

Payment Protection Insurance (“PPI”) Market Investigation Remittal

The Royal Bank of Scotland Group PLC (“RBSG”): Response to the Competition Commission’s (“CC”) Provisional Decision

This submission sets out RBSG’s comments in relation to the CC’s Provisional Decision in the PPI Remittal (the “**Remittal Provisional Decision**”).

RBSG does not consider that it is proportionate for the CC to re-introduce a POS ban as part of its remedy package. In the 2009 Final Report the CC found four features of the market which resulted in an adverse effect on competition (“**AEC**”): (i) firms’ failure to compete; (ii) barriers to search; (iii) barriers to switching; and (iv) the point-of-sale (“**POS**”) advantage. RBSG believes that the scale of these features of the market have diminished since the CC’s original investigation and that taking into account the limited scope of the net welfare benefits which might result from a POS ban, the AEC can be remedied proportionately without a POS ban. Given customer preference and the loss of convenience to customers which would flow from a POS ban, RBSG finds that a POS ban would be disproportionate and indeed harmful to the majority of customers who want to buy PPI at POS, as evidenced by the CC’s research. RBSG therefore believes that the CC should further reconsider the balance before confirming the POS ban in its Remittal Final Report.

1 The AEC has changed

Before turning to RBSG’s main comments which concern the CC’s analysis on loss of convenience (Section 2 of this paper), RBSG has the following comments on the AEC. Looking at the AEC today, RBSG believes that the CC should consider further the extent to which the AEC can still be characterised in the same terms that it was in the 2009 Final Report such as to justify a POS ban. A number of features of the market today mean that the AEC has diminished:

1.1 Single premium policies are no longer being sold so barriers to search and switching must have diminished

First, single premium policies are no longer offered in the market following the Financial Services Authority’s (“**FSA**”) requirement that firms withdraw from selling single premium PLPPI products by May 2009 (noting that CCPPI and MPPI are sold as regular premium products). RBSG considers that there is no realistic possibility that the FSA will change its requirement meaning that this has the effect of banning single premium PPI policies from the market.¹

Because single premium policies are no longer a feature of the market then any part of the AEC resulting from the sale of single premium products must fall away. This must impact the CC’s findings because certain barriers to search and switching identified in the AEC, for example, only relate to single premium policies (e.g. product complexity as a barrier to search and terms which make switching expensive). Equally the CC’s concerns around failure to compete for rivals’ customers and the POS advantage which had attached to the sale of single premium policies can no longer form part of the AEC if single premium policies are not sold. RBSG also notes that withdrawal of single premium policies will have lowered profit margins (although this will not yet be reflected in the data provided to the CC) and also brings to an end PPI policies which can only be sold at POS. Regular premium policies can be bought away from POS.

¹ We note that the CC’s remedy to ban single premium products will mean that in future there will be no single premium PLPPI or SMPPI policies in any event.

1.2 Different consumer and regulatory environment exists today

Second, RBSG considers that certain features of the AEC identified in the 2009 Final Report no longer exist because firms and consumers operate in a different environment today. In particular, RBSG considers that since the CC began its investigation in early 2007 there has been a significant increase in consumers' knowledge and awareness of PPI due to factors such as the considerable press comment on PPI, action taken by consumer organisations, and regulatory action taken by the FSA against firms selling PPI products,² as well as the stance adopted by the Financial Ombudsman Service (the "FOS") in dealing with consumer complaints about sales of PPI. This increased consumer awareness undoubtedly addresses a number of the features of the AEC identified by the CC such as barriers to search and switching and aspects of the POS advantage.

Furthermore, changes in the regulatory environment since 2007 mean that certain features of the CC's AEC are likely to be overstated. We have already referred to the fact that the sale of single premium policies is effectively banned. PPI selling is regulated by the FSA which has imposed a number of specific and detailed requirements on firms aimed at ensuring transparency, the disclosure of product and firm specific information and that customers are treated fairly. For example, the actions taken by the FSA such as stopping the sale of single premium policies and publishing new ICOBs rules (in force since July 2008) address elements of the CC's concerns including barriers to entry such as product complexity, the perception that PPI increases customers' chances of getting credit, the lack of awareness that PPI is an optional product and the bundling of PPI with credit.

