credit point of sale is a feature of PPI markets, which prevents, restricts and distorts competition.

Responses to the Notice and our views on the issues raised

211. Consumer organizations⁶⁹ and stand-alone providers⁷⁰ were generally supportive of a point-of-sale ban. Provided the case for intervention was made out, the OFT was generally supportive of a point-of-sale ban and it considered that this more structural form of intervention appeared that which was most likely to address effectively the AEC. However, other parties, including all credit providers and many of their underwriters who responded to the Notice, were not in favour of a point-of-sale ban. These parties generally thought that such a ban was disproportionate to the AEC that

⁶⁹Citizens Advice preferred an option, which was not included in the Notice, of long-term price caps with minimum standard products. It considered that this would be a more optimal way of dealing with the mis-selling issue it had found and was concerned that the stand-alone market would not develop. Citizens' Advice response to Remedies Notice p2.

⁷⁰Post Office response to Remedies Notice p4.

we had provisionally found and that a ban would lead to a significant decline in the number of people buying PPI. They raised many issues around the proposed remedy.

212. The following issues were raised in consultation:

- (a) the potential benefits of a point-of-sale ban;
- (b) the risk that a point-of-sale ban would lead to a reduced take-up of PPI;
- (c) the risk that a ban would not address all aspects of the point-of-sale advantage;
- (d) the appropriate length of any ban;
- (e) whether a ban would lead to a reduction in consumer choice;
- (f) whether a ban would lead to a reduction in product quality;
- (g) whether a point-of-sale ban would lead to higher distribution costs;
- (h) whether a point-of-sale ban would have a differential effect on distributors;
- (i) whether a point-of-sale ban represented a restriction on the freedom of establishment;
- (j) the information that should be provided to customers at the credit point of sale; and
- (k) alternatives to a point-of-sale ban.

- *Positive effects of a point-of-sale ban*

213. Parties that were supportive of the point-of-sale ban considered that it would give customers more choice and would encourage customers to shop around, and hence would increase competition. The Post Office and [X] said that additional providers would enter the stand-alone market and the Post Office said that all the existing providers would stay in the market as the product would still provide profitability without underwriting risk. One party ([X]) said that the ban would increase customer choice as they would have a choice of provider and policy whereas now they were only presented with one option. These parties said that the option would be more

effective if information about PPI was provided at the credit sale as this would stimulate demand, and if the ban was for a period that was long enough for customers to search.

214. For distributors, the choice to stay in the market would depend on how many customers would still buy PPI and how many they could access—in other words, it would be a straight business decision based on expected returns. We were told that, if there was a point-of-sale ban, they were concerned that others might leave the market. [X] said that it would need to consider the economics of selling PPI in such an environment, including what the success rate would be in contacting the customer and getting them to listen to advice and to take the product. [X] said that it believed that, if option 4 were imposed, it would need to launch a stand-alone PPI proposition to continue to operate in the market, and [X] said that it would have to consider launching a stand-alone policy if certain remedies, in particular options 4 and 11, were to be imposed. [X] said that there was contribution and income associated with PPI that it would not want to lose and so therefore it would seek to get it if it was economically viable for it to do so.

- *Reduced take-up of PPI*

215. Many parties said that a point-of-sale ban would reduce the take-up of PPI⁷¹ in the short term, and, in the views of many, in the longer term as well. They said that, without promoting PPI at the point of sale, certain customers would not identify their need, particularly as customer awareness of PPI before the point of sale was low.⁷² In addition, parties said that a high proportion of customers would not bother to

⁷¹[X] estimated that sales would reduce to a third of the current level based on lower levels of sales coming from post-point-of-sale marketing.

⁷²ABI response to Remedies Notice p6, Axa response to the Remedies Notice, p6, Capital One response to Remedies Notice p3, Legal and General response to Remedies Notice pp3–4, Lloyds TSB response to the Remedies Notice p15, RBSG response to the Remedies Notice p11.

purchase PPI following the credit sale as it would be less convenient for them to do so.⁷³

216. We were also told⁷⁴ that parties would be unable to contact credit customers regarding PPI after the credit sale as many signed to say that they did not want to be contacted, or the parties were likely to find it difficult to arrange another meeting or conversation with the customer, once he/she had concluded his/her credit arrangement. The FLA said that a large proportion of credit customers did not want to be followed up with additional marketing materials. The BBA said that a significant proportion of bank customers used the option of ruling out any further contact from their bank at the credit point of sale. According to data it had received from its members, this applied to up to 76 per cent of all bank customers in some cases. Nationwide said that only 3 per cent of its unsecured personal loan and credit card customers had bought PPI or altered an existing PPI policy to cover the new credit after it temporarily withdrew its PPI product in August 2007;⁷⁵ Nationwide told us that this indicated that only a small number of people would buy PPI if it was not sold at the point of sale. Parties also said that customer complaints may or would rise; different reasons were put forward by different parties, including that customers would not understand why they could not purchase at the point of sale and that some customers might become suspicious of the product.⁷⁶

217. In this context, we also looked at the change in the number of LifeChoices policies and PPI policies that HSBC sold through its branch network. In December 2007,

⁷³ Abbey response to Remedies Notice p10, BBA response to Remedies Notice p4, Citizens' Advice response to Remedies Notice pp10–11, Genworth response to Remedies Notice pp6–7, Lloyds TSB response to Remedies Notice p16, RBSG response to Remedies Notice pp11–12.

⁷⁴ Barclays response to the Notice, p15, BBA response to Remedies Notice p4, Banque PSA response to Remedies Notice p6, Council of Mortgage Lenders response to Remedies Notice p5, FLA response to Remedies Notice p21, Lloyds TSB response to the Notice, p16.

⁷⁵ Since 16 August 2007 Nationwide has temporarily stopped selling CCPPI and PLPPI. The revised sales process included a discussion on PPI and a suggestion of useful sources for information regarding PPI. In January to April 2008 Nationwide contacted 946 of its customers and found that 5 per cent of them had gone on to get a PPI quote and 1 per cent had gone on to purchase a new PPI policy, while 2 per cent altered an existing policy to get the additional cover to protect the new credit.

⁷⁶ Axa response to Remedies Notice p7, RBSG response to Remedies Notice p11.

HSBC withdrew advised sales in branches of PLPPI and instead offered personal loan customers the opportunity to discuss their wider protection needs with a Financial Planning Manager, with LifeChoices one of the products offered to those customers.⁷⁷ Figure 2 of [Appendix 2.3](#) of our provisional findings showed that there was a decline in PLPPI sales for which the increased sales of LifeChoices did not fully compensate, and we considered that this could be explained by the delay in the time from when the customer buys the credit product to the time they spoke to the Financial Planning Manager to discuss their protection needs.

218. We consider that the potential reduction in PPI sales has been overestimated by some parties and that, by increasing competition and thereby reducing price, our remedy package should lead to PPI sales that are higher than they would otherwise be. Most of the estimates of the potential drop in PPI sales have been based on PPI take-up rates after the point of sale at which point the majority of customers who were interested in buying PPI have been able to do so. In Nationwide's case, the estimates of the potential fall in penetration have been based on a situation where stand-alone PPI products are not widely promoted, at a time before the FSA comparison website was available and where the credit provider was not selling PPI at all.
219. In addition, we consider that our proposal to permit the provision of information about PPI at the credit point of sale (see paragraphs 251 to 261) and our requirement to provide a firm quote (see [Figure 6](#)) would significantly reduce any risk that customers would not consider the product, due to lack of awareness at the credit point of sale.
220. We note that there is no intrinsic reason why distributors would stop selling any type of PPI if they could not sell it at the point of sale. No distributor said that it would

⁷⁷Advised sales in branches of CCPPI were also withdrawn at this time. HSBC's MPPI product had been replaced by LifeChoices earlier in 2007. See paragraphs 3 to 7 of [Appendix 2.3](#) of our provisional findings.

leave the market if a ban like the one described below was introduced; most distributors said that they would have to consider the business case for continuing to sell PPI. [X] said that it believed that, if option 4 were imposed, it would need to launch a stand-alone PPI proposition to continue to operate in the market. [X] said that it would have to consider launching a stand-alone policy if certain remedies, in particular options 4 and 11, were to be imposed (see paragraph 214). Given that the income and margins from PPI are currently high (see [Appendix 4.4](#) of our provisional findings),⁷⁸ and PPI sales also benefit distributors, whose credit customers are insured, we consider that even if marketing costs increased, it would still be beneficial to firms actively to sell PPI. We also note that the option outlined below allows for customers—at their own instigation—to buy PPI directly from the distributor by Internet or over the phone 24 hours after the credit sale, which would decrease any follow-up costs for those customers.

221. Another way of considering the impact of the point-of-sale ban put to us was that fewer credit sales would be made. [X] said that a consequence of [X] was that it had significantly increased its credit cut-offs, resulting in a large reduction in credit sales. It said that a point-of-sale ban would result in a combination of losses to customers through higher credit prices and reduced credit availability, the cost to consumers of adverse selection, and the cost to consumers of additional search. We considered in paragraph 115 that, with increased competition in PPI markets, credit prices and cut-off scores would reach a new equilibrium, and we concluded in paragraph 121 that we should not amend our remedies to take account of a relevant customer benefit of lower credit cut-off scores.

⁷⁸The aggregate income as a percentage of GWP was 69 per cent for all PPI, 66 per cent for PLPPI, 77 per cent for CCPPI and 52 per cent for MPPI.

- *Inability of the remedy to address all aspects of the point-of-sale advantage*

222. A few parties⁷⁹ expressed concern that the option would not comprehensively address the point-of-sale advantage. These parties said that the incumbency advantage of the credit supplier was not limited to the customer interaction of the point of sale but was an issue throughout the term of the credit as the credit supplier was the only firm that would be aware of the credit.

223. We agree that the remedy proposal outlined in Figure 6 would not entirely remove all aspects of the point-of-sale advantage. However, we did not think that we needed completely to remove the incumbency advantage of distributors in order effectively to remedy the AEC.

- *Length of the ban*

224. There are four main issues that we have had to consider regarding the length of the ban:

- (a) the potential for customer detriment from not being able to buy the distributor's PPI policy at the time of the credit purchase and hence not be covered from that point;
- (b) the interaction with other regulations regarding the credit agreement and the insurance;
- (c) the length of time that it will take customers to search the market; and
- (d) the length of time it may take other PPI providers to market effectively to customers who had recently bought a credit product. We were told that stand-alone providers may need up to 90 days to find and sell to individual customers, but that, conversely, customers could search the market in a matter of hours.

⁷⁹ABI response to Remedies Notice p7, Axa response to Remedies Notice p6, Capital One response to Remedies Notice p3.

225. Nearly all parties⁸⁰ highlighted that a point-of-sale ban could lead to customers being exposed to more risk during the initial period of the credit agreement. Several⁸¹ pointed to a significant number of claims in the first period of the policy; eg 7 to 26 per cent of policies that are claimed on are claimed on in the first 90 days.

226. We sought evidence from the parties⁸² on the number of PPI customers who have claimable events early in the life of a policy. The evidence suggested that only very few customers suffer a claimable event in the first 14 days of a PPI sale, and very few receive the first payment on a claim in the first 14 days. For example, for most PPI policies sold in 2007, fewer than one in 1,000 customers received the first payment on an insured event within the first 14 days. Moreover as the current proposal would allow customers to buy stand-alone products during the ban, so the figures in Table 1 represent an upper bound on potential customer detriment.

TABLE 1 **Percentage of PPI customers experiencing insured events in either the first 14 days or from 15 to 30 days of the policy***

	<i>per cent</i>							
	<i>PLPPI</i>		<i>SMPPPI</i>		<i>CCPPI</i>		<i>MPPI</i>	
	<i>0–14 days</i>	<i>15–29 days</i>	<i>0–14 days</i>	<i>15–29 days</i>	<i>0–14 days</i>	<i>15–29 days</i>	<i>0–14 days</i>	<i>15–29 days</i>
<i>Customers who suffer a claimable event within these time periods</i>								
[X]	0.06	0.09	-	-	0.01	0.01	0.13	0.09
[X]	0.05	0.09	0.11	0.12	-	-	-	-
[X]	0.11	0.06	0.16	0.06	0.02	0.02	0.02	0.05
<i>Customers to whom the first payment on a claimable event was made within these time periods</i>								
[X]	0.00	0.00	-	-	-	-	0.00	0.00
[X]	0.18	0.09	-	-	-	-	0.00	0.00
[X]	0.04	0.04	0.57	0.00	0.00	0.01	0.17	0.01
[X]	-	-	-	-	0.00	0.01	-	-
[X]	0.00	0.01	0.00	0.00	0.00	0.00	0.29	0.12
[X]	-	-	-	-	-	-	-	-
[X]	-	-	-	-	0.00	0.00	-	-
[X]	0.00	0.00	0.00	0.00	0.00	0.00	0.02	0.00

Source: CC, based on information provided by the parties.

*As we are concerned with assessing detriment to the total customer base, we have based the table on the percentage of claiming customers/total customers who could claim rather than the percentage who have claimed as in paragraph 225. In most cases, the percentage figures relate to the first payment date. However, for [X], [X] and [X], the figures relate to when the loss event actually occurred. Numbers are rounded to two decimal places.

⁸⁰Abbey response to Remedies Notice p10, ABI response to Remedies Notice p6, AFB response to Remedies Notice p5, AIFA/AMI response to Remedies Notice pp3–4, Axa, Barclays response to Remedies Notice p14, Cattles response to Remedies Notice p16, FLA response to Remedies Notice p21, FISA response to Remedies Notice pp1–2, FSA response to Remedies Notice p14, Lloyds TSB response to Remedies Notice p15, MBNA response to Remedies Notice p7, Paymentshield response to Remedies Notice p2, RBSG response to Remedies Notice p11.

⁸¹AFB response to Remedies Notice p5, Barclays response to Remedies Notice p15, Cattles response to Remedies Notice p21, FLA response to Remedies Notice p21, Genworth response to Remedies Notice p7, Lloyds response to Remedies Notice p15, RBSG response to Remedies Notice p10.

⁸²[X].

