

PPI REMITTAL

The Competition Commission's approach to reconsidering the point-of-sale prohibition as part of its remedies package

Introduction

1. This document outlines the Competition Commission's (CC) initial view of how it will approach its reconsideration of the inclusion of the point-of-sale prohibition (POSP) as part of its remedies package in line with the Competition Appeal Tribunal's (the Tribunal) Order of 26 November 2009. Our thinking may evolve in light of further analysis and comments received on this document.
2. We invite comments on our proposed approach, and suggestions of methodologies or sources of data that might assist our analysis. Comments that include suggestions for additional or alternative lines of analysis should outline the specific benefits of any such analysis. Please provide submissions by or on **6 January 2010** to allow us to take them into account as appropriate in determining the best approach to adopt.

The market investigation

3. On 7 February 2007 the Office of Fair Trading (OFT) referred to the CC for investigation the supply of payment protection insurance (PPI) services in the UK. In its [final report](#) (the report) published on 29 January 2009, the CC found that certain features of the PPI market, including the sale of PPI at the point of sale of credit, gave rise to an adverse effect on competition (AEC) and proposed a package of remedies, which included the POSP, to address the AEC.

The Tribunal's judgment and remittal to the CC

4. On 30 March 2009 Barclays Bank PLC (Barclays) challenged aspects of our final report, including the inclusion of the POSP in the package of remedies. Lloyds Banking Group PLC (Lloyds) and Shop Direct Group Financial Services Ltd (SDGFS)

intervened in support of Barclays; the Financial Services Authority (FSA) intervened in support of the CC.

5. The Tribunal handed down its judgment on 16 October 2009.¹ It quashed the decision to impose the POSP as part of the remedies package on the grounds that the CC, in conducting its proportionality analysis, had failed to take account of a material consideration namely the effect of the loss of convenience of purchasing PPI at the point of sale of credit on take-up rates, which should also have been included in the modelling of the effects on consumer welfare of the remedies package. The Tribunal stated explicitly that this decision did not mean that the CC cannot by that process lawfully decide to include the POSP as the result of its reconsideration.

6. In addition, whilst not sufficient in themselves to warrant the quashing of the decision, the Tribunal identified the following issues to be included in a reconsideration of the decision to include the POSP:
 - (a) The timescale over which the remedy package (including the POSP) may be expected to take effect. The Tribunal concluded that the CC should have addressed the issue of timescale in the report in more detail; however, this failing was more in the expression of reasoning than in any deeper failure to take the question of timescale into account.
 - (b) Inclusion of the likely costs of implementing the package of remedies, and the on-going costs of the remedies, as well as the likely increased costs of marketing PPI products in the model used to determine the consumer gains from the remedy package ('the model').
 - (c) Reconsideration of the input of price elasticity of demand for PPI into the model.

¹www.catribunal.org.uk/files/Judg_1109_Barclays_16.10.09.pdf.

7. Finally, the Tribunal suggested that the CC may wish to bear in mind, in its reconsideration of the POSP as a remedy, SDGFS's submission that our remedies package offered no solution to a 'conundrum': that the CC's choice of remedies package involved a judgement that stand-alone providers would be able to offer real competition to distributors; but in relation to retail PPI the CC recognized that competition from stand-alone providers was adversely impacted by their inability to tailor a stand-alone PPI policy to the exact amount owed from time to time by the consumer.
8. On 26 November 2009 the Tribunal directed the CC to reconsider the imposition of its POSP as part of its remedies package in accordance with the principles set out in the judgment.²

Analytical approach

9. We set out below the broad approach and outline of the analysis that we are considering adopting to comply with the Tribunal's direction.
10. The POSP was proposed as part of a package of remedies to address the AEC that we found to arise from the following features: absence of competition on price or quality of PPI; barriers to search by customers because of difficulty of comparing PPI prices; barriers to switching between PPI policies; and the sale of PPI at the credit point of sale, which further restricts the extent to which other providers can compete effectively. Within this package, the CC saw the POSP as particularly important in addressing the point-of-sale advantage associated with selling PPI combined with a credit product.
11. The key questions we need to address are:

²www.catribunal.org.uk/files/1109_Barclays_1109_26.11.09.pdf.