1.3 Changes to the competitive environment

The CC notes throughout the Remittal Provisional Decision that traditional stand-alone provision has declined (see paragraphs 4.5, 5.12 and in particular 7.77 where the CC notes that "*with the remedy package in force, we would expect some of the traditional stand-alone providers to remain in the market (with underwriters supporting them), although we noted that there have been some recent exits. But, there would be, in our view, a key development: large PPI distributors would enter the stand-alone market*"). RBSG considers that this is a material change in the competitive environment. The CC's original decision was taken in an environment where stand-alone providers (i.e. non credit arrangers) were seen as a key feature of the market and there were concerns over whether there was a level-playing field between the two types of providers. This no longer seems to be the case.

1.4 The CC cannot rely on 2009 as evidence of failure to compete

At paragraph 5.3 of the Remittal Provisional Decision, the CC finds "*no indication of distributors or intermediaries actively seeking to win customers from their rivals. The economic situation led to a number of mergers [...] which we did not think led to an increase in competition among PPI providers. We found no evidence of distributors in 2009 starting to offer PPI products to anyone other than their own credit customers. As set out in paragraphs 7.51 to 7.64 we found that in response to the 2009 report many parties have been developing products that could be used to target competitors' customers. However none of these has yet come to market.*"

The fact that firms have not yet launched new products cannot be used to inform the CC's reconsideration of firms' ability to compete for their rivals' customers: 2009 was a transitional

² RBSG also notes MBNA's comments published in the Remittal Provisional Decision that the recent work of the FSA and FOS has significantly increased consumer awareness of PPI and their needs.

year for the market as firms withdrew single premium products and considered introducing new products. Firms' decisions will reflect the severe economic conditions in 2009, as well as changes in the regulatory climate all of which is likely to have had a temporary impact on firms' willingness to introduce new products during this period. Instead we would expect the CC to look at the fact that a number of providers *are* developing standalone products that could be used to target competitors' customers and to take this into account as a relevant feature of the market in reassessing the AEC. **[CONFIDENTIAL]**

In RBSG's view, the changes above mean that the AEC which the CC is seeking to solve has diminished since the CC's original investigation and RBSG considers that the remaining features can be addressed by the CC's informational and switching remedies alone. This, not the CC's 2009 findings, should be the starting point for the CC's proportionality assessment in determining the net welfare benefits of a POS ban.

2 Assessing Loss of Convenience – Proportionality of the POS ban

In order to assess the impact of the POS ban in remedying the AEC, the CC considers the likely benefits of, and the loss of convenience from, buying away from POS. In its analysis, the CC looks at evidence including parties' natural experiments to simulate the POS ban, internal estimates of likely take-up of PPI with a POS ban in place, and survey evidence on the preference for buying PPI away from POS. The CC then concludes that the POS ban will lead to a net welfare benefit.

However, RBSG considers that while the CC has undertaken extensive analysis to attempt to demonstrate the net welfare benefit, the net welfare benefit from the POS ban is likely to be minimal or even become a welfare detriment. The CC does not seem to have produced satisfactory answers to certain aspects of the cost-benefit-analysis of the POS ban. In particular, the cost-benefit-analysis is based upon:

- a) the order of magnitude of the benefits. The CC's results incorporates two primary benefits that are expected after a POS ban: (i) lower PPI prices as a result of increased competition; and (ii) higher welfare for consumers who prefer to purchase PPI away from POS;
- b) the order of magnitude of the costs. The POS ban also entails costs arising from the inconvenience of buying PPI later, including: (i) the lower welfare for consumers who prefer to purchase at POS but would be required to purchase PPI later; and (ii) a proportion of consumers will cease to purchase PPI because of the inconvenience of buying PPI later.