227. In addition, PPI policies sold by the credit provider could be designed to offer cover backdated to the date of the credit sale, particularly given the information that is gathered at the credit sale regarding the ability for the customer to repay the loan.
228. We consider that 14 days would give customers adequate time to search the market and to have the opportunity to see advertisements from stand-alone providers. However, the remedy proposal allows customers proactively to return to their credit provider 24 hours after the credit sale and, when they have the price quote, to buy PPI from the credit provider, if they wish to do so.
- *Reduced consumer choice*
229. Many parties said that any point-of-sale ban would lead to a reduction in consumer choice. The main reason put forward for this was that consumers would be unable to purchase their credit provider's PPI during the period of the ban. Several parties also considered that the reduction in choice would be particularly detrimental to customers as the PPI provided by the credit provider was generally of a better quality, or may be better value, than that provided by stand-alone PPI providers.⁸³ Some parties⁸⁴ also suggested that the point-of-sale ban would lead to market exit by some providers, perhaps as a result of increased adverse selection, and hence a reduced choice for customers.
230. We conclude that option 4 will not reduce customer choice. If customers wish to buy the distributor's product, they can do so from 24 hours after the credit sale. However, in the meantime customers will have been able to shop around for alternative policies. The number of alternatives is likely to rise as both high street banks and

⁸³Abbey response to Remedies Notice p10, Aviva response to Remedies Notice p14, Barclays response to Remedies Notice p16, MBNA response to Remedies Notice p7.

⁸⁴Abbey response to the Remedies Notice, pp10–11, Aviva response to the Remedies Notice, pp1&15, Banque PSA response, Barclays response to the Remedies Notice, p16, HSBC response to the Remedies Notice, p12, Lloyds TSB response to the Remedies Notice, p16, MBNA response.

specialist stand-alone providers are more likely to offer more stand-alone PPI policies if the ban is introduced, because of the increased pool of customers searching for such policies. We therefore consider that the remedy increases the choice to consumers from one to many.

- *Lower-quality products*

231. We were told⁸⁵ that a prohibition on selling PPI at the point of sale, or any option that increased stand-alone provision would lead to a decline in quality and a less tailored PPI product. Parties⁸⁶ highlighted our provisional findings which, they said, indicated that in general the stand-alone providers had less feature-rich policies and longer exclusion periods. They also said that as stand-alone providers had greater adverse selection issues, it was unlikely that the policies could ever be of the same quality. However, stand-alone providers told us that if the market for stand-alone increased, many of the adverse selection issues would decrease as the pool of risk would be larger. Furthermore credit providers highlighted their unique position, not shared by stand-alone providers, of being able to pay the insurance against the loan—thus not affecting state benefits—and being able to assess the combined affordability of the credit and the PPI so that customers did not become over-indebted.

232. Whilst there are stand-alone products which offer a lower level or quality of cover, these products are also generally sold at a significant discount to those sold at the point of sale. However, using Defaqto score as a comparative indicator of quality,⁸⁷ we noted that stand-alone MPPI products achieve similar scores to MPPI products sold at the point of sale (see [Figure 1](#)). We did not carry out a similar analysis for stand-alone and point-of-sale PLPPI policies, as we could not find a suitable metric

⁸⁵See, for example, Abbey response to the Remedies Notice, paragraph 4.1.5, ABI response to the Remedies Notice, p7, Aviva response to the Remedies Notice, p16.

⁸⁶See, for example, Abbey response to the Remedies Notice, paragraph 4.1.5, Aviva response to the Remedies Notice, p16.

⁸⁷We considered the merits of using the Defaqto rating system as a measure of product quality in paragraph 4.27 of our provisional findings.

which allowed a simple and fair comparison of the price of each type (see paragraphs 322 and 323).

233. A clearer comparison of the quality of point-of-sale and stand-alone policies would take into account these differences in price. We have found that once differences in price are accounted for, there is no evidence that stand-alone policies are more highly priced (for a given level of quality), or offer lower quality (for a given price) than policies offered at the point of sale. If anything, the data indicated that the opposite appears to be true (see paragraph 41 and [Figure 1](#)).

- *Higher costs for distributors*

234. It was also put to us⁸⁸ that the point-of-sale ban would lead to additional costs, as credit providers would have to contact customers at the end of the ban and in many cases the information from the loan would have to be collected again. Capital One told us that this increase in costs would mean that it would be uneconomical proactively to offer PPI to customers with lower credit limits (who were in general higher risk) and as a result higher-risk customers might have reduced access to PPI (though if these customers wanted PPI they would be able to buy it).

235. We noted that our remedy proposal would mitigate some of these costs compared, for example, with a longer ban or one in which customers were not able proactively to return to the credit provider soon after the credit sale. We did not see any reason, in particular, why a distributor would need to collect information in relation to a loan a second time, 14 days after issuing a loan, in order to offer PPI to one of its credit customers.

⁸⁸See, for example, Capital One response to the Remedies Notice, p3, and Lloyds TSB response to the Remedies Notice, p15.

236. However, we acknowledge that this remedy option will impose set-up and ongoing costs on distributors. Our analysis of evidence submitted to us so far on the costs of implementing our remedy package can be found in paragraphs 387 to 394 and in Appendix 11. We did not have much confidence that the estimates provided to us to date, in relation to this remedy in particular, represent an accurate indication of its likely set-up and ongoing costs. Some providers told us that they were unable to provide us with any estimate of costs, given the level of detail that was provided in the Notice. There was a wide variation in the estimates that were provided (see paragraph 389), possibly reflecting different perceptions of what the remedy would entail as well as different business models. We are therefore inviting further representations on costs (see paragraph 392).

- *Different impact on different providers*

237. We were told⁸⁹ that a point-of-sale ban would give an unfair advantage to stand-alone PPI providers. A number of parties talked about the removal of a level playing field. Barclays said that the option was ‘pro-competitor’ rather than ‘pro-customer’. However, two firms, [X] and [X], told us that it would give a competitive advantage to high street banks, which would be able to cross-sell PPI in many different circumstances such as when customers came into a branch, and because they could leverage their knowledge of customers’ current accounts to cross-sell PPI policies on new loans.

238. We consider that a point-of-sale ban will provide additional commercial opportunities to firms that sell stand-alone PPI but see no reason why distributors could not also benefit from these opportunities by selling PPI on a stand-alone basis. By allowing consumers proactively to return to the credit provider to buy PPI soon after the credit

⁸⁹See, for example, Abbey response to the Remedies Notice, pp3&12, Barclays response to the Remedies Notice, p14, Lloyds TSB response to the Remedies Notice, p17, RBSG response to the Remedies Notice, pp1,13.

sale, we are ensuring that consumers can buy PPI from their credit provider within a similar timescale as they could buy it from a stand-alone provider. This in turn minimizes any competitive disadvantage experienced by distributors.

- *Restriction on the freedom of establishment*

239. One party ([X]) also raised concerns that the option could amount to a restriction of the right of freedom of establishment under EU law, which could only be justified where overriding requirements of public interest were at stake (such as protection of consumers), and provided that the measures proposed were suitable for securing the attainment of this objective and did not go beyond what was necessary in order to attain this objective.

240. Whilst we do not agree that the proposals would infringe the right of freedom of establishment, we note that proportionality is in any event a relevant consideration under the Act. The test that we are obliged to apply in considering remedies under the Act requires us to have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the AEC and any detrimental effects on consumers resulting from the AEC.⁹⁰ In addition, our guidance makes clear that in considering remedies we will have regard to the principle of proportionality.⁹¹

- *Information at the point of sale*

241. We received various comments about the information that should be provided to customers about PPI at the point of sale. One party (RBSG) raised concerns that a point-of-sale ban would impact on its duty of care to its customers. It said that regulatory requirements meant that it had to have appropriate discussions with credit customers about the consequences of entering into credit arrangements and the steps that they could take to protect their interest before selling credit to them. In

⁹⁰Enterprise Act 2002, [section 134\(6\)](#).

⁹¹CC3, paragraph 4.9.

RBSG's view, these requirements would require it to inform customers about the existence of protection products such as PPI. However, HBOS did not agree and said that it had found nothing in the Consumer Credit Act 2004 which would require that the credit provider gave advice on or offered protection for the credit product. Another party (Legal & General) said that for MPPI the point-of-sale ban would be in direct conflict with the Government's sustainable house ownership initiative where customers were encouraged to make provision for times of hardship.

242. Some distributors and the FLA said that lenders needed to assess affordability of the package. Lloyds TSB said that it needed to inform customers about the overall affordability of the loan and PPI so that they would have a clear view of the cost.
243. The Post Office said that its preferred outcome was that credit providers would encourage customers to consider their protection needs through a number of agreed statements and be able to offer a firm quote and product information to assist the customer in comparing alternatives.
244. The FSA told us that, to be effective, the information provided would have to be given to all consumers who requested it rather than just to consumers who went through the sales process, as was currently the case, to enable consumers to use them for comparative purposes.
245. In our view, identifying the appropriate information to be provided at the point of sale depends on a number of factors:
- (a) the amount of information required by customers to make an informed choice when shopping around (after the point of sale);
 - (b) the cost to the distributor of providing the information (both in terms of interview time and marketing materials);

- (c) the need to ensure that customers who would benefit from PPI are informed about it; and
- (d) the need for credit providers to exercise their duty of care to customers as well as the need for customers to be able to assess the affordability of credit with or without PPI.

246. We consider that the provision of a personal quote would enable customers to compare the credit provider's PPI policies against others in the market and make an informed choice as to which would most suit their needs and their income. It would also help consumers if they wish to search for the best combination of credit and PPI. In addition, the provision of a price quote would allow lenders to fulfil any duty of care they believe they have to customers. Finally, we do not consider that there is any inherent reason why most customers could not in the future compare products and choose the policy that most suits their needs.

- *Alternatives to a point-of-sale ban*

247. A number of parties also suggested alternatives to the point-of-sale ban which they considered would address the AEC in a more proportionate manner. These alternatives are listed below:

- (a) Some parties⁹² suggested continuing to sell PPI at the credit point of sale, but emphasizing or increasing the cooling-off period in which PPI could be cancelled without cost to the consumer (for example, increasing it to 90 days); in addition, the customer could be given information about the existence of other PPI policies at the point of sale and use the cooling-off period to search for a more attractive alternative.

⁹²See, for example, Barclays response to the Remedies Notice, p18, HSBC response to the Remedies Notice, pp11–12, Lloyds TSB response to the Remedies Notice, p17.

(b) Two parties ([REDACTED]) suggested an access remedy as an alternative to option 4. This would involve a number (possibly three or four) of PPI providers having access to the customer at the point of sale. The credit provider would have PPI policies from these providers available at the point of sale of credit and would advise on the most appropriate one for the customer's needs. One party ([REDACTED]) said that this option would have to be introduced with [REDACTED] an IT system that took the decision out of the hands of the salesperson. The remedy envisaged that sales would be made on an advised basis.

(c) Which? suggested that all PPI sales should be advised and that sales personnel that sold PPI would have to explain to the customer why PPI was better than an income protection product. It said that that would result in a similar system to how pensions are sold under the RU64 FSA⁹³ rules for pension advisers.

248. We consider that a ban on selling PPI at the point of sale would be the most effective way of addressing the point-of-sale advantage and would form part of a reasonable and practicable solution to the AEC that we have provisionally found. The alternative suggestions from the parties would either be more complicated to monitor and likely to be ineffective or would not address the AEC that we provisionally found:

(a) Increasing the cooling-off period would not effectively address the AEC as customers seem less inclined to change policies once they have purchased them, even when they consider that they could get a better value-for-money product elsewhere.⁹⁴ For example, Cardif Pinnacle said that it was actually quite difficult to convince consumers to switch once they had made that emotional commitment and the selling process got a little bit tougher. We noted that on average 5 per cent of customers between January 2006 and December 2007 cancelled their PPI policy in the first 30 days, and at least some of those did not

⁹³RU64 requires an adviser to explain to a customer in writing why the personal pension they are recommending is at least as suitable as a stakeholder pension—source www.fsa.gov.uk/pages/Library/Communication/Statements/2007/ru64.shtml.

⁹⁴Financial Services Authority—*Financial Capability: A Behavioural Economics Perspective*, 2008.

switch another policy but just stopped buying protection. Further, we found that few consumers who did compare policies revisited their purchase decision during the cooling-off period (see paragraph 5.109 of our [provisional findings](#)).

- (b) In terms of an access option, controlling the sales process to enable the sale or promotion of alternative PPI at the point of sale would be very challenging and difficult to monitor, particularly given the benefits to distributors of selling PPI and the benefit of selling their own PPI in a vertically integrated firm.
- (c) A requirement to sell PPI on an advised basis would not, in our view, address competition issues, as an advised sale relates only to the suitability of the product or products offered by that distributor or independent financial adviser.
- (d) In addition, ensuring that customers are told about income protection products would not necessarily address the lack of shopping around or significantly decrease the point-of-sale advantage.

249. We also considered whether the provision of a personal quote at the point of sale would be sufficient, alongside the information remedies we propose to implement and an existing or extended cooling-off period, to facilitate competition without the need for a point-of-sale ban. We decided that this would not be an effective remedy package. As noted in paragraph 248(a), we found that few consumers who did compare policies revisited their purchase decision during the cooling-off period. We noted that a recent study found that the incorporation of a written quotation into the remedy package for extended warranties, where no point-of-sale ban was put in place, does not appear to have had an appreciable impact on customer behaviour.⁹⁵ We concluded that providing a quote at the point of sale, after the customer has taken out the loan and during the sales process for a linked PPI product, would not have a significant effect on a consumer's searching behaviour.

⁹⁵ *Evaluating the impact of the Supply of Extended Warranties on Domestic Electrical Goods Order 2005*, prepared for the OFT by LECG, October 2005. LECG found that customers did not always receive the quotation and, where they did, there was little evidence that they used it for shopping around.

250. We also found in paragraph 5.87 of our [provisional findings](#) that there are significant barriers to entry for stand-alone PPI providers seeking to sell PPI products without access to customers at the credit point of sale, due to adverse selection, poor consumer awareness and high marketing costs. These factors would not be addressed by the provision of a personal quote, as part of a package of information remedies. We concluded that a package of information remedies alone would not be sufficient to remedy the AEC that we found.