- whether our original package of remedies (including the POSP) is a proportionate, solution to the AEC that we found; and
 - if not, how should we modify our package of remedies.
12. We set out below how we propose to address the first question. If we conclude that the original package of remedies would not be a proportionate solution, we will turn our attention to the second question.
13. In carrying out this additional analysis, we will not be starting from scratch. We will draw on analysis conducted during our PPI market investigation wherever possible, and rely on general principles or empirical evidence that may help inform our view of how the POSP is likely to affect consumers within the UK.

How has the market changed since we published the report?

14. In the report we looked at the state of PPI markets up to 2007³ and in some cases the first half of 2008;⁴ in addition, we considered the implications of the economic downturn for our remedies decision.⁵
15. We will gather data from parties on how PPI markets have developed since then, looking at data on sales of credit and of PPI for the second half of 2008 and the first nine months of 2009. To this end we are sending data requests to significant current or former PPI distributors, underwriters and stand-alone providers. This will give us a clear picture of the current state of PPI markets, as relevant background to our new analysis of the POSP part of the remedy package.

³For example, we examined profitability of PPI in 2007 in Figure 7 of Appendix 4.4.

⁴For example, we looked at the GWP of PPI policies in Table 2.3, penetration rates in Table 2.5, share of supply in Table 2.7, and sales of stand-alone policies in Table 3.3.

⁵See paragraphs 10.14–10.20 of the report.

What will the markets look like when the remedy package comes into force?

16. We will consider what the state of PPI markets may be expected to be starting from when the remedies are due to come into force. This is important as the benefits that may be expected to accrue from the remedies package will need to be assessed against how the market would operate without the remedy package in place from that time on.

17. To do this we shall need to make an assumption about when the remedies may be expected to come into force. If we were to conclude that the remedies package, including the POSP, would be an effective and proportionate remedy to the AEC, we expect that the remedies package would be brought into force through an Order similar to the one consulted upon in July 2009.⁶ This envisaged some elements of the remedies package coming into force within six months of making the Order, with the remaining measures (including the POSP) coming into force within 12 months—though we may reconsider whether the implementation time frames within the Order should remain as currently specified. We expect that our reconsideration of the inclusion of the POSP in the remedies package and the putting in place of an Order would mean that all elements of the remedies package (including the POSP, if we decide that it should be retained) should be in force in the second half of 2011. We propose, therefore, to assume for the purpose of evaluating the proportionality of including the POSP in the remedies package, that the remedies package would come fully into force in the second half of 2011.

18. We will consider what the state of PPI markets is likely to be from the second half of 2011 onwards. In reaching a judgement on this we will have regard to evidence including, but not limited to, any projections or targets for credit sales and PPI sales produced by distributors or underwriters.

⁶www.competition-commission.org.uk/press_rel/2009/july/pdf/31-09.pdf.

Proportionality of the remedies package

19. We will reconsider whether the imposition of a remedies package including a POSP is justified, once the effect of such a remedies package on consumer convenience is taken into account.

20. In order to consider this question we shall need to take views on the extent to which the imposition of a POSP will reduce sales of PPI because of a loss of convenience for consumers; and the extent to which other aspects of the remedies package, and the behaviour of PPI distributors and stand-alone providers in response to the remedies package, will increase convenience and/or sales of PPI.

The scale of the reduction in convenience

21. We propose to consider the extent to which the POSP would result in reduced sales of PPI due to a loss of convenience. In reaching a judgement on this point we will re-assess evidence that has already been submitted as to how changes to PPI sales processes could affect PPI take-up,⁷ and consider any new evidence submitted by parties on this issue. In considering the weight to be attached to this evidence, we will have regard to factors such as the quality of the evidence, its relevance to the remedies package that was proposed by the CC and the extent to which any identified drop off in PPI sales may be attributed to a loss of convenience.