The CC's analysis concludes that the benefits outweigh the costs because the price reduction will be significant, consumers attach a higher value to purchasing away from POS relative to purchasing at POS, and the reduction in sales due to consumers not purchasing PPI as a result of the inconvenience is not significant. Yet RBSG considers that the CC has overstated the benefits and understated the cost of the inconvenience of purchasing PPI away from POS, as follows:

- *Limited evidence to support a significant price reduction as a result of a POS ban:* the assumption of a significant price reduction and increased competition does not seem robust as there is limited evidence that consumers will shop around for PPI. Results from the Accent survey indicate that only 12 - 18% of all respondents would prefer to

shop around. This is discussed in more detail in section 2.1 below.

- *The take-up of PPI is likely to reduce:* a break-even analysis conducted on the models used by the CC (not accounting for the inconvenience costs from the Accent survey) shows that if PPI penetration drops by around 15 - 21%, the net benefits of the remedies would be zero.³ Evidence from the CC, as well as from some of the PPI providers, suggest that it is very likely that the PPI penetration would indeed reduce by at least 20% and therefore the net benefit of the POS ban would be zero.⁴ The Accent survey highlights that more than 50% of consumers prefer to purchase at POS and the LBG pilot simulating the POS ban showed a significant reduction in take-up rates (around 60%). Moreover, the limited shopping around suggests that even those people who prefer to purchase PPI later may in practice not shop around but instead wait to be contacted by the PPI provider. Outbound telemarketing experience in the industry indicates that it is unlikely that providers will be able to contact more than 50% of such customers implying a further reduction in the PPI take-up rate. This is discussed in more detail at section 2.2 below.
- *Strength of preference attached to purchasing later (in the Accent survey) is unreliable:* the high valuations of purchasing away from POS seem inconsistent with the high incidence (85% of all respondents) of POS purchase. In general, as detailed below, the survey evidence on the value attached by consumers to purchasing PPI at POS or away from POS seems unrealistic and warrants further investigation. Moreover, in taking into account both the reduction in PPI prices and the value attached to purchasing later, the CC seems to have double-counted (at least part of) the benefits (explained in more detail at section 2.3 below).

In the light of the above evidence, RBSG does not consider that the CC's finding of a net welfare benefit resulting from a POS ban is sufficiently robust. This is also borne out by the CC's own sensitivity analysis which shows that when the model excludes some of the unrealistic and large valuations for purchasing later (including the double-counting of some of the benefits), the net benefit would be close to zero, and in some cases, negative.⁵ All in all, RBSG has serious concerns about the CC's analysis.

2.1 CC's assumptions about the future of the PPI market and likely price reduction

When assessing the benefits of the POS ban (and its proportionality), the CC makes a number of assumptions about the future of the PPI market resulting from the remedies. In particular, the CC assumes that the 2009 remedies will lead to: (i) market entry by new stand-alone PPI providers; (ii) an increase in shopping around by consumers from having more information about PPI policies; and (iii) distributors offering cheaper products. These assumptions are clearly critical to the CC's analysis because they form the basis for the CC's view of the future PPI market and on which the CC assesses the proportionality of the POS ban. If these assumptions prove to be wrong then there is a considerable risk that the POS ban intervention will result in a net welfare detriment rather than a net welfare benefit. RBSG would therefore query whether these assumptions have been tested to the extent required before imposing such a significant remedy.

³ This analysis has been conducted using the CC's model as sent to all parties with the modification that the inconvenience costs are not taken into account; the counterfactual penetration rate which yields a net benefit of zero is then calculated from this model. The reduction of penetration rate required for a net benefit of zero varies by product.

⁴ Although we note that a part of this reduction is taken into account by the CC in their modelling of the inconvenience caused to consumers who prefer to buy at POS.

⁵ Moreover, the CC has only conducted individual sensitivities along with other base case assumptions, each of which give rise to some uncertainty.

2.1.1 *Market entry by stand-alone providers*

In its assessment of the future market the CC considers that there will be more market entry by new stand-alone providers. However, as outlined in section 1.3 above, the CC recognises that traditional stand-alone providers have withdrawn from the market and that therefore standalone provision will need to come from distributors. RBSG considers that the CC should adjust its assumptions to take into account this change in market conditions.