Provisional decision on implementation of remedy

251. We concluded that a prohibition on selling PPI at the point of sale of credit, and for 14 days afterwards, would mitigate the effect on competition of the point-of-sale advantage by prompting customers to shop around and thereby addressing the credit provider's market power at source. Allowing consumers to receive information about the credit provider's PPI product during the credit sale, alongside the obligation to provide a personal quote if the provider intends subsequently to offer PPI to that customer, would provide consumers with information that would help them search between PPI policies as well as an incentive and opportunity to search. We consider that, given the margins currently earned on PPI and the size of the market, it would be in the interest of most credit providers to continue to sell PPI and to compete for customers by increasing marketing spend and reducing prices. The ability of customers to purchase PPI during the period of the ban, provided that 24 hours has elapsed since the purchase of credit, will prevent distributors from being placed at a competitive disadvantage. Hence we consider that this option will lead to more competition, increased advertising, and lower prices for customers. We conclude that a point-of-sale ban is the only option that will effectively address the point-of-sale advantage outlined in the provisional findings, and as such is essential to achieving a comprehensive solution to the AEC and resulting consumer detriment.

252. We have developed the point-of-sale ban remedy option into a set of measures (see [Figure 6](#)). These measures aim to ensure the remedy's effectiveness in addressing the point-of-sale advantage enjoyed by distributors, in providing a greater incentive and opportunity for customers to search for PPI after the credit sale, and in making it easier for stand-alone providers to access customers around the time of the credit sale. The measures also address some of the parties' concerns regarding the option, in particular the concern about not being able to discuss PPI at the initial credit sale and allowing customers who want the credit provider's PPI to purchase it quickly and conveniently.
253. The remedy proposal builds on option 4 in the Notice to separate the sales process for PPI and credit. The proposal allows credit providers to talk to customers about PPI at the credit sale and requires them to provide a personalized PPI quote if they intend subsequently to offer them PPI (see Appendix 8) but not actively to sell PPI to or contact the customer regarding PPI for a short period (14 days) after the credit sale. In addition, the proposal allows customers who want to purchase the credit provider's PPI to do so through the Internet or by telephone one day after the credit sale, if they confirm that they have received a personalized quote. We will work with the FSA to ensure that the obligation to provide the personalized PPI quote is fully compatible with the ICOBS requirement to provide a policy summary or key features document and to provide a document that outlines prices in a durable medium so that no additional documents need to be sent or given to the customer.⁹⁶

⁹⁶The Policy Summary informs the customer about the product: <http://fsahandbook.info/FSA/html/handbook/ICOBS/6/Annex2>. This document has no standard format, except that it must be in a durable medium. Firms can choose to give customers the key features document instead (only the general requirements are need for PPI): <http://fsahandbook.info/FSA/handbook/COBS/13/3.pdf>. A document that outlines prices in a durable medium—before the conclusion of a contract in a non-distance sale or immediately after the conclusion in a distance sale: <http://fsahandbook.info/FSA/handbook/ICOBS/6/4.pdf>.

FIGURE 6

Remedy proposal for all PPI sales by distributors

Before the credit sale

PPI advertising is allowed; sales personnel can discuss PPI in general terms with customers.*

At the credit sale†

The credit provider cannot sell PPI at any point in this interview.

The credit provider cannot include PPI in the 'primary credit agreement' (the credit agreement which relates to the credit that the PPI is primarily sold to insure).

Generic information‡ regarding PPI can be provided to the customer.

A standard form personal PPI quote (the 'personal PPI quote') must be provided to the customer in a durable medium (see Appendix 8 for details) if the credit provider provides information about PPI to the customer at the credit sale. For Internet, direct mail and telesales, this personal PPI quote must be emailed or otherwise sent to the customer within 3 days of the credit sale.

If a credit provider does not provide a personal PPI quote at the credit sale, but subsequently contacts the customer to offer PPI, a personal PPI quote must be provided at that time and the prohibition period starts from the date on which the personal PPI quote is provided to the customer.

No distributor can charge more for PPI than the cost of the regular or annual premium. For example, there can be no administration fees, set-up fees or early termination fees.

If the sales person mentions PPI orally, then they must also orally disclose the key messages (see paragraphs 1 to 3 of Figure 4).

Directly after the credit sale

The customer can buy a PPI policy from any distributor other than the credit provider, any company recommended by the credit provider at the point of sale, or any company to which information regarding the customer which was obtained in the credit sale has been passed.

24 hours after the credit sale§

The customer can buy a PPI policy on the Internet or by calling a telephone number from the credit provider (which is provided in the personal PPI quote). However, the customer must confirm that they have seen the personal PPI quote (and the credit provider has to be reasonably satisfied that the customer has seen the personal PPI quote) before any PPI sale can be made.

Fourteen days or more after the credit sale§

The credit provider can contact the customer with regard to PPI. However, the customer must confirm that they have seen the personal PPI quote (and the credit provider has to be reasonably satisfied that the customer has seen the personal PPI quote) before any PPI sale can be made. This contact can be made in the activation process of a credit card, provided this is 14 days after this credit sale.

*To avoid circumvention of this remedy, the credit provider cannot 'pre-sell' PPI to insure a credit agreement it has discussed with a consumer and has reasonable grounds to expect it will agree with that consumer within the following 14 days.

†Defined as the interview to arrange credit with the credit provider or an interview in which credit is sold by the credit provider to the consumer. For telesales, the credit sale is the telephone call in which the credit is arranged or orally confirmed, whereas with an Internet or direct mail sale, the credit sale is only complete once a confirmation email or letter is sent to the customer confirming that the credit is arranged or has been transferred.

‡Generic (ie not personalized for the customer). The FSA describes this information as information that could reflect the terms of a contract which is representative of the PPI normally undertaken by the firm rather than the terms of a particular contract with, or that will be offered to, a particular customer.

§Or after the provision of a personalized PPI quote if one were not provided at the credit sale.

254. We consider that all costs should be included in the price of the premium. If there were other fees included, then it would become harder for customers to compare price and to shop around using the personal price quote.

255. Given the importance of the personal PPI quote to the effectiveness of this remedy, we propose that credit providers should have to confirm with customers that they have seen it and that they have to be reasonably sure that the customer could have seen it.⁹⁷ To enable customers to shop around for PPI in situations in which the credit provider does not normally mention PPI at the initial credit sale but contacts the customer at a later date to offer PPI, we propose that, in these circumstances, the prohibition period should apply from the date on which the personal PPI quote was provided, rather than date of the credit sale.
256. We propose that customers should be able proactively to buy PPI from their credit provider 24 hours after the credit sale (or provision of a personal PPI quote). This enables customers to consider their options and also reduces the risk that customers are in any way encouraged to buy PPI after the credit sale but before they either leave the credit provider's premises or put down the telephone—for example, by being given access to the Internet in-branch or given assistance to complete a PPI application. We also consider that the clear break will be easier for sales staff to understand and will make the remedy easier to monitor.
257. We consider that the proposal above will give credit providers sufficient scope to contact and follow up with customers who are interested in PPI, and to achieve sales from those consumers who actively want to contract with them. We noted that in other insurance markets, notably travel and household insurance, advertising is not restricted to direct marketing to individual customers; television and press advertising are also used effectively to obtain sales. Even if credit providers could not follow up with all their customers individually, they would still be able to attract sales through other forms of marketing.

⁹⁷For example, if a provider sent a personal price quote on a Monday evening by second class post and the customer called on the Tuesday morning, it would be unlikely that they customer would have seen it.

258. We consider that this remedy would increase marketing spend on PPI, which we consider to be low given the size and profitability of the market. For example, we note that the UK travel insurance market is estimated to be worth around £709 million⁹⁸ in terms of net written premium and has an advertising spend of £5.5 million⁹⁹ (not including Internet advertising). We also noted that the household insurance market grew to £6,392 million in GWP in 2006 and had a marketing spend of over £100 million¹⁰⁰ and that [X] predicted that it would spend £7.5 million on direct marketing business in 2008, whereas PPI had a GWP of £4.4 billion in 2006 and only a few examples of distributors actively promoting their PPI or advertising campaigns specifically featuring PPI policies (see paragraph 4.20 of our [provisional findings](#)).
259. A point-of-sale ban would have the greatest impact and be most effective if:
- (a) distributors continue to promote PPI at the point of sale: this would prompt customers to consider PPI and to shop around;
 - (b) standardized information is provided, to ease comparison with information from other PPI providers;
 - (c) stand-alone providers (including credit providers selling PPI to other credit providers' customers) take advantage of the point-of-sale ban to expand the marketing of their PPI policies: this would increase customers' awareness of PPI and the price of PPI; and
 - (d) customers use the opportunity to shop for alternative protection products.
260. We consider that the option above would work best in conjunction with other options aimed facilitating consumer search, in particular options 1 (requirement to provide information in advertisements), 3 (requirement to provide information to the FSA for use on its website) and 7(a) (ban on single premiums).

⁹⁸Defaqto—*Travel Insurance 2008; Adapting to a changing world*, 2008.

⁹⁹Datamonitor—*UK Travel Insurance 2007*, 2007.

¹⁰⁰Datamonitor—*UK Household Insurance 2007*, 2007.

261. We consider that if we took this remedy forward it could be implemented within 9 to 12 months of any CC Order and could be monitored by the OFT, supported by suitably comprehensive compliance reporting requirements on the parties (see paragraph 370).

Option 6: Annual statement of cost and a reminder of the customer's right to cancel and early settlement terms

A summary of the proposal from the Notice

262. In the Notice, we proposed a requirement mandating the provision of a statement every 12 months from the date of purchase (the 'annual statement') detailing the annual and lifetime cost to the consumer of the PPI policy and containing a reminder of the customer's right to cancel the policy and to switch PPI provider, the existence of alternatives and, in the case of single-premium policies, a reminder of the early settlement terms. We suggested that this statement could be provided along with the CCA 2006 statement.
263. We provisionally found that there are barriers to switching, which prevent, restrict and distort competition. We considered that an annual statement could raise awareness of customers' ability to switch PPI provider, enhancing the effectiveness of other measures aimed at directly reducing switching costs.

Responses to the Notice and our views on the issues raised

264. Many parties were in favour of an annual statement. In general, parties said that annual statements would increase transparency and clarity and would be likely to increase customer switching.¹⁰¹ At a minimum, parties told us that an annual statement would ensure that customers were considering whether the policy continued to meet their needs on a regular basis (the Post Office) and would remind customers

¹⁰¹See, for example, Citizens Advice response to the Remedies Notice, p12, and HBOS response to the Remedies Notice, p5.

that they had a policy (PaymentShield). Openwork also said that annual statements would be a sensible move, which would bring the product more in line with consumers' understanding of other general insurance products, such as motor and home insurance. In addition, [X] and [X] said that they would see the statements as an opportunity to gain customers. [X] said that it would be likely to market to them more. [X] said that it seemed like an opportunity it could attempt to make something of. A few parties¹⁰² said that this option would encourage customers to cancel their policies rather than switch, which they said would be detrimental to those customers as they would no longer be protected. Furthermore, CCPPI distributors said that their customers effectively received such a statement every month and therefore the provision of an annual statement would be superfluous and would just add to costs.

265. We agree with the parties that an annual statement would be helpful to customers and would increase switching. We consider that an annual statement would increase transparency and would help customers compare prices of PPI policies against other PPI policies and other insurance products such as critical illness or income protection. We also consider that the option would increase marketing spend on PPI which we currently consider to be low, given the size and profitability of the market (see paragraph 1 of our [provisional findings](#)). The annual statement would also increase customers' awareness of PPI, the cost they are paying and their ability to switch products. We consider that these benefits apply equally to all types of PPI.

266. Many parties commented on the design and implementation of this remedy, for example:

- (a) whether the statement should be sent with the CCA 2006 statement;
- (b) whether it should remind customers of the benefits of cover; and
- (c) whether the statements should be standardized and if so to what extent.

¹⁰²See, for example, AMI response to the Remedies Notice, p4, and Defaqto response to the Remedies Notice, p12.

- *When the statement should be sent*

267. Respondents were divided as to whether the statement should be sent with the CCA 2006 statement. Some parties,¹⁰³ mostly distributors, said that it should be provided with the annual credit statement as this would reduce costs. However, it was also said that this would be impossible if we also ordered a point-of-sale ban as the timing of the two anniversaries would be different. Other parties, including the OFT and the Post Office, said that the statement should be separate, as combining the statement would further entrench in customers' minds the idea that PPI can only be bought from the credit provider. Which? said that the PPI and the credit were separate purchases and so the two statements should be sent separately. The Post Office also said that combining the statement with the CCA 2006 statement would put stand-alone providers at a cost disadvantage—distributors would be able to minimize the cost impact of this remedy by combining it with credit information they already provided, whereas stand-alone providers would incur the costs of producing and sending out a separate statement.
268. It was suggested that the statements all be sent at the same time in the calendar year as this would enable companies to market PPI, and compete for PPI, most efficiently. Other parties said that this might confuse customers, as they could get an annual statement just after taking out a policy. We were also told that a mass communication at one point in the year might be more costly than sending out statements on the anniversary of each policy's issue.
269. We consider that the statement should not be provided at the same time as the CCA statement. We accepted arguments that the interaction between this remedy and the point-of-sale ban would make it impractical to have the two statements together, and

¹⁰³See, for example, Abbey response to the Remedies Notice, paragraph 5.2.2, and FLA response to the Remedies Notice, p26.

that sending the two statements together would risk sending a mixed message to customers about whether the two products were linked; this could discourage customers from switching to stand-alone providers.

270. We considered the suggestion that all policies should be sent out in the same month. We thought that this might help stand-alone providers to target their advertising in a particular time frame, maximizing advertising impact. However, we agreed with the parties' submissions that sending out all the PPI annual statements in the same month might be confusing to customers, particularly if they had only just taken out a policy and immediately received an annual statement.

271. We concluded therefore that the statement should be sent out every 12 months (or in the two weeks leading up to the anniversary) after the PPI policy is taken out.

