Policy Statement

10/12

Financial Services Authority

The assessment and redress of Payment Protection Insurance complaints

Feedback on the further consultation in CP10/6 and final Handbook text

August 2010

Financial Services Authority

Contents

1 Executive summary 3

2 The rationale, cost and scope of our package of measures 9

3 Our Handbook provisions on assessing and redressing PPI complaints 39

4 Implementation and monitoring 56

Annex 1: Our cost-benefit analysis and assessment of other costs and benefits of our measures

Annex 2: Compatibility statement

Annex 3: List of non-confidential respondents to CP10/6

Appendix 1: Final Handbook text

Appendix 2: Material (including examples) supporting the Handbook text

Appendix 3: The implications of the Consumer Credit Act for our redress approaches

Appendix 4: Open letter, listing common PPI sales failings, with a mapping to our Handbook provisions

This Policy Statement reports on the main issues arising from Consultation Paper 10/6 (*The assessment and redress of Payment Protection Insurance complaints*) and publishes final Handbook text.
Please address any comments or enquiries to:

Julian Watts
Conduct Risk
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7066 1046
Fax: 020 7066 1047
E-mail: cp10_6@fsa.gov.uk

Copies of this Policy Statement are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

1 Executive summary

Purpose

1.1 Following Consultation Paper 09/23,[1] in Consultation Paper 10/6[2] we further explained the need for our proposed measures and sought further views on the justification for, and content (as amended) of, our:

- proposed Handbook text and supporting material concerning the fair assessment and, where appropriate, redress of Payment Protection Insurance (PPI) complaints;
- statements on root cause analysis and firms' obligations toward non-complainants potentially affected by recurrent sales problems;
- open letter that listed common failings in PPI sales; and
- estimate of the costs and analysis of the benefits of our proposed Handbook text, and estimate of the wider impact of our package of measures (in particular from some firms' potential reviews of non-complainants' sales).

1.2 This Policy Statement (PS) reports on the responses we received to the further consultation, and on the decisions we have reached in light of them, including final Handbook text.

Background and strategy

1.3 Our package of measures stemmed from our serious concerns about:

- widespread weaknesses in previous PPI selling practices and the detriment such selling was likely to have caused to a significant number of consumers; and

1 CP09/23 *The assessment and redress of Payment Protection Insurance complaints* (September 2009)
2 CP10/6 *The assessment and redress of Payment Protection Insurance complaints – feedback on CP09/23 and further consultation* (March 2010)

- the industry's poor handling of the increasing volume of PPI complaints, and its neglect of root cause analysis and fairness obligations toward non-complainants.

1.4 We anticipated our package of measures would lead firms to:

- handle PPI complaints more fairly and consistently, benefiting consumers who may have been mis-sold PPI and who complain, and reducing the heavy burden of cases on the Financial Ombudsman Service (FOS); and
- deliver fairer outcomes to consumers who may have been mis-sold PPI but who have not complained.

1.5 We emphasised that this package of measures should be seen in the context of our wider strategy and work concerning weaknesses in past PPI selling practices, which includes:

- 24 enforcement actions against the mis-selling of PPI, which have imposed fines totalling £12.6m;
- agreeing past business reviews in a number of the enforcement cases;
- several major firms delivering appropriate past business reviews of single premium PPI sold face to face with unsecured personal loans;
- our pursuing targeted sales assessment work in the credit card and second charge mortgage PPI markets; and
- examining the new generation of protection products now being developed to supplant PPI and the risks these may bring and, where necessary, robustly challenging firms on these.

1.6 We would also note the industry-wide steps we have taken to improve PPI outcomes for consumers including:

- securing industry agreement to not include nil refund terms in contracts with new customers and not apply such terms in contracts with existing customers;
- securing industry agreement to stop selling single premium PPI with unsecured loans;
- feeding into and supporting the package of measures being implemented by the Competition Commission in the PPI market; and
- securing agreement with the Mortgage Payment Protection Insurance sector to proactively refund increases in premiums and reverse reductions in cover for customers who experienced these changes to their policy in 2009.

1.7 All our interventions in PPI, whether addressing past mis-selling and unfair post-sale behaviour, or securing improved sales practices, reflect the strategic importance we attach to retail conduct and the principle of Treating Customers Fairly.

Responses to our consultation

1.8 We received 34 responses to CP10/6. In Annex 3 we list respondents who did not ask for their responses to remain confidential.

1.9 Responses from consumer representatives expressed concern at the delay to delivering improved consumer outcomes that the further consultation entailed, but mainly supported our:

- proposed material on PPI complaint handling as fair, relevant and practical, and likely to lead to a fairer outcome for PPI complainants;
- proposed 'comparative redress' approach, and the scope it would give many complainants for maintaining their PPI cover if they so wished (although some expressed doubts about our proposed increase in the referent price from £6 to £9 per £100 of cover); and
- statements on firms' obligations to consider the position of non-complainant consumers who may have suffered detriment from recurrent PPI sales failings.