2.1.2 *Customers will shop around with more market information*

The CC concludes that following the implementation of the full remedy package there would be an increase in the extent to which customers would shop around for PPI, which would reinforce the increase in price competition. While RBSG would expect the informational remedies to increase shopping around, we note that the results from the survey conducted by Accent do not provide conclusive evidence on significant levels of shopping around by customers. The survey indicates that around 30 - 36% of all respondents preferred to purchase PPI at a later stage, and only around 40 - 50% of these customers preferred to delay in order to shop around.⁶ Hence, overall, only 12 - 18% of all respondents stated that they would prefer to shop around. Furthermore, all of these customers may not actually delay and shop around with a POS ban in place. The Accent survey indicates that over 85% of all respondents currently purchase PPI at POS.⁷ This seems to be inconsistent with a strong preference for delay and shopping around, especially because respondents already have the option of purchasing regular premium PPI at a later stage. The results from the qualitative survey conducted by Accent also suggest that customers may not actually delay and shop around. For example respondents highlighted that it is easier and faster to get PPI from the same provider because the credit provider already has the necessary information; and that there is a trade-off between a cheaper alternative and the longer time and effort it will take to finalise the loan and take out PPI. The risk of forgetting about buying PPI at a later stage was also highlighted.⁸

2.1.3 *Will the POS ban lead to cheaper products?*

It is not clear to RBSG why the CC concludes that PPI prices will unambiguously drop after implementing the POS ban. While the evidence on shopping around and market entry - both of which potentially increases competition and lowers prices - are limited, there are a number of other factors that suggest that prices may go up as a result of a POS ban. For example, the possibility that adverse selection may inflate prices as this increases the risk borne by underwriters and hence the price **[CONFIDENTIAL]**.

2.2 **Reduction in take-up**

The LBG pilot looked at take-up of PPI with a simulated POS ban in place (i.e. they invited customers to call back after 24 hours, and initiated calls to customers after seven days). The pilot showed that penetration rates were around 0 - 10% with a POS ban in branches as well as over the telephone. This is compared to a penetration rate of around 40 - 50% without a POS ban.⁹ RBSG considers that this is an important discovery, although notes that the CC chooses not to rely on the results of the pilot because:

⁶ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, pp. 43 - 45.

⁷ The figure is 91% for PLPPI and 86% for MPPI, and a maximum of 11% may have been due to misselling; Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, pp. 30-31.

⁸ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, section 3.

⁹ CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010 Appendix C, p. C9.

- the pilot did not account for the new market environment resulting from the other remedies and did not offer the Internet as a medium for customers to return to buy PPI. The CC suggests that the penetration rate is likely to be higher if such factors are taken into account. The CC is also concerned about very low take-up of personal quotes in branch (13.4%), querying the effect of factors such as sales staff behaviour;
- the proportion of loan customers receiving a quote for PLPPI was around one-third of the penetration rate for PLPPI. The CC suggests this was due to sales staff not putting in sufficient effort in the pilot (which is likely to be influenced by staff incentives) or because a significant proportion of LBG's normal PLPPI purchasers buy PPI policies that they would not if given the time to reflect. The CC does not appear to consider that a drop-in penetration may result from the inconvenience of buying away from POS.

It is not clear to RBSG why this evidence has not been applied to the CC's re-consideration of the POS ban. RBSG's submits that many of these issues may apply to real-life selling and therefore the pilot provides the CC with a helpful example of the POS ban at work. In addition, the LBG pilot also provides other evidence, which the CC does not consider explicitly but which RBSG considers is relevant to the analysis and should be taken into account when assessing the likely reduction in the penetration rate following the implementation of the remedies:

- take-up of quotes via telephone was higher (40.6%) and similar to the corresponding penetration rate.¹⁰ We assume that the incentive structure for telephone staff was similar to that for staff in branches. Therefore it is not apparent that the incentive structure applicable to staff sales, and hence the process of sales, is the reason for the low take-up of quotes in branch;
- of the customers who received quotes but did not purchase PPI, 11% said they would have purchased the product if the price was 30% lower.¹¹ If this is taken into account, the penetration rate would be around 20% (current 0 - 10% + 11%), which is still much lower than the penetration rate in branches without the POS ban (and constitutes a drop of around 60%);
- the LBG pilot also provides useful evidence on the extent to which customers would be "lost" due to difficulties in contacting them after POS. As a first-stage loss, a proportion of customers would opt-out of receiving quotes via post and/or being contacted via telephone by the PPI provider. Furthermore, even when customers agree to be contacted, the provider may be unable to contact the decision maker, because the telephone call is unanswered or even if answered by someone, the decision maker may not be available. The LBG pilot shows that only 55% of customers could be contacted via outbound calls to sell PPI after the initial sale and hence some potential PPI purchasers might not purchase PPI at all.¹² **[CONFIDENTIAL]**