- *Information to be included in the statement*

272. In terms of the financial information to be included in a statement, most parties¹⁰⁴ considered that the lifetime cost was of less interest to the customer than the monthly or annual cost. Cardif Pinnacle also said that the statement could include information relevant to obtaining a 'no claims' qualification. It was suggested that the statement could contain the average balance outstanding for CCPPI customers over the previous period, which would give consumers and stand-alone providers an indication as to the level of protection the CCPPI customer would on average need.

273. On the question of what information should be included in the statements, many parties¹⁰⁵ said that customers should be reminded of the benefits of PPI and the need to protect their repayments against certain events. Others suggested that customers should be reminded that they have a choice of PPI supplier and that they

¹⁰⁴See, for example, HBOS response to the Remedies Notice, p5, and MBNA response to the Remedies Notice, p9.

¹⁰⁵See, for example, Assurant response to the Remedies Notice, p4, and Cassidy Davis response to the Remedies Notice, p4.

should be made aware of the risks of switching policies. Some mentioned the likely impact in terms of qualification periods and on pre-existing conditions. Aviva suggested that customers should be provided with a query line for general enquiries.

274. We conclude that annual and monthly costs ought to be provided as part of the statement. This will entail providing the same information as is provided in a personal quote (see option 4). This information will make it easier for consumers to compare their current policy with alternatives, to understand the cost of their policy. We also consider that the statement should set out payments made in the preceding 12 months, allowing customers to see the amount that they have spent on PPI.
275. We agreed with Cardif Pinnacle that providing a summary of the customer's claims history would be useful, both in terms of reminding the consumer as to the actual benefits received during the year (in addition to peace of mind) and in terms of providing information which stand-alone providers might find useful in determining the best price to offer someone interested in switching PPI provider, or whether to offer PPI (for example, in 2008 Cardif Pinnacle advertised a stand-alone PPI policy for consumers who had made no claims on their existing PPI policy).
276. Similarly, we conclude that the provision of the average balance information for credit cards is likely to assist the development of stand-alone provision of CCPPI as it would give customers and stand-alone providers a better indication than the credit limit as to the amount of cover that the customer will actually need.
277. We agreed with Aviva that the inclusion in the statement of a telephone number which consumers can use would be helpful. Consumers should be able to ring the number in order to raise any queries about their policy, or to cancel the policy if they so wish.

278. We conclude that the statement should provide information on what the PPI policy covers (such as the elements it covers, and, for CCPPI, the percentage of balance it pays out each month of a claim). However, we did not agree with parties that the statement should set out the risks of not being insured or the risks of switching. The former was, in our view, unnecessary, and the latter would simply be counter-productive for a remedy aimed at making it easier to switch.

- *Standardization of statements*

279. Some parties¹⁰⁶ were in favour of standardized information which they considered would make the statement easier to use as a comparison tool. Which? said that the key information should be presented in a standardized format in a summary box, while the OFT said that the statement should have to contain prescribed information, with rules on format and prominence. Others¹⁰⁷ considered that this standardization would make the implementation costs higher and could decrease innovation; these parties said that the CC should just state the items that would need to be provided to the customer. For example, HSBC said that we should provide a framework detailing the type of information to be provided, rather than prescribe an exact layout or style, suggesting that this would be more proportionate.¹⁰⁸ Defaqto suggested that the statement should look as much as possible like the personal quote that was given at the point of sale (as set out in option 4). In addition, HSBC said that the annual reminders should be in the same format as the information at the point of sale so that when somebody got a reminder it was very comparable to other quotes provided.

280. The FSA said that any statement should be consumer tested to ensure that it would be effective.

¹⁰⁶See, for example, a large underwriter's response to the Remedies Notice, pp8&9, and Paymentsshield response to the Remedies Notice, p3.

¹⁰⁷See, for example, Paymentsshield response to the Remedies Notice, p3.

¹⁰⁸HSBC response to the Remedies Notice, paragraph 6.7.2.

281. We conclude that a high level of standardization (ie the same information in the same format) would increase the ability of customers to compare products. We note that the *Mortgage Conduct of Business* review by BMRB for the FSA said that the different formats for the disclosure documents, such as the key facts illustration, can make it more difficult for customers to undertake comparisons.¹⁰⁹ In our view, the format should therefore be similar to that of the personal PPI quote (see option 4), to aid comparability. At a minimum, the statement should have to contain prescribed information (outlined in Appendix 9), with rules on format and prominence.

Provisional decision on implementation of remedy

282. We concluded that the provision of an annual statement, including information similar to that provided in a personal quote, would encourage consumers to think about their PPI policy on a regular basis and would make it easier for consumers to switch. We concluded that we should implement this remedy.

283. The proposed remedy is set out below (see Figure 7). These measures aim to ensure the remedy's effectiveness in addressing barriers to switching (which prevent, restrict and distort competition) by providing an additional impetus for customers to search for the best-value PPI and increasing the opportunity for stand-alone provision of PPI.

FIGURE 7

Remedy proposal for an annual statement

On, or in the two weeks leading up to, each anniversary of the customer's purchase of PPI, the customer will be sent an annual statement (see Appendix 9 for details).
Provision of this statement will be the responsibility of the company which sold the PPI policy to the customer (usually either the distributor or the stand-alone provider).
The statement must be provided in a separate mailing from any information on a credit product held by the customer.

¹⁰⁹ *Consumers and mortgage disclosure documentation*, September 2006, FSA (p9).

284. An annual statement would have the greatest impact and be most effective if:
- (a) stand-alone providers (including credit providers selling PPI to other credit providers' customers) take advantage of the annual statement to expand the marketing of their PPI policies; this would in turn increase customers' awareness of PPI and the price of PPI; and
 - (b) customers are prompted to compare alternative PPI products annually and switch if they find better deals.
285. We consider that the annual statement would work best in conjunction with other remedies aimed at increasing the ability for customers to compare PPI products and which remove barriers to switching, in particular options 1 (requirement to provide information in advertisements), 3 (requirement to provide information to the FSA for use on its website) and 7(a) (ban on single premiums).
286. We consider that if we took this remedy forward, it could be implemented within six months of any CC Order and could be monitored by the OFT (supported by standard compliance reporting requirements on the parties). We also agree with the FSA that its design should be consumer tested before implementation to make sure that it has the greatest impact possible.

Option 7(a): A prohibition on single-premium policies

A summary of the proposal from the Notice

287. We have provisionally found that consumers who want to switch PPI policies to alternative PPI providers or to alternative insurance products are hindered in doing so. In the case of single-premium policies, we found that terms which make switching expensive (such as rebates for early termination) act as barriers to switching for PLPPI and SMPPI policies. We consider that this remedy could reduce the financial costs to customers of switching PPI providers.

Responses to the Notice and our views on the issues raised

288. Some parties (Paymentsshield, [X] and the Post Office) were in favour of banning single-premium policies as they considered that regular-premium policies allowed customers to switch more easily between products. Which? said that it could not see any benefits to consumers of single-premium policies. Citizens Advice said that we should consider banning single-premium policies if we thought that the other options would not be effective; it was not convinced by the arguments that single-premium policies benefited customers. In addition, a large distributor ([X]) said that it did not believe that pro-rata rebates would be sufficient to remedy the adverse effects identified by the CC associated with single-premium policies.
289. Other parties¹¹⁰ considered that minimum rebates (option 7(c)) would be equally effective at addressing the switching AEC. These parties considered that option 7(c) was more proportionate as it would not involve reducing customer choice or restricting a firm's product line. We were also told that any move to ban single premiums would lead to a customer detriment as it would lead to higher prices and lower quality.
290. The following issues were raised in consultation:
- (a) whether the remedy would be effective in addressing barriers to switching and whether other remedies are available that would be equally effective;
 - (b) the proportionality of a ban on single premiums if other equally effective remedies were available;
 - (c) whether a prohibition on single-premium policies would increase comparability of PPI policies; and
 - (d) whether a prohibition on single-premium PPI would harm consumers.

¹¹⁰See, for example, Abbey response to the Remedies Notice, pp14&15, and Nationwide response to the Remedies Notice, pp13&14.

- *Effectiveness in removing barriers to switching*

291. We did not receive any representations to suggest that a ban of single-premium policies would be an ineffective remedy to the switching barrier identified.
292. In the Notice, we also put forward two other possible ways of addressing the switching barrier identified:
- (a) requiring distributors of single-premium policies to offer a regular-premium policy with an identical level of cover as the single-premium policy they offered (option 7(b)); and
 - (b) a requirement mandating that single-premium products offered by distributors at least meet minimum terms for early settlement rebates and any additional charges ('minimum rebates'). In particular, we asked whether early settlement rebates should be based on a pro-rata calculation to address the switching costs (option 7(c)).
293. After further analysis and consultation we did not consider that option 7(b) would be an effective way of addressing the switching barrier that we identified and we have not included it in our proposed remedy packages (see paragraphs 352 and 353). However, many parties told us that minimum rebates (option 7(c)) would address all our concerns regarding the switching costs of single-premium policies.
294. All parties were in favour of a fair rebate for customers who cancelled their single-premium PPI policies. However, parties had different views as to what they considered to be fair to the customer and to PPI providers.

295. Some parties¹¹¹ told us that rebates were already fair and that there was therefore little need to change current arrangements significantly. In our view, the current rebate arrangements are a barrier to switching (see paragraph 5.75 of our [provisional findings](#)). As such, we believe that the current rebate arrangements are insufficient. We did not, therefore, accept the views of those parties who told us that a rebate along the lines of those currently offered was sufficient.
296. Other providers told us that pro-rata rebates would be sufficient to address the barrier to switching that we had identified. For example, Nationwide said that it introduced pro-rata rebates when it reintroduced PLPPI policies.¹¹² Nationwide said that it introduced these terms as it considered that such rebates were consumer friendly, as they were easier to explain and more transparent. It also believed that pro-rata rebates would address the barrier to switching that the CC had provisionally found. Nationwide told us that it had been able to introduce this change while making no other changes to its PLPPI product specification. The FSA also said that a pro-rata approach would adequately address switching costs for consumers. London General Insurance said that it accepted that for combined PPI products (which provide cover for life, critical illness, involuntary unemployment and disability due to accident or sickness), pro-rata rebates would be acceptable, due to the risk profile.¹¹³
297. Citizens Advice said that the rebate on a single-premium policy should provide sufficient funds to meet the settlement figure on the loan, otherwise the consumer would either have to borrow more money to settle the loan or would not be able to settle early.¹¹⁴ Citizens Advice said that the rebates currently being offered were not

¹¹¹For example, MBNA noted that rebates are already governed by FSA 'fairness' rules; see MBNA response to the Remedies Notice, paragraph 4.32.

¹¹²As a result, it would refund any premium amount relating to the remaining term of the policy at the time of cancellation. Interest would be charged on the premium on an actuarial basis to the point of cancellation of the PPI policy.

¹¹³However, it said that for products which offered life or critical illness cover only, a rule-of-78-based calculation was a fair and appropriate refund basis.

¹¹⁴Citizens Advice response to the Remedies Notice, p13.

proportional to the period of the insurance policy remaining and as a result cancelling early appeared to be poor value for consumers.

298. We considered whether requiring pro-rata rebates would be sufficient to remedy the switching barrier we identified.
299. We noted first that, in addition to switching costs associated with low rebates, customers may also face switching costs arising from administration charges. We considered that we would be able to address this aspect of switching costs directly—and avoid circumvention of a remedy aimed at increasing rebates—by prohibiting such administration charges. We also took the view that giving customers the choice of obtaining the rebate in cash or reducing the balance on the loan would maximize customers' opportunity to switch under pro-rata rebates.¹¹⁵
300. In light of the submissions that we received, we then revisited the work we did in our provisional findings on switching costs,¹¹⁶ to see the extent to which switching costs would remain if providers were required to offer pro-rata rebates. This further analysis is set out in Appendix 10. As in our provisional findings, we used two methods to estimate switching costs:
- (a) calculating the cost to customers of changing to a regular-premium policy with the same policy conditions; and
 - (b) calculating the cost to customers of changing to another single-premium policy with the same policy conditions.

¹¹⁵Parties were divided as to how the rebate should be paid back to the customer under option 7(c). Cattles and some other credit providers, along with the OFT and the FSA, said that it should be up to the PPI provider to decide whether the rebate would be paid against the loan or given to the customer in cash. Aviva said that a direct payment to the customer would ensure that they would be able to continue with a policy that provided the same level of cover as their current PPI policy. Nationwide told us that it would give its customers the option as to whether the rebate was paid in cash or used to pay down the loan. Some parties told us that the rebate should be used to reduce the size of the outstanding loan. These providers said that customers would be better off if they repaid the debt. Barclays said that it was in the long-term interest of the customer for the rebate to be paid against the loan rather than in cash. Lloyds TSB said that it had given the customer a loan in the first place to pay for the insurance, hence the customer had not given it any money, so, when it came to a rebate, there was no question of it giving them any money back.

¹¹⁶See [Appendix 5.2](#) of our provisional findings.

301. We looked first at the cost of switching to a regular-premium policy. We found that, for a typical example of a prime personal loan with PPI, an obligation on providers to offer pro-rata rebates would reduce switching costs to about one-eighth of their current level.
302. This analysis implied that even with a pro-rata rebate on the PPI premium and supporting measures—a prohibition on administration charges and giving customers the choice of how to receive the rebate—material switching costs would remain. These costs are associated with the interest payable on the single premium. Single-premium policies are usually funded by a loan from the credit provider, which pays for the premium up front. The Consumer Credit (Early Settlement) Regulations 2004 sets out the rules governing the minimum rebates payable for loans that settle early.¹¹⁷ These regulations are underpinned by the principle that customers should be rebated the interest remaining on the loan at the point of early settlement. For fixed-term loans, this produces a declining rebate profile, similar in shape to the rule of 78. So a customer who decided to terminate a single-premium policy early would receive a rebate on the interest of the loan that was not calculated on a pro-rata basis.
303. We therefore considered the impact on switching costs of the interest rate charged on the single premium. We found that this made a substantial difference to the switching costs that remained with pro-rata rebates, both in absolute terms and, as when compared with the current level of switching costs, absent the remedy. Table 2 shows the magnitude of the costs of switching to an equivalent regular-premium policy with pro-rata rebates, in relation to the example set out in Appendix 10. Table

¹¹⁷From 2010 early settlement rebates on credit products will be regulated under the Consumer Credit Directive, which will apply similar principles.