22. We will examine business plans and other internal documents of PPI distributors, underwriters, and stand-alone providers for any evidence relevant to this issue.

23. We will also look at markets where insurance has been, or is, de-linked from the sale of a related product to understand the extent to which de-linking involves a loss of convenience in these markets and, if so, what has been the response of consumers

⁷This evidence is referred to in paragraphs 10.46–10.49 of the report.

and providers. Examples that we plan to consider are travel insurance (most of which is no longer sold by travel agents) and buildings insurance (which can be sold alongside mortgages or on a stand-alone basis).

24. In addition, we intend to conduct consumer research to develop an understanding of the value consumers place on the convenience of buying PPI at the same time as credit, as opposed to buying it at a later point in time. The aim of this research will be to give us additional insight into consumers' attitudes towards the convenience of buying PPI at the same time as credit and an indication of the magnitude of any loss of convenience that might be expected from the imposition of a POSP alongside the other measures in the remedies package.

25. In taking a view on the impact of any loss of convenience, we will also look at whether sales to date have been at a level such that they are an appropriate starting point for an evaluation of this issue.⁸ In particular we will gather information from parties on complaints about sales processes, and consider information about mis-selling from the FSA and Financial Ombudsman Service (FOS).

The modelling of proportionality

26. In the report, one of the inputs to our assessment of the proportionality of imposing the remedies package, including a POSP, was the use of a model to estimate the magnitude of one part of the static consumer detriment associated with the AEC that the remedies package would address.⁹

⁸See paragraphs 5.135–5.138 of the report.

⁹See paragraph 10.494 of the report. We were unable to use the model to estimate the static consumer detriment for CCPPI, though the evidence of profitability in the sector was consistent with substantial further static consumer detriment. In relation to retail PPI, the model was not relevant to the estimation of static consumer detriment, which we estimated by another method (see paragraph 10.496). In addition, there were a large category of dynamic consumer detriment which we did not quantify (paragraph 10.493) and a static consumer detriment associated with adverse selection which we did not quantify (paragraph 10.495).

27. We propose using this model again, amending it as appropriate. Some of the inputs to the model used data from 2006, and we will seek to understand changes to levels of sales of credit and PPI, penetration rates, and the price of PPI relative to credit since 2006, in order to evaluate the way in which these changes affect the results from the model.
28. We will be modelling what we expect to happen in 2011 and beyond. We will consider whether it is more appropriate to use data from the period 2007–2009 or data from within the period 2003–2006 as the starting point for our analysis. We will consider whether 2009 data might represent a period of unusually low sales of credit and PPI (due to the credit crunch and subsequent recession), such that it would not be an appropriate starting point.¹⁰ Similarly we will consider whether data from the period 2003–2006 might represent a period of sales higher than might reasonably be expected at least in 2011. In exercising our judgement on this question we will have regard to the evidence mentioned in paragraph 18.
29. We will consider whether and, if so how, to adapt the model to take account of the loss of convenience associated with not being able to buy PPI at the same time as credit, using our judgement based on the analysis set out in paragraphs 19 to 24 as to the magnitude of the loss of convenience. A loss of convenience could be modelled as an increase in the overall costs to consumers of taking out PPI, resulting in a reduction in consumers' demand for PPI for any given PPI price level (ie modelling a shift in the demand curve). We will consider the appropriateness of this modelling approach as well as any other robust methodologies put forward by parties.

¹⁰We also note that, for PLPPI, 2009 represented an abnormal year. Distributors stopped selling single-premium policies, and whilst some of these were replaced by regular-premium policies the level of GWP for PLPPI sales in 2009 may be unrepresentatively low as there is neither a full year of single premium policies nor a back-book of existing regular-premium policies.