2.3 Accent consumer research estimates of consumer preference/valuation unrealistic

RBSG has a number of comments in relation to the CC's interpretation of the Accent consumer research:

2.3.1 Valuation attached to buying PPI after POS

¹⁰ CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010 Appendix C, Table 2.

¹¹ CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010, Appendix C, para 28 (c).

¹² CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010, Appendix C, para 27.

Our main concern is the valuation supposedly attached to buying PPI after POS, by those who prefer to do so. The Accent survey and subsequent analysis¹³ of consumer attitudes towards PLPPI and MPPI highlight the significant value consumers place on the convenience of buying at POS, and the value associated with being able to choose whether to purchase at POS or afterwards. The survey evidence shows that for PLPPI and MPPI 60% and 50% respectively of consumers prefer the convenience of having the option to buy PPI at POS.¹⁴ This shows that for the majority of customers the ability to purchase at POS is important and that the POS ban would remove the choice consumers currently have. However, the CC then finds that the minority who prefer to purchase away from POS value this option more than those who prefer to buy at POS (notwithstanding the fact that those who wish to buy away from POS can already do so, an awareness that could be easily enhanced as part of the remedy package). This finding is used to support a POS ban. The CC does not appear to consider that where customers buy at POS they must value the POS purchase and would continue to buy at POS if they were allowed to do so.

2.3.2 *High consumer valuations and their interpretation*

RBSG is concerned by the CCs' findings regarding the valuation of delay in the survey results. For MPPI customers the average cost of PPI was £35.30¹⁵ per month while the average willingness to not purchase at POS, but for a provider to call you after 7 days, was estimated at an additional £30 per month,¹⁶ by those respondents who preferred to buy after POS. It seems unlikely that a consumer would pay £65 per month in total, nearly double the monthly cost of PPI in order to obtain an extra 7 days to consider the purchase (something which they can do now and for no extra cost). This means that customers who prefer to buy after POS would be willing to pay £30 a month *more* for the option not to buy at POS (i.e. to receive a call later). RBSG questions the credibility of such a finding. It implies that consumers would be indifferent between the following situations: (i) paying £35 for PPI at the POS, without an opportunity to buy it later; and (ii) paying £30 at the POS to buy seven days delay before being offered PPI for a further £35. Paying to delay the purchase seems akin to buying an option. Usually in such cases a customer pays for the option of finding alternatives that may be cheaper but are not known at the POS. This behaviour is understandable if the customer has an expectation that they can obtain cheaper PPI through another provider. Although we would expect that even then it would need to be cheaper by more than the price you paid for the option (e.g. customers would need to be able to obtain PPI for less than £5 from other providers (£35 - £30 = £5). But it is not reasonable to expect to be able to obtain PPI from another provider for 85% less than that offered by the credit provider. Therefore these questionably large valuations bring the CC's reliance on the estimates of willingness to pay into question and the evidence seems unreliable. RBSG would suggest that survey respondents did not understand the hypothetical situation that was presented to them. While the CC appears to acknowledge the high valuations and potential misinterpretation by respondents,¹⁷ its response that a sensitivity analysis can be conducted is inappropriate for such a significant flaw in the analysis.

Such high relative willingness to pay by consumers who prefer to delay also seems inconsistent with the usual potential reduction in prices as a result of shopping around

¹³ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April.

¹⁴ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, Tables 10 and 11.

¹⁵ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, p 23.

¹⁶ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, Table 10.