3 shows what proportion of the current costs of switching to an equivalent regular-premium policy this represents.

TABLE 2 **Magnitude of switching costs remaining under option 7(c)***

APR	5%	10%	20%	30%	40%	50%	60%
Percentage of switching costs if policy terminates after:							
12 months	£15	£29	£54	£77	£96	£114	£129
18 months	£17	£33	£63	£90	£115	£137	£157
24 months	£15	£30	£58	£84	£108	£130	£151

Source: CC.

*Based on example set out in Appendix 10. Estimates relate to a 36-month £5,000 loan with a single insurance premium of £800 on which interest is charged at various APRs, terminating after 12, 18 and 24 months.

TABLE 3 **Proportion of switching costs remaining under option 7(c)**

APR	5%	10%	20%	30%	40%	50%	60%
Proportion of switching costs without remedy, if policy terminates after:							
12 months	7%	13%	21%	28%	32%	36%	39%
18 months	7%	13%	22%	29%	34%	38%	41%
24 months	7%	13%	22%	29%	35%	39%	43%

Source: CC.

*Based on example set out in Appendix 10. Estimates relate to a 36-month £5,000 loan with a single insurance premium of £800 on which interest is charged at various APRs, terminating after 12, 18 and 24 months.

304. Given our terms of reference and the nature of our AEC findings, we do not have the powers to address the interest element of switching costs, as it relates to the rebate on credit rather than on PPI. We noted also that it would be possible for distributors to charge higher APRs on the loan to fund the single premium than they charge on the underlying loan. This would increase the scale of the switching cost, relative to calculations based on the APR on the insured loan. Again, we do not consider that we would have the powers to prevent distributors from doing this.

305. We concluded from this analysis that pro-rata rebates would remove many but not all of the costs of switching to an equivalent regular-premium policy and that the remaining costs could be material, particularly where a high APR was charged on the loan funding the single premium.

306. When we looked at the costs of switching to another single-premium policy we found that, under the rebate systems in place at the time of writing, there would be significant financial disincentives were a customer to switch to another single-premium policy to cover their remaining payments. When we calculated the switching cost using a pro-rata rebate on the PPI premium, the costs associated with the interest payable on the single premium, referred to in paragraph 302, were overcome by other factors. In particular, the rates at which PPI premiums are charged for single-premium policies are lower the shorter the term of the single-premium policy.¹¹⁸ This could give customers an incentive to switch to shorter-term single-premium PPI policies order to take advantage of lower premium rates. Our analysis shows that given the current structure of single-premium charging schedules, this incentive would outweigh the costs associated with the interest payable on the single premium outlined in paragraph 302, in most cases.
307. Our analysis of switching costs showed that a pro-rata rebate was insufficient to buy an equivalent regular-premium PPI policy but, in the absence of administrative charges, was usually sufficient to buy an equivalent single-premium policy for the remainder of the loan.
308. We considered whether it was necessary to remove all of the costs of switching to a regular-premium policy, in order to remedy the switching barrier we identified, or whether a measure that removed the costs of switching to a single-premium policy—and many of the costs of switching to a regular-premium policy—would be sufficient. We noted that the remaining costs of switching to a regular-premium policy would not necessarily deter particular customers from switching to a regular-premium policy in practice. Customers could still have an incentive to switch to a regular-premium policy if, for example, it were offered to customers at a lower price, either because it

¹¹⁸This is illustrated in Tables 4 and 5 of Appendix 10.

cost less to produce or because the provider sought a lower profit margin. However, we consider that more competition would be prompted if all switching costs were removed and that there is a risk that the remaining switching cost associated with the interest on the PPI premium would act as a disincentive for at least some customers, reducing the effectiveness of this remedy option.

309. We also noted that some customers may wish to switch on the 'bundle' of credit with PPI, rather than on a stand-alone basis, and that our analysis indicated that with pro-rata rebates, the costs of terminating the PPI early would not act as a disincentive to this type of switching. In our view, for switching to drive competition, it is important to remove barriers to switching both on the 'bundle' of credit with PPI and on a stand-alone basis. In this context, we noted that customers can face barriers to switching the 'bundle', that are associated with the credit rather than the PPI. Customers may not be able to obtain credit or may face higher APRs on the credit if, for example, they are borrowing a smaller amount or if interest rates have risen. In a worsening economic climate, customers may find it hard to obtain credit from a new provider than when they took out the initial loan (for example, if the customer is at the higher end of the risk spectrum and credit cut-off scores have risen). In these circumstances, switching to a stand-alone PPI provider may represent the customer's only or best opportunity for obtaining better-value PPI. Stand-alone PPI is only offered on a regular-premium basis and we have not heard evidence that any parties would intend to offer stand-alone PPI on a single-premium basis.
310. We concluded that a remedy which did not remove all costs of switching to regular-premium PPI would not fully address the barrier to switching associated with single-premium PPI.

311. As well as looking at the impact on the financial disincentive to switch, we also considered whether there was likely to be any difference between a ban on single premiums and pro-rata rebates in terms of likely customer awareness of their ability to switch providers at low cost. Defaqto told us that a move to regular premiums would mean that cancellation terms would be more explicit, as well as less onerous, from the consumer viewpoint.
312. With a regular-premium policy, in the absence of an explicit charge for cancellation, it would be clear to customers that they could switch without incurring a financial cost. Policies paid for on an annual basis would be familiar to consumers from other contexts, and could also remove barriers to switching if monthly repayments were permitted and customers were rebated pro-rata if they terminated early in the year. In contrast, with pro-rata rebates on a single PPI premium, it would not always be the case that customers could switch costlessly and, even if it were, customers would require a high degree of financial sophistication to be confident that this was so. To give an example of the level of sophistication required, the sum that customers would receive on termination of a single-premium PPI policy would be a combination of the rebate on the PPI, and the interest that had not been incurred on the loan funding the PPI premium, each of which would be calculated on a different basis. We concluded that the relative simplicity for consumers (in terms of understanding the cost and therefore the benefit) of terminating a regular-premium policy would further enhance the effectiveness of a prohibition on single premiums compared with requiring an increased rebate.
313. We also noted that the current structure of single-premium PPI pricing may not be sustainable in the context of pro-rata rebates, or the other changes to the market envisaged in our remedies package. Were customers to identify the switching incentives identified in paragraph 306, this could introduce incentives for customers

to switch to shorter-term single-premium PPI policies simply to realize these benefits. If this was the case, then distributors might need to flatten their price structure in the face of the churn that these incentives might generate. If this were the case, then the residual switching costs identified in paragraph 302 could reappear in relation to switching to single-premium as well as to regular-premium PPI.

314. We concluded that banning of single-premium policies would be an effective remedy to the switching barrier identified. We do not consider that either of the other options that we considered would be fully effective in addressing this aspect of the AEC. Offering a choice of products at the point of sale would not be effective at all. Pro-rata rebates would be partially effective in addressing the switching barrier we identified; however, we had two concerns about whether it would be sufficiently effective:
- (a) It would remove some, but not all, of the financial costs of switching to a regular-premium policy. We also noted that those features of the current structure of PPI pricing that may provide an incentive to switch to shorter-term single-premium policies may not be sustainable in the context of pro-rata rebates.
 - (b) It was likely to require a greater deal of financial sophistication on the part of consumers to switch with confidence, and we were not satisfied that all consumers possess the required level of financial sophistication.

- *Effectiveness in removing barriers to searching*

315. It was also put to us that a ban on single premiums could help remedy other aspects of the AEC that we provisionally found, in particular customers' ability to search the market for the best value. Defaqto told us that a changeover to regular premiums would enable customers to shop around much more easily.

316. The discussion in paragraphs 287 to 314 has considered this option, and options 7(b) and 7(c), primarily as a means of addressing the switching costs associated with

single premiums. In our provisional findings, we also found that those customers who did want to compare products were hindered by product complexity, and that the variations in pricing structures were one aspect of this. We therefore considered whether a ban on single premiums would help address barriers to search, either on its own or in combination with other measures.

317. While we noted the importance of product complexity and variations in pricing structures in our provisional findings,¹¹⁹ we did not focus at length on the pricing of single-premium PPI as a specific factor in generating this complexity. We did note that the single premium is calculated from using an insurance premium and the APR on the loan that funds the premium, and that different providers calculate this in different ways.¹²⁰ This meant that it was difficult for a customer to make a comparison between single-premium PPI policies without obtaining a specific quote from both providers.
318. Our appreciation of this issue has developed further during the remedies phase for three reasons.
319. First, our discussions with the parties have highlighted the extent of complexity of the pricing of single-premium PPI. For example, [X] told us, in the context of a discussion about price caps, that it priced its personal loans with PPI broadly on the following factors: [X].
320. Each of these factors, if multiplied together, gives rise to a large number of price permutations and, therefore, possible price points. While [X] does not use all of the 1,120 possible pricing points, this example shows the complexity of PLPPI pricing. Providers of regular-premium PPI may also offer PPI at different prices, but such

¹¹⁹See paragraph 5.34.

¹²⁰See paragraphs 18 to 30 of [Appendix 2.1](#) of our provisional findings.

variation is normally determined either by differences in the level of cover offered (for example, whether a PPI policy is LASU, ASU, AS or U) or, less frequently, differences in the risk posed by the customer.

321. Second, our consideration of how a ‘common currency’ might be developed in the context of option 1 (see paragraphs 176 and 177) to enable customers to use advertisements to compare the price of PPI between competing providers illustrated that there was no simple way of expressing the price of single-premium products that would be relevant to the majority of customers. As an example, by using the Loan Calculator on its website, we calculated the total monthly cost of PLPPI as a £ per £100 of monthly benefit and the total monthly cost of credit with PPI as a combined APR for NatWest. The results are shown in Tables 4 and 5.

TABLE 4 Monthly cost of PPI as £ per £100 of monthly benefit

Amount borrowed (£)	2,000	5,000
<i>Term (years)</i>		
1	9.67	9.34
2	12.92	12.19
3	16.07	14.80
4	20.83	18.83
5	25.90	23.06

Source: CC analysis of company website.

TABLE 5 Cost of personal loan with PPI expressed as a combined APR

Amount borrowed (£)	2,000	5,000
	<i>per cent</i>	
<i>Term (years)</i>		
1 yr	46.5	35.5
2 yrs	39.1	28.3
3 yrs	37.0	25.9
4 yrs	38.0	26.1
5 yrs	39.7	26.8

Note: Credit APR 20.4 12.4

Source: CC analysis of company website.

322. These examples show that, even with a policy offering identical cover, the price of PLPPI from a provider can vary substantially even for an individual customer, depending on the term of the loan and the APR. All other metrics that we considered

exhibited a similar degree of variation, when applied to single-premium policies or bundles of credit with single-premium PPI, and we would expect to observe a similar degree of variation for other providers of single-premium PPI. We were unable to find any simple metric which allowed customers easily to compare the cost of single-premium PPI products in a consistent way. The price of a regular-premium policy, by contrast, does not vary according to these factors.

323. Third, these considerations have highlighted the difficulty that customers currently face in making quick comparison between the cost of a single-premium policy and a regular-premium policy offered on a stand-alone basis (we are not aware of any stand-alone PPI sold on a single-premium basis).

324. We therefore concluded that, in addition to removing the switching costs associated with single-premium PPI, a ban on single premiums would also contribute to addressing the barriers to search arising from product complexity and variations in pricing structures. We concluded that this was also a relevant consideration in assessing the effectiveness of this option (and its effectiveness relative to alternatives, such as pro-rata rebates) as part of our remedy package.

- *Whether a ban would result in consumer detriment*

325. Some providers told us that a ban on single premiums would result in significant customer detriment. We considered the main arguments in paragraphs 45 to 65, in which we concluded that single premiums did not result in any relevant customer benefits.

326. Some providers also told us that a prohibition on single-premium PPI would result in a reduction in choice for customers. We accepted that a prohibition on single premiums would remove products with a particular pricing structure from the market

and that this involved some reduction in customer choice. We are not aware of any customers currently being offered a choice between single- and regular-premium PPI at the point of sale,¹²¹ despite the FSA's views on the limited number of people for whom single-premium policies are appropriate (see paragraph 328), and we noted that there was some evidence of customer confusion about the distinction between single- and regular-premium policies (see paragraph 352). We concluded that the benefits to customers arising from the lower switching and search costs would outweigh any detriment from this reduction in choice.

327. The ABI said that the price of regular premiums rose by 40 per cent when single-premium policies were banned in South Africa. South Africa introduced the National Credit Act 2005, which requires PPI to be optional¹²² and for the insurance premiums to be payable on a monthly basis (or on a monthly or annual basis in the case of large agreements).¹²³ The National Credit Act also requires the credit provider to give the customer the opportunity to take insurance from a provider other than the credit provider, and to disclose the cost of the PPI to the customer.¹²⁴ The South African National Credit Regulator¹²⁵ told us that the National Credit Act had only come into force very recently, but the early signs were encouraging; banks were still offering PPI and appeared to be competing on price. There also seemed to be more advertising of PPI. We therefore did not consider that, based on the limited evidence available, the South African experience indicated that the price of PPI policies would rise as a result of a ban on single-premium policies.

328. We also sought the views of regulators and customer organizations on this matter. The FSA said that single-premium policies were appropriate only for a minority of

¹²¹We are aware of one experiment, conducted by [§], where customers were offered a choice of single- or regular-premium policies (see paragraph 352).

¹²²Section 106(3).

¹²³Section 106(4).

¹²⁴Section 106(5).

¹²⁵www.ncr.org.za.

consumers: it estimated a maximum of 8 per cent of the population.¹²⁶ In light of this, the FSA told us that there was little risk of customer detriment from a ban on single-premium PPI policies.