30. We will look at what an appropriate value for the market-level price elasticity of demand for PPI would be (see paragraph 6(c)). Market-level price elasticities are generally lower than firm-specific price elasticities, because the latter also incorporate switching between firms in the market. However, we found very little evidence of competitive interaction between PPI providers in our final report. We shall therefore consider carefully the extent to which an estimate of firm-specific elasticity of demand is likely to be a good proxy for a market-level price elasticity of demand in light of these findings.
31. We will consider how to take account in the model of the ongoing costs of implementing the remedy package including any increase in marketing costs (see paragraph 6(b)). We will look for evidence to inform a judgement about how an increase in marketing activity for PPI would increase the demand for PPI products (see paragraph 23).
32. As well as considering which costs of the remedy package it is appropriate to take account of in the model, we also intend to take account of the positive effects of the package in the model, where this is feasible. To this end we propose to consider whether there are any positive effects of the remedies package—in addition to lower PPI prices, which are already incorporated into the model—which we should take account of in the model, and how these might be modelled. Such effects might include:
- increased take-up of PPI as a result of increased advertising;
 - distributors encouraging consumers to return and take out PPI by making the completion process as straightforward as possible;
 - stand-alone providers developing and delivering good-value products which are convenient to take out;

- increased quality of PPI products due to increased competition between PPI providers for customers;
- increased take-up of PPI as a result of an improved perception of PPI due to better-value and better-quality products;
- improved quality of PPI sales resulting from consumers' ability to consider their options away from the credit POS;
- increased take-up of PPI as a result of an improved perception of PPI due to a reduced incentive and ability for firms to mis-sell policies, which could arise from the inability to sell PPI at the credit point of sale and/or from the lower profit margins that we would expect to result from more competitive PPI markets.

33. We will also consider whether in light of recent developments in the market and further information received we should amend or conduct further sensitivity analysis in relation to any of the underlying assumptions in the model as used in the report. These might include the proportion of excess profits made on PPI that are passed through to credit consumers as lower credit prices and where the remedies package lies on the spectrum between 'system' and 'non-system' remedies.

The timescale over which the remedies package will take effect

34. As part of our assessment of whether the remedies package including the POSP would be an effective and proportionate solution to the AEC, we will set out our reasoning as to how quickly the remedies package, including a POSP, would take effect (see paragraph 6(a)). In doing so we will have regard to any new submissions put to us.

Retail PPI

35. The Tribunal did not address the submissions made about retail PPI on behalf of SDGFS. However, the Tribunal indicated that in reconsidering the POSP as a

remedy in relation to retail PPI, the CC may wish to bear in mind the ‘conundrum’ that SDGFS had identified. This arose from our finding that, in relation to retail PPI competition by stand-alone providers was adversely affected by their inability to know the level of credit being extended by the retailer on a fluctuating credit account, so that they could not tailor a stand-alone PPI policy to the precise amount owed from time to time by the consumer. We made a similar finding in relation to CCPPI. We did not put in place a measure that would enable stand-alone providers to offer products that were tailored to consumer balances with this degree of precision, and SDGFS submitted that, in the absence of such a remedy our remedies package could not rationally be expected effectively to remedy the AEC in relation to retail PPI.

36. We propose to consider, and set out, our reasoning on the question of the extent to which retail PPI and CCPPI distributors would face effective competition if a remedy package, including the POSP, were implemented. We will have regard to the evidence already to hand and any other relevant evidence we receive.

Key outputs

37. The key output of this investigation will be a new decision on whether to impose a POSP as part of the remedy package (and if not, what remedies should be imposed). Prior to that decision we will publish a provisional decision for consultation.

Timings and information requirement

38. The CC will shortly publish an administrative timetable. We aim to complete the work by summer 2010. During the course of the investigation, we are likely to seek information and documents, possibly at short notice. Compliance with any deadlines we specify will greatly assist us and help to ensure that the timetable is met.