¹⁷ CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010, 14 May 2010, p. 69 para 7.100.

and purchasing PPI later. Moreover, the survey evidence implies that the extent of shopping around is not likely to be significant which also calls this evidence into question as consumers are likely to be willing to pay more *only* if they expect to gain from such delay through shopping around. It is therefore useful to explore further the possible reasons for such valuations in order to ensure a reliable and robust analysis.

The qualitative parts of Accent's survey suggest reasons why some consumers prefer to purchase at POS, such as immediacy and certainty of cover, reduction in form-filling and sharing of financial information¹⁸, while other consumers prefer the option to delay so that they can shop around or reflect on the offering¹⁹. But neither Accent, nor the CC, explain why they might expect consumers who prefer to delay purchase to have a higher willingness to pay for this option than those who prefer to purchase at POS to retain that option. Given that the POS ban essentially depends on the difference in willingness to pay between these two consumer groups, the lack of economic rationale for the finding and the unexpectedly large magnitudes suggests that the finding should be tested thoroughly to see if it is robust. This could be done either through further examination of the data and/or cross-checking with other surveys of consumers or controlled experiments.

Furthermore, the large valuations, particularly those for consumers who would prefer to buy PPI after POS, seem inconsistent with the numbers of respondents who have purchased at POS, even though the option to purchase later already exists. If respondents' preferences to wait 7 days/24 hours are as high as suggested in the Accent report it seems counter-intuitive that they have purchased at POS and would not have already sought alternatives. These large valuations, relative to the base cost of the product, suggest that more investigation is needed.

Finally, one potential reason for the large valuations by both groups of consumers might be that if consumers were offered such choices in reality they would decide not to purchase PPI at all. As highlighted in RBSG's response to the design of the consumer survey, the survey does not include a 'no purchase option' which would have allowed consumers to say whether the loss of convenience (caused by the delay) would mean that they would not purchase PPI. Thus the consumer research did not offer customers the choice set which they would face in reality, which includes the option not to purchase, if a delay is imposed. Omitting one of the options from the choice set is likely to bias the results of the econometrics and may explain the surprisingly large magnitude and lack of economic explanation for the finding.

2.3.3 *Indirect observation of demand loss from inconvenience*

Instead of directly observing the demand loss from selling at POS, the CC indirectly observes the effect of inconvenience through a consumer's willingness to pay. The high value of willingness to pay for the choice of when to purchase PPI for both groups of consumers (i.e. those who prefer to purchase at POS and those who prefer to wait) may indicate that many consumers would not purchase PPI due to loss of convenience if they did not have the choice of when to purchase.

2.3.4 *Variation in willingness to pay for the choice to buy at POS*

The willingness to pay results in Tables 10 and 11 of Accent's report relate to the average value for the sample as a whole. It would be instructive to see the distribution of those values and in particular examine how those values are distributed and which

¹⁸ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, Section 3.4.

¹⁹ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, Section 3.5.

demographic groups would be most affected. In particular, those demographics for whom PPI is most important may have particularly high willingness to pay at POS. It is likely that those who most value the option to purchase PPI at POS may be those for whom PPI is most important (i.e., those on low/more volatile incomes or those for whom their borrowings are a larger proportion of their income). Note that it is common practice in stated preference exercises to examine how willingness to pay changes over different demographic groups by interacting the timing variables with demographic characteristics to identify which particular demographic groups are likely to be affected. Examining willingness to pay by demographic groups may identify that particular groups of consumers who value the reassurance of PPI have high willingness to pay to maintain the option to buy at POS in both MPPI and PLPPI markets.

Further, it is not clear why the willingness to pay to retain the option to purchase at POS for those customers who prefer to buy at POS is different between those purchasing a mortgage and those purchasing a loan. Neither Accent nor the CC offer an explanation for these apparent differences in willingness to pay between MPPI and PLPPI but one possible explanation is the different demographics of the two groups and that certain demographics of mortgage customers would be willing to pay to purchase at POS.

Finally, in addition to the distributional issues around which consumers are harmed, if the average willingness to pay does is significantly different from the willingness to pay of certain types of consumers, then using the mean in any welfare calculations will lead to biased estimates of the effect on overall consumer welfare. Hence examining how and where the burden of the POS ban will fall is important for getting an unbiased estimate of overall consumer welfare.