329. Which? told us that it could not see any benefits to consumers provided by single-premium policies. In its view, prohibiting single premiums would cause no harm to consumers. Citizens Advice told us that, though it could not disprove that single-premium policies benefited customers, it was not convinced by the arguments.
330. We also noted that [§] is reviewing its use of single-premium policies, in the light of changes to the commercial and regulatory environment, including, among other matters, changing penetration rates and loan volumes, and that HSBC currently offers a regular-premium product (LifeChoices) rather than a single-premium PPI policy (though LifeChoices was originally designed to replace HSBC's mortgage product).¹²⁷
331. Based on our analysis of relevant customer benefits, and the submissions from the parties and others, we concluded that a ban on single premiums would not cause any significant harm to customers.

Provisional decision on implementation of remedy

332. We concluded that a ban on single-premium policies would address the barriers to switching associated with single-premium policies, and was the only option which would do so effectively. We also found that such a ban would reduce barriers to

¹²⁶FSA letter, 15 August 2008, based on the thematic work that the FSA has done this summer into PPI. The FSA told us that this estimate was 'likely to be a very generous, top-end, estimate of the proportion of the population who might find a single premium PPI product is suitable for their needs. In practice, we believe this figure is likely to be much lower, perhaps as little as a couple of percent'.

¹²⁷See [Appendix 2.3](#) of our provisional findings.

search associated with product complexity and variations in pricing structure. We concluded that we should implement this option as part of our remedy package.

333. We propose to implement the remedy proposal as set out below. These measures aim to ensure the remedy's effectiveness in addressing barriers to switching and search, which prevent, restrict and distort competition.

FIGURE 8

Remedy proposal for a prohibition on single premiums

No distributor can charge for PPI on a single-premium basis. The only charge that can be levied on a PPI policy is a regular premium charged at a constant rate, paid monthly or annually. If an annual premium is charged, then a rebate must be paid to customers on a pro-rata basis, if the customer terminates the policy during the year.
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334. We consider that the option outlined above would fully address the switching barrier caused by single-premium policies which we provisionally found would contribute to addressing barriers to search, arising from the product complexity and the variety in pricing structures.
335. We considered whether other measures would be effective. In particular, we found that a requirement to offer pro-rata early settlement rebates, as outlined in option 7(c), would be partially effective in addressing the switching barrier that we found. However, we had three concerns about this remedy option which led us to conclude that it would not be sufficiently effective:
- (a) It would remove some, but not all, of the financial costs of switching to a regular-premium policy. In particular, a switching cost associated with the rebate on the interest on the single premium would remain. We noted that those features of the current structure of PPI pricing that may provide an incentive to switch to shorter-term single-premium policies may not be sustainable in the context of pro-rata rebates.

(b) It is likely to require a greater deal of financial sophistication on the part of consumers to switch with confidence than a move to regular-premium PPI, and we were not satisfied that enough consumers possess the required level of financial sophistication.

(c) It would not contribute to addressing the barriers to search arising from product complexity and variations in pricing structures. This would make it harder to develop a 'common currency' for disclosing the price of PPI on a comparable basis, inhibiting the effectiveness of other remedies, notably options 1 and 4.

336. Given that it is more effective in addressing the switching costs associated with single premiums than any alternative, and the contribution it makes to addressing barriers to search, we consider that it is proportionate to include this remedy in the remedy package.

337. A ban on single-premium PPI would have the greatest impact and be most effective if customers take account of the greater opportunities to switch PLPPI and SMPPI and of the reduced barriers to search both before and after the credit point of sale. This measure therefore complements all the other options in our proposed package of remedies.

338. We consider that if we took this remedy forward, it could be implemented within a year of any CC Order and could be monitored by the OFT (supported by suitably comprehensive compliance reporting requirements on the parties).

Implications of remedies package for providers of stand-alone PPI and short-term IP

339. The remedies package we are proposing to take forward will be most effective if providers of stand-alone PPI¹²⁸ and short-term IP are bound by some of the same requirements as distributors of credit and PPI. We set out here the requirements on providers of stand-alone PPI and short-term IP.
340. With regard to option 1, providers of stand-alone PPI and short-term IP are required to provide the all of the following information in direct marketing materials about their products but only (a) and (c) in regard to their non-direct marketing materials:
- (a) the cost of PPI per £100 of monthly benefit (if the benefit pays out for less than 12 months, notice of this fact must also be clearly disclosed to customers alongside the cost of the policy);
 - (b) that PPI is available from other firms (without specifying those other firms); and
 - (c) that information on PPI and short-term IP, alternative providers and other forms of protection products can be found on the FSA's moneymadeclear website.
341. Requiring the provision of this information will ensure that consumers can compare effectively stand-alone PPI and short-term IP policies with PPI policies offered by distributors, minimizing search costs for consumers.
342. Providers of stand-alone PPI and short-term IP are required to implement remedy option 3 in full. This will minimize search costs for consumers, providing one source of web-based information on which consumers can compare all relevant policies.
343. With regard to option 4, in order to for the ban on sale of PPI at the credit point of sale to be most effective, providers of stand-alone PPI and short-term IP are required:

¹²⁸As set out in paragraph 2.52 of our [provisional findings](#), providers of stand-alone PPI includes distributors which offer PPI to insure repayments on credit supplied by other distributors.

- (a) to provide a personal PPI quote to the customer in a durable medium (see Appendix 8 for details) if the consumer asks the provider about the cost and/or features of a stand-alone PPI and short-term IP policy sold by that provider; and
- (b) not to charge more for stand-alone PPI and short-term IP than the cost of the regular or annual premium. For example, there can be no administration fees, set-up fees or early termination fees.

344. The requirement to provide a personal PPI quote will enable consumers easily to compare the offers of different providers. The prohibition on charging more than the regular or annual premium will ensure that consumers are comparing like with like (with no hidden costs) when making their comparisons.
345. Providers of stand-alone PPI and short-term IP are required to implement remedy options 6 and 7(a) in full. The provision of the annual statement will ensure that customers of stand-alone PPI and short-term IP providers have, on a regular basis, the information required to facilitate switching.
346. Whilst there are no current providers of stand-alone PPI and short-term IP policies offering them on a single-premium basis, for the reasons set out in paragraphs 287 to 338 they should be covered by a prohibition from starting to offer such policies.

Options we are not proposing to take forward

347. There are a number of options that were in the Notice or were suggested to us during the remedies process which we are not proposing to take forward. The reasons for these decisions are set out below (except for alternatives to option 4, which are discussed in paragraphs 247 to 249).

Option 2: Further standardization of PPI information given to the customer at the point of sale

348. Parties were generally in favour of option 2 and considered that it would make the comparison of different providers' products and prices easier for customers. For example, Capital One was supportive of increased standardized disclosure for PPI products as it considered that it would reduce the risk of providers/distributors misinterpreting principle-based regulation and would improve comparability for consumers. It was put to us that the message that PPI could be bought from other parties was particularly important. However, a number of parties did not consider that additional information at the point of sale would address the AEC that we provisionally found. The FSA said that it was unclear what additional benefits more cost information would provide and that it did not think that further standardization of documents would create significant additional benefits within the current market structure. Other parties¹²⁹ considered that the remedy might just add cost and more paperwork, which could confuse customers and reduce innovation.

349. We are not proposing to take option 2 further. However, we have included elements of option 2 into the point-of-sale ban (option 4). We agree with the FSA that solely providing more information at the point of sale is unlikely to be effective at addressing the AEC in the current market structure as it will take time and more fundamental change to the operation of the market to impact customer and supplier behaviour to a sufficient degree. However, we conclude that a point-of-sale ban, as part of our overall remedy package, will be more effective with the addition of standardized information at the credit sale (see paragraph 259).

¹²⁹See, for example, AFB response to the Remedies Notice, p4.

Option 5: All policies to be renewed annually

350. Parties¹³⁰ told us that option 5 (annually renewed PPI policies with a requirement for customers to opt in each year) would result in customers not being covered when they thought they were. Parties¹³¹ told us that many customers would ignore the renewal statements and would continue to think they were covered when they were not. They said that most insurance products were sold on an opt-out basis. Some parties¹³² interpreted the option as requiring that PPI policies be sold with annual premiums. They told us that such a remedy would be expensive to introduce as the parties would have to follow up with customers once a year and having an annual policy would require a change in the policy terms and in the distributors' systems. Furthermore, some parties suggested that the move to annual products would mean that continuing customers would have exclusion periods each year. Others, however, disagreed with this assertion. Parties also said that customers were currently able to cancel and switch a regular-premium policy at any time and if the remedy moved firms from regular to annual policies the remedy could decrease rather than increase these customers' ability to switch.

351. We are not proposing to implement option 5. We agreed with the arguments that an annual opt-in to a policy could cause some accidental lapsing, though we thought that distributors would minimize this risk through reminders. In this context we noted that an opt-in system is used for other types of insurance¹³³ and that insurance companies using an opt-in must follow up with customers to be compliant with FSA rules. However, as we thought that an annual statement together with increased advertising and the information provided at the point-of-sale ban, as set out in paragraph 372, would be effective in providing the information and impetus to

¹³⁰See, for example, a large underwriter's response to the Remedies Notice, p7, and MBNA response to the Remedies Notice, paragraph 4.25.

¹³¹See, for example, ABI response to the Remedies Notice, p8, and HSBC response to the Remedies Notice, paragraph 6.7.1.

¹³²See, for example, Barclays response to the Remedies Notice, p20, and MBNA response to the Remedies Notice, paragraph 4.26.

¹³³The FSA said that it was the commercial decision of the firm as to whether it had an opt-in or opt-out regime.

encourage consumers to consider whether their existing policy was still right for them or whether they should switch, we did not consider it necessary to impose this remedy, which we considered would be more onerous on parties.

Option 7(b): Requiring distributors of single-premium policies to offer a regular-premium policy with an identical level of cover as the single-premium policy they offered

352. Parties were divided regarding option 7(b). Some parties¹³⁴ considered that it would provide customers with additional choice, while others considered that it would lead to some firms exiting the PPI market. Some parties¹³⁵ put it to us that if the two products were offered the sale would have to become an advised sale,¹³⁶ which could reduce the number of firms that offered PPI and increase costs for those currently selling on a non-advised basis. Other parties told us that selling both products could lead to customer confusion and that the salesperson's advice would be key in any customer decision. One party ([X]) provided evidence of a pilot in 2006 where it sold both single- and regular-premium policies in some of its branches. The report noted that wide-scale confusion existed; the pilot suggested that customers did not understand the difference between single and regular policies. A number of parties considered that it would be very difficult to offer equivalent single- and regular-premium policies given the differences between them. Finally, Cattles said that if we required all companies offering single-premium policies to offer regular-premium policies as well, we should similarly require companies selling regular-premium policies to offer equivalent single-premium policies.

353. We are not proposing to implement option 7(b). We noted the evidence relating to customer confusion about single- and regular-premium policies. We thought that many customers were likely to seek the advice of a salesperson on which was the

¹³⁴See, for example, Assurant response to the Remedies Notice, p4, and Genworth response to the Remedies Notice, paragraph 2.29.

¹³⁵See, for example, Abbey response to the Remedies Notice, paragraph 5.3.3, HSBC response to the Remedies Notice, p14.

¹³⁶An advised sale is a sale by an adviser or intermediary who makes a personal recommendation to the customer.

more suitable product in these circumstances, and thought that the incentives on a salesperson as to which product to recommend (if the salesperson was authorized to provide advice) would be complex, and it would be impractical to monitor and enforce without a significant amount of resource. We were not convinced that selling single- and regular-premium policies alongside each other could only be achieved through an advised sales route, and we did not consider it logical that companies currently selling regular-premium policies should be required to introduce a single-premium policy, given that the issue at stake is problems associated with single-premium policies. We were therefore not convinced that option 7(b) would adequately remedy the switching barrier associated with single-premium policies.

Option 8: Minimum standards for elements of PPI policies that act as a barrier to switching (initial exclusion periods and pre-existing conditions qualification periods)

354. Parties in favour of minimum standards for exclusion and pre-existing conditions qualification periods (option 8) considered that they would improve ‘peace of mind’ for customers as they would be sure that their needs were covered from the moment they switched. Some parties¹³⁷ said that there would be cost implications—and maybe even firm exits from PPI—resulting from a move to individual underwriting or from a greater degree of adverse selection. The adverse selection issues were considered to be particularly severe for stand-alone providers who rely on the exclusions to protect themselves. A few parties¹³⁸ suggested that a better option would be for PPI providers to offer to remove or lessen exclusion and pre-existing conditions for switching customers when those customers switched to an equivalent or lower-specified PPI policy.

355. We were told¹³⁹ that minimum standards, in general, would make comparison between products easier. A few parties¹⁴⁰ referred us to the minimum standards for

¹³⁷ See, for example, ABI response to the Remedies Notice, p13, and HSBC response to the Remedies Notice, p14.

¹³⁸ See AXA response to the Remedies Notice, paragraph 64, and Cassidy Davis response to the Remedies Notice, p6.

¹³⁹ See Claim 2 Gain response to the Remedies Notice, p3.

MPPI,¹⁴¹ which they believed was generally considered to be beneficial. By contrast, other parties¹⁴² said that any minimum standards would or could lead to less product differentiation and maybe less switching as a result, and that minimum standards would limit innovation. Other parties¹⁴³ suggested that standard terminology would be beneficial.

356. We are not proposing to implement option 8. We do not think it is necessary to address the AEC that we have provisionally found. We considered that the effect of this option of product innovation would be minimal. However, we did not think that having minimum standards for exclusion and pre-existing conditions qualification periods would be necessary in a market where suppliers actively compete for switching customers. We thought that if the conditions to encourage competition among suppliers for switching customers existed, then suppliers would themselves waive or lower qualification periods in order to win customers. We believe that implementation of our proposed remedies package would encourage consumers to consider switching provider more actively and that this would in turn encourage suppliers to be more active in seeking switching customers. On this basis we do not think it necessary to pursue the introduction of minimum standards on terms which might discourage switching between policies.

Option 9: Obligation to share information about customer claims

357. Most parties were against the obligation to share information about customer claims (option 9). In general, parties¹⁴⁴ considered that setting up a database to share claims information would be costly compared with other methods of proving that

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¹⁴⁰See, for example, Aviva response to the Remedies Notice, p25, and Coventry Building Society response to the Remedies Notice, p9.

¹⁴¹Annex A of MPPI: Response by the Council of Mortgage Lenders to the OFT Report on the Payment Protection Insurance Market Study, 2006.

¹⁴²See, for example, Barclays response to the Remedies Notice, p31, and Openwork response to the Remedies Notice, p2 (regarding MPPI).

¹⁴³See Barclays response to the Remedies Notice, p31, and Defaqto response to the Remedies Notice, p14.

¹⁴⁴See, for example, FLA response to the Remedies Notice, p31 and HSBC response to the Remedies Notice, paragraph 6.7.5.

customers had not claimed and that in any event past claims were not an indication of future claims.¹⁴⁵ For example, AXA said that currently no proof or statement that the insured had not made claims was required. The ABI¹⁴⁶ highlighted the issue that customers who claimed might find it more difficult to switch—or might consider that it would be harder to switch. Some parties¹⁴⁷ were concerned that such a database would be difficult to set up given the sensitivity of the data and the Data Protection Act.¹⁴⁸ A few parties said that the option could reduce adverse selection issues for stand-alone providers and we also noted that Cardif Pinnacle currently advertises that it will cover customers, and beat their current premiums, as long as those customers have no claims. Some parties (Cardif, Barclays, PaymentShield and MBNA) suggested that claims information could be added to the annual statement and could be provided to a customer on request.

358. We are not proposing to implement option 9. We consider that claims data may be important information for firms trying to mitigate the risks of adverse selection. However, given that there are other, cheaper, mechanisms for sharing claims data, which are currently being used, and in particular that we have provisionally decided on the introduction of a claims history on an annual statement (see option 6, paragraphs 272 to 275), the creation of a new database would be superfluous.

Option 10: Obligation to share information about customers' credit card balance with a nominated underwriter

359. Nearly all parties, including all stand-alone providers, said that they would not be interested in credit card balance data. Only one party, [X], expressed any interest in

¹⁴⁵However, evidence from the parties was mixed on this point with [X] and [X] saying that they were predictive. [X] said that its MPPI customers (from 2002 to 2006) that claimed were three times more likely to claim again (7.2 per cent a year vs 2.4 per cent a year). [X] said that 'we may reject a null hypothesis of no difference in rate of a successful claim in favour of the alternative that there is an increase in the rate of successful claim amongst those policies claiming more than once', while Abbey, AXA and MBNA said that they were not.

¹⁴⁶See ABI response to the Remedies Notice, p14.

¹⁴⁷See, for example, ABI response to the Remedies Notice, p14, and Cassidy Davis response to the Remedies Notice, p6.

¹⁴⁸We were also told by one CRA (Experian) that the current cost of PPI may make it uneconomic for such a system to be set up.

gaining access to this data for the purposes of producing a more bespoke product. [X] also suggested an alternative remedy involving providing access to CRA data to enable providers to offer multi-product PPI policies (so, for example, a PPI provider could use CRA information to provide a tailored PPI product to cover a customer's credit card and mortgage). The stand-alone providers (Paymentsshield and the Post Office) said that they would prefer to offer an income protection product which covered the aggregate credit card repayments, and as a result some said that the average annual balance and minimum repayment amount would be useful, while one said that customers were aware of their average outstanding balance and did not require the information. Parties¹⁴⁹ said that option 10 would be difficult and costly to set up, would expose customers to a greater risk of fraud and would put the company that collected the data in a very strong position. APACS said that there were a number of issues which would need to be addressed, including: the governance rules; user validation; liability for errors; agreement of messaging standards; recovery of costs; and how disputed transactions would be treated. The CRAs ([X] and [X]) said that the option would be costly, that the data they currently held on credit cards could not be used for this purpose under the principles of reciprocity¹⁵⁰ and that they did not currently hold full data on all credit card accounts.¹⁵¹

360. We thought that option 10 could, in theory, allow businesses to create more tailored products for stand-alone CCPPI. However, given the lack of interest in gaining access to this data, we were not convinced that in practice the information would be used in this way, and therefore we were not convinced that option 10 would be an effective remedy. We also assessed [X] additional suggestion. We thought that it

¹⁴⁹See, for example, Capital One response to the Remedies Notice, pp6&7, and MBNA response to the Remedies Notice, pp11&12.

¹⁵⁰The Principles of Reciprocity is an agreement between the subscribers and the holders of negative, positive and search data. The agreement regulates the access to data and the use to which subscribers can put data. The body that revises POR agreements is the Steering Committee on Reciprocity (SCOR). SCOR is made up of a number of trade associations as well as CRAs (Equifax, Experian and Callcredit). Recent joiners include the Consumer Credit Association and the Credit Services Association.

¹⁵¹[X] said that it had 60 million accounts but estimated that there were at least 5 million which still needed to be added.

would be equally difficult and costly to set up. Moreover, as CRA data cannot be used in this way currently under the principles of reciprocity, it would require both industry and CRA agreement which would make the implementation of the remedy uncertain. And, given the lack of enthusiasm for creating tailored CCPPI policies, we did not think there would be any greater enthusiasm for [redacted] proposal. We are, however, proposing to add average balance and minimum repayment data to the annual statement (option 6), as this was considered to be useful for assessing the level of cover a customer would need.

Option 11: Price caps

361. Three parties (Citizens Advice, the Post Office and [redacted]) were in favour of price caps. All three said that the scale of the excess profits justified the imposition of a price cap. The Post Office said that there should be a temporary price cap to ensure that excessive pricing were removed. However, Citizens Advice favoured long-term price caps as part of its preferred package of remedies.
362. Other respondents did not agree with price caps. Their arguments fell into five main areas:
- (a) they would not address the competition issues that the CC had provisionally found;¹⁵²
 - (b) they were disproportionate and inappropriate, given the absence of a consumer detriment in the overall markets for PPI and the underlying credit products;¹⁵³
 - (c) they would have other negative effects on the market; for example, they would decrease innovation and reduce quality;¹⁵⁴
 - (d) they would lessen the effectiveness of other remedies; for example, they could increase the point-of-sale advantage, as customers could be discouraged from

¹⁵²See, for example, ABI submission covering letter, p2, and Aviva response to the Remedies Notice, p30.

¹⁵³See, for example, RBSG response to the Remedies Notice, p17.

¹⁵⁴See, for example, Barclays response to the Remedies Notice, p37, and Paymentsshield response to the Remedies Notice, p4.

shopping around as they would assume that they already had a good price;¹⁵⁵

and

(e) they would be complex to set up and difficult to enforce given the range of PPI policies in the market and the lack of any minimum standards.¹⁵⁶

363. We consider that that package of remedies proposed in this paper will deal with the AEC that we have provisionally identified (see paragraphs 8.2 and 8.3 of our [provisional findings](#)) in a timely manner. Because of this, we do not consider that we have to deal specifically with the customer detriment of higher prices arising from the AEC that we have provisionally found.¹⁵⁷ Although we believe that price caps could address the customer detriment of higher prices and have not been persuaded by the evidence that price caps would have negative impacts on competition, we are not proposing to take this option forward. We believe that by dealing with the AEC we will also deal with the customer detriment.

Implementation of remedies

How the remedies should be implemented

364. The CC can take remedial action in a number of ways. These are:

- (a) making an Order;¹⁵⁸
- (b) accepting undertakings to stop or to take particular action ‘from such persons as the CC considers appropriate’;¹⁵⁹ or
- (c) recommending the taking of action by others.¹⁶⁰

365. We consider that a CC Order relating to all relevant parties would be the most effective means of implementing those parts of our remedies package relating to

¹⁵⁵See, for example, ABI response to the Remedies Notice, p16, and Axa response to the Remedies Notice, paragraph 84.

¹⁵⁶See, for example, Abbey response to the Remedies Notice, paragraph 6.1.2, and Lloyds TSB response to the Remedies Notice, paragraph 7.3.

¹⁵⁷CC3, [paragraph 4.22](#).

¹⁵⁸[Section 161](#) Enterprise Act 2002.

¹⁵⁹[Section 159](#) Enterprise Act 2002.

¹⁶⁰[Section 134](#)(4)(b) Enterprise Act 2002.

businesses. The CC's guidance notes that a market investigation remedy will often be most effective if it imposed by Order rather than sought through undertakings, due to the likely number of parties involved.¹⁶¹ Given the large number of PPI distributors active in the UK, an Order is likely to be the most suitable means of addressing the AEC in this case.

366. We propose to make one recommendation to the FSA, that it use the information provided to it under option 3 to populate its PPI price comparison tables. The FSA has told us that it does not object to this proposal.

The timescale for implementation

367. Table 6 summarizes the responses from the parties regarding implementation timescales. The table suggests that all the remedies in the package could be implemented in between 6 and 12 months. We would welcome further representations regarding the time to implement this package of remedies and any impact that implementation time on had on overall cost, in the light of the further detail set out in this provisional decision.

TABLE 6 Estimates of time required to implement remedies

	<i>months</i>				
	<i>Option 1</i>	<i>Option 3</i>	<i>Option 4</i>	<i>Option 6</i>	<i>Option 7(a)</i>
[X]	12–24	3–6	12–24	6–12	12–24
[X]	3–6	3	18–24	6–9	18
[X]	-	2	2–9	6	-
[X]	6–12	0 if FSA only	6–12	12–18	-
[X]	2	4	11	9	10
[X]	3–4	4	12	3–9	6
[X]	9	3	9	6	-
<i>Range</i>					
High	24	6	24	18	12
Low	2	0	6	3	0

Source: CC analysis of data provided by the large distributors.

¹⁶¹ CC3, [paragraph 4.44](#).

368. We consider that options 1, 3 and 6 could be implemented by nearly all the parties within six months of any CC Order (see paragraphs 188, 208 and 286), while options 4 and 7 could be implemented within 12 months of a CC Order (see paragraphs 261 and 338). In addition, we note that the Government has indicated that it will aim to have two common commencement dates each year for new legislation and regulations. The dates are 6 April and 1 October.

Monitoring and enforcement

369. The ABI said that the FSA would be best placed to oversee the implementation and monitoring of remedies that impact on the sales process. MBNA said that it would prefer monitoring to be done through the existing channels where possible.

370. Once the remedies package is implemented, it will need to be monitored and enforced under the Act by the OFT.

371. We believe that the OFT's monitoring should be supported by suitably comprehensive reporting requirements. We propose that the package should include:

- (a) a requirement on all PPI providers to provide the OFT with quarterly compliance reports¹⁶² produced by an independent party (approved by the CC/OFT) and signed by a company director and a non-executive director. Such a report should include the information set out in Figure 5 (when relevant), any steps taken to ensure compliance, representative samples of advertising materials, sales scripts etc, details of any incidences of non-compliance and steps taken to rectify this, details of training of staff re compliance, details of their internal monitoring systems;

¹⁶²We propose that smaller distributors (ie with annual sales of PPI of less than £90 million based on GWP—see [Appendix 2.8](#) of our provisional findings) should only have to provide annual compliance reports.

- (b) a requirement on all PPI providers to appoint a compliance officer who has responsibility for monitoring compliance, facilitating provision of information to the OFT and acting as a point of contact at the firm if the OFT has any questions. Firms would have to notify the OFT of the identity of the compliance officer (and the OFT has the ability to require replacement if they are not performing their functions adequately);
- (c) a requirement on all originators of sales and marketing material for PPI to provide an annual report from an independent research agency establishing that wording used in sales and marketing materials is easy to understand—in particular, with regard to the additional advertisements required under option 1; and
- (d) a requirement that each large supplier (those with annual sales of PPI in terms of GWP are more than £90 million) commission an annual, independent mystery shopping exercise and report results to the OFT within a compliance report.

We note that these requirements may involve additional cost to the parties and seek views on this.

The proposed package of remedies: effectiveness and proportionality

372. Our analysis and provisional decisions on the proposals set out in the Notice and put to us subsequently give rise to a package of six remedies:

- (a) a prohibition on the sale of PPI by a distributor to a customer within 14 days of the distributor selling credit to that customer. Customers may proactively return to the distributor to initiate a purchase by telephone or online from 24 hours after the credit sale;
- (b) a requirement on all PPI providers to provide certain information and messages in PPI advertisements, and a requirement on distributors to advertise PLPPI and SMPPI in close proximity to their respective personal loan advertisements;
- (c) a requirement on all PPI providers to provide certain information on PPI policies to the FSA;

- (d) a recommendation to the FSA that it use the information provided under the requirement in (c) to populate its PPI price comparison tables;
- (e) a requirement on distributors to provide an annual statement for PPI customers; and
- (f) a prohibition on the selling of single-premium PPI policies.

The rationale for implementation of all elements of the remedy package

373. We considered whether we needed to implement all of these remedies in order to address the AEC and adverse effects provisionally identified.
374. Many parties said that they were in favour of remedies which improved transparency and encouraged shopping around (remedies 372(b), 372(c) and 372(d) of the package we are proposing to implement—see paragraph 372). Some of these parties made clear that, in their view, a package of remedies based around additional information provision to address search and switch issues would remedy the detriments we identified. However, it was not always clear that parties believed that the remedies they favoured would remedy the AEC we provisionally found (and with which they often disagreed). For example, Abbey said that it ‘did not consider it to be certain that there would be a significant change in consumer behaviour if consumers were given more information/opportunities to switch’.¹⁶³
375. The FSA told us that, whilst further information to enable consumers to search the market could bring some additional benefits, the incremental benefit would be limited, as it could not address the barriers to searching and switching we had identified.¹⁶⁴ Cardif Pinnacle told us that [X] it did not believe that informational remedies alone would have a material effect on the market, and consumer switching in particular.

¹⁶³In Abbey’s response to the Remedies Notice, paragraph 2.4.

¹⁶⁴FSA response to the Remedies Notice, p8.