2.3.5 *Differentiating the impact of misselling from inconvenience effects*

The CC goes on to suggest that any reduction in sales from the POS ban could be due to the inconvenience factor but also due to consumers not being missold PPI. One simple way to test this would be to examine consumer preference around the timing of PPI purchase excluding those who felt they had been somewhat pressurised (15 of the 710 respondents).²⁰ Removing this group from the analysis would give a clearer view of what the pure effect of the POS ban is on consumer welfare. It is not clear why the CC has not undertaken this analysis and RBSG considers that it is inappropriate for the CC to simply equate those who do not buy PPI following a POS ban with those who may have otherwise been missold PPI. RBSG also suggests that to the extent that there is any misselling now, then surely that risk potentially remains even with a POS ban in place and so should not be incorporated into these results.

2.3.6 *Implication of using the survey results to estimate the costs of a POS ban*

The CC states that the model they use to assess the costs and benefits of the POS ban accounts for the loss of convenience²¹. However there are several conceptual problems with the application of the survey evidence to arrive at the conclusions found by the CC:

- The choice offered by the survey, as stated above, did not give consumers the option to not purchase. Instead it offered an alternative PPI product. If there is a POS ban then the real choice faced by consumers would be to not

²⁰ Accent (2010), 'Consumer Attitudes to Payment Protection Insurance Report', April, p 31.

²¹ CC PPI Market Investigation: Remittal Provisional Decision, 14 May 2010, p. 101 para 9.71.

purchase or to wait 7 days/24 hours. Had a “no purchase” option been offered in the survey then the choice set would have better matched the real choice faced by consumers, many of whom may not purchase instead of waiting for 7 days/24 hours. This omission may bias the valuations from the survey and means the implied elasticity is relative to the consumer choosing to delay their PPI purchase and therefore not the correct elasticity to evaluate how many customers would not purchase.

- Neither the CC's model nor the survey have taken into account how valuations vary by type of consumer. Those consumers who need PPI the most are also likely to be those who have the highest willingness to pay to retain the option to purchase at POS to ensure they receive the benefit of PPI.
- As well as being potentially biased by the comments above, the price elasticity used to estimate loss of demand from inconvenience is averaged across all consumers. If the distribution of willingness to pay is not, in fact, a normal distribution then the answers provided by the model are likely to be skewed. It would be reasonable to expect the willingness to pay for PPI to vary with income, age and other demographic variables which describe a consumer's likely need for PPI. In order to estimate the effects of the POS ban it is likely to be important to consider how the effects will be distributed across different demographics and to value the effects of removing the ability to buy at POS differently.

RBSG therefore considers that the above concerns should be sensitivity checked. The existing approach provides an indirect measure of how many consumers would not purchase relying on certain assumptions about the shape of the demand curve for PPI and the behaviour of consumers. If these findings are robust they would be consistent with an alternative direct method of estimating how many consumers would not purchase PPI. Direct methods of estimating the inconvenience effect could be in the form of a simple survey asking what people would do if PPI were not available or from running controlled experiments at two or more locations where POS ban for PPI is removed from one set of stores but not another and the differences in behaviour observed.

In addition, the CC's welfare analysis may also have implicitly double-counted the impact of a higher degree of price-competition, post-remedies. In its model of welfare impact, the CC incorporates, among others factors, the following two factors:

- (i) the value attached to delay: the CC measures the convenience benefits (and costs) of different consumer groups following a POS purchase in terms of valuations people attach to their preferences. These valuations may reflect a number of factors including what consumers expect to gain from having more time to shop around;
- (ii) the consumer gain from a higher degree of competition and lower prices are also accounted for separately by assuming that providers will earn normal profits after the implementation of the remedies and prices will be equal to costs.

The first factor i.e., the willingness to pay for purchasing PPI later includes the expected gain from shopping around which in turn depends on the extent of price competition. By incorporating both the value attached to buying PPI later as well as

the lower prices, the CC seems to have (at least partly) double-counted the benefits of competition.

Given these issues, in RBSG's view it does not seem reasonable to conclude that the benefits of a POS ban outweigh the costs.