376. We also noted that the recent evaluation of the Extended Warranty Order found that while the remedy package put in place following the CC's investigation—comprising information provision at the point of sale, a cooling-off period for 45 days and pro-rata rebates beyond that point—has had a net beneficial effect on customers, the Order has only resulted in a relatively small reduction in consumer detriment (of £18.6 million a year) compared with an estimated annual detriment of £366 million.¹⁶⁵
377. In our provisional findings we concluded that, in the current market structure, the focusing of marketing by distributors at the credit point of sale appeared to be the only effective way of marketing PPI.¹⁶⁶ We found, in paragraph 5.87 of our [provisional findings](#), that there are significant barriers to entry for stand-alone PPI providers seeking to sell PPI products without access to customers at the credit point of sale, due to adverse selection, poor consumer awareness and high marketing costs.¹⁶⁷ These factors would not be addressed by a package of information remedies.
378. The evidence led us to conclude that informational remedies (b) and (c) (along with recommendation (d)) would help remedy the AEC identified, but that these alone would not be sufficient to remedy the lack of competition we saw between PPI providers; we would also need to address the point-of-sale advantage.
379. It was put to us that, if we adopted remedies designed to incentivize distributors to price credit and PPI combinations more efficiently, that would be likely to result in cost savings associated with selling PPI at the point of sale being passed on, at least in substantial part, to consumers (see paragraph **Error! Reference source not found.**). However, if there were efficiencies to pass on to consumers, they would

¹⁶⁵ *Evaluating the impact of the Supply of Extended Warranties on Domestic Electrical Goods Order 2005*, prepared for the OFT by LECG, October 2005.

¹⁶⁶ [Provisional findings](#), paragraph 51.

¹⁶⁷ [Provisional findings](#), paragraph 5.87.

only be passed on if competitive markets could be achieved without a point-of-sale ban. As set out in paragraph 249, we concluded that we could not address the point-of-sale advantage by providing information alone at the point of sale. Further, as set out in paragraphs 247 and 248, we did not find an effective way of addressing the point-of-sale advantage without introducing a prohibition on a distributor selling PPI within a certain time period of the sale of the underlying credit product, whilst allowing consumers proactively to return to the distributor to purchase its PPI. We concluded therefore that it was necessary to include remedy 372(a) in the remedy package.

380. Having determined the remedies necessary to address customer search and the impact of the point-of-sale advantage, we considered whether we needed any further remedies to address switching barriers. The provision of an annual statement (remedy 372(e)) is needed to help consumers to focus periodically on their PPI policy and whether it still represents the best value PPI policy on offer. The remedies to enhance search will help potential switching customers to identify policies which might represent best value for them.
381. However, the annual statement would not be sufficient to reduce the switching barriers associated with single premiums. As set out in paragraph 314, a prohibition on the sale of single-premium policies (remedy 372(f)) would be the only effective way of removing this switching barrier, as well as helping to address barriers to search.
382. We concluded, therefore, that it was necessary to implement all the elements of the remedies package,

Benefits and synergies of the remedies package

383. These remedies will encourage customers to search by removing many of the barriers to searching that we identified in our provisional findings report. In particular, this remedy package 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. In addition, the package will decrease the point-of-sale advantage and as a result will provide more opportunities for stand-alone providers to compete for PPI customers. By prohibiting single-premium PPI, the package will also remove the most significant switching cost, an important source of product complexity and variety in pricing structures and the largest impediment to having a simple measure for price comparison. We consider that 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 provisionally found and resulting consumer detriment.
384. Additionally, we believe that our proposed remedies interact positively with one another to enhance the overall effectiveness of the remedy package. Each element of the package, when considered separately, contributes to addressing the AEC. Taken together they will have a greater effect in increasing competition than if they were implemented individually. For example, we consider that requiring a similar format for price quotes and annual statements will increase the impact of both. Similarly, prohibiting single premiums will make the provision of additional information in advertisements and the point-of-sale ban more effective, as customers will be able to use a single price metric to compare PPI policies across different providers (including stand-alone providers) both before and after the credit point of sale.

Extent of customer detriment

385. It is not possible to evaluate the full extent of the consumer detriment that we aim to address through our remedies package. First, there is a large category of ‘dynamic’ benefits to consumers that we would expect to arise from increased competition in the provision of PPI. Such benefits will arise, for example, from 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). Indeed, we would expect greater competition to bring about 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. Given the considerable size of the PPI sector even at the current high prices, we would expect these dynamic benefits of competition to be on a very large scale, but we have not been able to put a value upon them.

386. Further, there are ‘static’ welfare implications of the current high PPI prices—in-
efficiencies 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). We used the Excel model set out in Appendix 5 to estimate the potential scale of these static effects on consumers. 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 PLPPI, MPPI and SMPPI in excess of £200 million, on the basis of our analysis of 2006 figures. We noted that a lower degree of pass-through of PPI profits than the full 100 per cent that underpins the figure above would imply greater potential ‘static’ gains from competition for consumers—for example, if one-fifth of the profits from PPI were not passed through in the form of lower credit prices, our lower-bound reasonable estimate for these static gains in PLPPI, MPPI and SMPPI would rise to £440 million. We were unable to make any estimate of the static consumer

detriment for CCPPI, but note that the profitability we identified in the sector (over a third of that found in the combination of PLPPI, MPPI and SMPPI) is consistent with substantial further static consumer detriment. We would therefore expect that the total consumer detriment (both static and dynamic) to be addressed would be significantly more than £200 million a year.

The cost of the package of remedies

387. We undertook an assessment of the cost of the remedies, based on the responses we received to the Notice and follow-up questions.¹⁶⁸ We note that it was difficult for the parties to estimate costs without a detailed view of what each option involved,¹⁶⁹ and that the parties may revise their view of the costs in the light of this provisional decision. If they do, we may revise our current assessment of costs in the light of these changes.
388. In addition to asking the parties for costs of implementing our remedy proposals, we reviewed the cost estimates for the implementation of ICOB (in 2005) and the CCA. We note that both of these regulatory changes impacted far larger numbers of firms and customers than the changes to PPI, with the CCA relating to all credit products and ICOB relating to all insurance products, but considered that the estimates were a useful point of reference when considering the cost implications of our remedies. Table 7 summarizes the estimated costs of these other regulatory changes. Given that the market for PPI is much smaller than the markets affected by these other changes, that supervisory systems are now in place for insurance products and the impact of the previous regulatory changes was generally greater (for example, the CCA information required four different notices to be sent to the customer), we would

¹⁶⁸On 22 July we asked a number of parties for cost estimates based on past implementations of EC directives or FSA rules. We requested that parties exclude income impacts as well as any declines in penetration rates.

¹⁶⁹We also note that [X] and [X] said that at this stage, it was not practicable for them to provide any useful estimates of the likely costs of implementing many of the possible remedies identified by the CC, and that [X] and [X] were only able to provide very rough estimates in the time available, such as 'low cost' or more than £5 million. However, most parties we asked were able to provide more detailed estimates.

expect the costs of these other regulatory changes to be significantly higher than the costs that would be incurred as a result of our remedies.

TABLE 7 **Costs of other regulatory changes**

Change	Costs (£m)	
	One-off	Ongoing
<i>ICOB 2005 (FSA)</i>		
Training and competence*	12.1	13.4
Product disclosure†	32.2	10.0
Record keeping	-	7.2
Internal supervision‡	35.5	123.8
System changes	84.9	-
Initial staff training	31.3	-
Total costs	197.4	165.6
<i>CCA 2006</i>		
Cost of new post-contract information	63§	N/A

Source: CP 187 FSA (www.fsa.gov.uk/pubs/cp/cp187.pdf) and The Full Regulatory Impact Assessment for the CCA 2006 (www.berr.gov.uk/files/file24434.pdf).

*The main drivers of costs associated with these proposals were one-off costs of implementing a formal training regime and the ongoing maintenance of the regime.

†The estimates are based on a number of factors including: the additional sales time to deliver policy summary information orally in telephone sales; additional printing costs for the policy summaries; the additional sales time to disclose significant and unusual exclusions; additional policy documents; additional printing and postage costs; and additional systems costs to provide policy summaries to medium and small intermediaries.

‡Firms estimated that they would need additional supervision and compliance resources to set up a compliance regime and to oversee compliance on an ongoing basis.

§This BERR estimate is based on the figures used in the RIAs relating to the new Consumer Credit Act 2006 and included in the introduction of four standard notices—relating to annual statements, arrears notices, the notice relating to fees and charges and notices in relation to post-judgment interest. It was estimated that the cost to small business was £31.5 million, intermediate businesses would total about £15.5 million and the cost to large businesses would be about £16 million. One party ([redacted]) said that these costs had to be revised and could have been up to 100 times higher in practice.

Note: N/A = not available.

389. The cost estimates provided by the parties of implementing our remedy proposals varied significantly (see Appendix 11), in part reflecting the level of detail in which these proposals were set out in the Notice and also the different business models operated by different parties. For example:

- [redacted] said that the set-up cost of implementing option 1 would be immaterial, whereas [redacted] said that it would cost between £9 million and £11 million to implement.
- [redacted] said that option 4 could cost between £15 million and £35 million for it to implement (including £10 million for the removal of single-premium products and the implementation of replacement products, as it assumed that single-premium

products could not be sold if there were a point-of-sale ban) whereas [X] said that it would entail set-up costs of between £2.3 million and £2.6 million.

- Similarly, [X] said that option 7(a) would cost about £10 million to implement, whereas [X] estimated it would cost £1.97 million to implement (though it assumed its underwriter would bear the cost of changes to product design).

We have summarized the cost estimates provided in Appendix 11.

390. Given the large variation in cost estimates provided by the parties, we were not convinced that the figures provided to date accurately estimated the likely costs of implementation. It appeared likely that some parties had substantially overestimated the costs of implementing our remedies. Further, the level of detail provided in responses varied significantly, such that it was not possible in most cases to infer the total cost of implementing the proposed remedies package other than by adding up the quoted costs of implementing individual remedies (which would involve double-counting of costs common to the implementation of more than one remedy).
391. In light of this, and the number of parties which felt unable to provide us with estimates at all, it is difficult to draw precise conclusions at this stage about the total cost of implementing these measures for individual companies and for the industry more widely. For example, the total industry set-up costs implied by individual providers' submissions¹⁷⁰ range from £50 million to over 20 times that amount, whereas the implied ongoing costs range from £10 million to over 20 times that amount.
392. We find it highly improbable that the costs of our remedies would be anywhere near the top of these ranges. By way of comparison, we looked at the costs of implementing ICOB (see Table 7)—which relate to the initial FSA regulation of all insurance

¹⁷⁰Calculated by taking the implementation cost of a provider and dividing by its market share.

products and are likely to be considerably larger than the costs of implementing our remedy package. The FSA estimated ongoing costs of less than £170 million and set-up costs of less than £200 million. Based on the cost estimates provided so far, we consider that one-off costs of implementing the proposed remedies package would probably be more than £50 million¹⁷¹ but considerably less than the cost of implementing ICOB. We think that the range of ongoing compliance costs could be between of £10 million and £70 million.¹⁷² In light of the more detailed proposals set out in this provisional decision, we would welcome further, detailed, representations on the cost to implement the proposed remedy package. We would also welcome views from parties of specific ways in which the remedies that we have proposed could be implemented, that would materially reduce the costs and the scale of potential cost savings associated with different methods of implementation.

393. Most of the set-up costs were for system changes, whereas most ongoing costs related to marketing and communication. Table 8 shows the most important cost factors by each option that we are proposing to take forward.

TABLE 8 The most important cost factors by option

	<i>Option 1</i>	<i>Option 3</i>	<i>Option 4</i>	<i>Option 6</i>	<i>Option 7(a)</i>
Set-up factors	IT systems changes and marketing	Information feeds and system changes	IT system/operational changes and training	System changes	Replacing the current product and system changes
Ongoing factors	Marketing and communications	Commissions to websites/updating information and credit and risk changes	Marketing and communications	Additional mailings/call centres and other communications	Additional monitoring

Source: CC analysis of data provided by the large distributors.

394. We acknowledge that this remedy package represents a substantial change to the way that PPI is bought and sold and that the transitional costs for distributors of

¹⁷¹Calculated by taking the minimum implementation costs submitted by a provider for each option and dividing this by its market share to get an estimate of the market cost.

¹⁷²Calculated by taking the ongoing compliance costs of all the providers which submitted cost estimates to us and dividing this number by their combined market share based on GWP.

implementing the package are likely to be material. However, based on the information we have seen so far, we conclude that the ongoing costs of the remedy package we are proposing would be significantly less than the annual customer detriment we have provisionally found (see paragraphs 385 and 386) so that, over time, the benefits to customers of putting this package in place will substantially outweigh the costs. The evidence we have so far received indicates that the proposed package would not increase parties' costs by an amount that was disproportionate to the AEC and related customer detriment we have provisionally found.

Conclusion on effectiveness and proportionality

395. We conclude that that package of remedies proposed in this paper will deal with the AEC that we have provisionally identified in a timely manner. Each of the remedies makes a significant contribution to addressing the AEC, and the elements of the remedy package interact with each other to enhance the overall effectiveness of the package.
396. Because the package will address the AEC in a timely manner, and in doing so will address the resultant customer detriment, we do not propose to deal separately with the customer detriment of higher prices arising from the AEC that we have provisionally found, and as a result are not proposing to impose price caps.
397. We considered other remedy options, including minimum standards for PPI policies and the provision of customer credit card balance data. We conclude that the other remedies options, both those proposed in the Notice and those put forward by parties, would be at least as uncertain in their effectiveness, would be less effective and/or could risk causing an adverse effect on customers as a whole. The reasons for these provisional decisions are set out in paragraphs 145 to 363. We have not

been able to identify any other remedies that would be as effective at addressing the AEC as those we propose to take forward.

398. Based on our analysis and the information that we have collected from the parties, we conclude that the remedy package will increase overall consumer welfare, taking into account the set-up and ongoing costs of implementing the remedies as well as the loss of any relevant customer benefits that customers are currently enjoying through lower credit prices.

399. As with any set of competition-enhancing remedies, we cannot predict exactly how the market will develop. However, we believe that our remedies will remove barriers to search and switching and 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. We consider that the remedies will lead to more active competition for PPI customers: through more active marketing before the credit sale; in response to increased customer search just after the credit point of sale; and by encouraging switching during the life of the credit product. This competition will manifest itself through more PPI advertising and lower prices.

400. We conclude that the remedies set out in this provisional decision represent as comprehensive a solution to the AEC and resultant consumer detriment that we have identified as is reasonable and practicable and that this package should not be modified to take account of credit prices being lower than they otherwise might be.