3 A POS ban is not proportionate

Taking all of the above into account, RBSG considers that a POS ban is disproportionate to the AEC in question and, bearing in mind consumer preference, the CC should not impose a POS ban as part of the remedy package. To the extent that the CC does not consider that the original remedy package, less a POS ban, is sufficient to address its concerns, then a number of other remedies could be included. For example:

- (i) A requirement for a "clear-break" between the credit sale and PPI sale as suggested at paragraph 6.17 *et seq.* of the Remittal Provisional Decision.
- (ii) In addition to the "clear-break" in the sales process, all policies could be annually renewable. RBSG considers that an "opt-out" approach to renewal is preferable because customers will not be left without cover in the event that they forget to renew their policy but clearly there would need to be an obligation on providers to contact customers reminding them that their policy is due for renewal, so as to avoid passive renewals.
- (iii) Providers must ensure that their products can be sold on a stand-alone basis.
- (iv) Finally, and in order to ensure that the POS advantage is fully addressed by the clear-break sales process, the CC could increase informational requirements in order to ensure that customers are made better aware of their right to cancel their PPI product in the cooling-off period.²² For example, the CC could require that firms make cancellation even easier for customers, e.g. by including a phone number or other contact details very prominently on all policy documents which a consumer can use to conveniently cancel a policy. RBSG submits that this unknown threat of cancellation would mean that firms would work hard to: (a) ensure that their products are good value and competitive in order to retain customers; and (b) market themselves to rivals' customers, for instance, in order to win back business lost during the cooling-off period. This would lead to a more dynamic stand-alone market yet would allow the majority of customers who do want to buy PPI at POS to do so, would ensure that there is no protection gap for those who want to have the benefit of cover from the outset, and will also encourage customers to shop around for a better deal elsewhere.

RBSG considers that this remedy package would easily address each of the remaining features of the AEC. Failure to compete is addressed through the requirement to provide a standalone product and customer awareness of the cooling-off period/ability to cancel the product. Barriers to search are addressed by the informational remedies, the clear-break in sales process, the cooling-off and the cancellation opportunities. Barriers to switching are addressed by the informational remedies, the annual renewal remedy and a customer's right to cancel. And finally the POS advantage is addressed by the informational remedies, the clear-break in sales process and the cooling-off period. As such, RBSG submits that this remedy package would be an effective substitute for the POS ban. Such a package avoids the detriment of the 2009 remedy package which denies those who want to buy PPI at the

²² At present, under FSA rules, PPI customers are entitled to cancel within 30 days of receiving policy documents but of course firms could extend the duration of the cooling-off period if customers are likely to shop around beyond 30 days.

same time as credit the opportunity to do so, which of course risks leaving customers who need cover without it.

4 Conclusion

RBSG considers that the POS ban goes too far. The 2009 remedy package addresses an out-of-date view of the market, and relies upon a narrow set of facts to find a net welfare benefit. As illustrated in Section 2, RBSG considers that a POS ban will result in a minimal consumer benefit at best, and possibly a net consumer detriment. While RBSG recognises that if all else holds true in the CC's analysis a net consumer benefit could be achieved, when the majority of customers prefer to purchase protection at POS, when the market structure gives customers freedom of choice over their purchasing decisions and when the market structure allows a customer to benefit from immediate protection (and to change their mind after buying), then any structural change must offer a more certain and positive outcome than is offered by the POS ban and must be capable of guaranteeing consumers a better deal.

If the CC presses ahead with a POS ban, RBSG suggests that a more proportionate approach would be to pursue a two-stage remedy process. The first stage would be to introduce the 2009 remedy package less the POS ban to see whether the other remedies are sufficient to address the harm identified in the market or whether a POS ban is really necessary. If having tested the effectiveness of the other remedies over a sufficient period of time the CC still considers that on balance further intervention is needed then it may subsequently decide to introduce a POS ban. However, should the CC decide to re-impose a POS ban from the start of the remedies process then, given the significance of a POS ban, RBSG considers that the CC should keep the outcome of the ban under careful review, with the option of withdrawing the POS ban if the perceived benefits to consumers are not realised within an appropriate period of time.