1.10 Industry responses mainly remained critical of our amended proposals, and generally reasserted, and in places amplified, previous criticisms by saying we have:

- not demonstrated there was a genuine problem concerning PPI sales or PPI sales complaint handling (having inappropriately and retrospectively raised our expectations of what was required at the point of sale);
- proposed a solution concerning PPI sales complaints handling that was inappropriate and disproportionate for the PPI industry as a whole or for its various sectors;
- still underestimated the costs of our solution and overstated its likely benefits;
- made inappropriate statements about firms' obligations concerning non-complainants who may have been mis-sold, which imply an excessive and disproportionate cost to industry; and
- underestimated the possible wider prudential impact on the industry of the costs from our measures.

Industry responses also criticised us for:

- proposing revised guidance on PPI complaint handling that:
    - is not balanced about the assessment of evidence about a complaint;
    - contains flawed presumptions about how the consumer would have acted if a failing by the firm had not occurred;
    - takes inappropriate and unworkable approaches to redressing upheld complaints (including setting an inappropriately low referent price); and
    - has an impractically short implementation period; and for

- conducting a further consultation that remained procedurally inadequate, including because it gave insufficient time or information to allow proper responses.

In addition, some industry responses continued to query the lawfulness of some aspects of our proposals.

Outcome of our consultation

1.11 After considering the responses to CP10/6, and carefully weighing the potential impact on the industry and consumers in light of our statutory objectives, we have concluded we should press forward with our measures in order to protect consumers, but with some amendments that will address some of the industry's concerns that we believe are well founded. Overall, we have concluded that:

- we have made a reasonable analysis of the benefits, and a reasonable estimate of the ranges of costs and of the wider impact, that may arise from our final measures;[3]
- the rationale for our final measures is sound, their scope appropriate, and their likely impact fair and proportionate, despite the large cost implications for industry;
- the overall PPI strategy, of which our final measures form a key part, remains appropriate and necessary to address significant consumer detriment;
- our approach to consultation has provided more than adequate information on our thinking and eventual proposals, and has given stakeholders ample time and opportunity to apprehend and comment upon them;
- we should stand by and retain the open letter having amended:
  - o the failing concerning the inadequate disclosure of terms concerning cancellation during the cooling-off period;
  - o the failing concerning inadequate disclosure of non-pro rata refund terms; and
  - o the text concerning 'clear, fair and not misleading communication' in the context of face-to-face and telephone sales;
- we should issue final Handbook text on PPI complaint handling, implementing our approach to assessing evidence and to redress largely as proposed, but with amendments that include:
  - o new text recognising that, in some limited circumstances, it may be open to firms to remedy a sales failing in a different way from the approaches we have set out (and we give examples);

3 Our final estimates are that the cost to industry (over the next 5 years) of our Handbook provisions on PPI complaint handling is c.£0.8bn-£1.3bn, and that the cost to industry of our wider package of measures (mainly concerning own initiative actions by some firms towards non-complainants) is c.£1.1bn-£3.2bn. Note these two ranges of costs are not strictly additive. These final estimates compare to the estimates in CP10/6 of c.£0.7bn-£1.2bn and c.£1.0bn-£3.0bn respectively. See Annex 1 for details.

- o Evidential Provisions (rather than Guidance) concerning the determination and, where appropriate, redress of a sales failing (as a type of rule, these are more likely to change firms' behaviour in the way we consider necessary);[4] and
- o new text that confirms our expectations concerning firms' obligations toward non-complainants potentially affected by recurrent sales problems, including firms taking fair and proportionate own initiative action toward them where necessary (and we give examples).

Other potential measures in our package

1.12 In CP10/6, we set aside the rejected PPI complaint review rule we had proposed in CP09/23.[5] We do not discuss this further in this PS.

1.13 We are also considering whether we should seek (following consultation) to extend the time limit consumers have for referring a PPI complaint to the FOS following receipt of a firm's final response letter. This would extend the protection available for consumers who may have had their complaints rejected unfairly (and would potentially be a more general version of the temporary time extension we made for some complainants in May 2010). We will reflect on this potential measure (and also whether to allow the temporary time extension to lapse on its scheduled date of 27 October 2010) in light of developments over the coming months.

Who should read this PS?

1.14 This PS will be of interest to firms currently or previously active in the sale of PPI. It will also be of interest to relevant trade and consumer bodies.

Consumers

1.15 This PS will be of interest to consumers who have bought PPI and who have complained about its sale or are considering doing so, and to third parties representing them.

Structure of this paper

1.16 This PS discusses the main points made in response to CP10/6, and especially new or amplified points (compared to those made in response to CP09/23). It sets out our views in response and our final decisions.

- Chapter 2 discusses the rationale, cost and scope of our measures.
- Chapter 3 discusses our final Handbook provisions on PPI complaint handling, including approaches to redress.
- Chapter 4 discusses implementation dates for firms and our intended monitoring of compliance and consumer outcomes in the future.

---

4 But note that the evidential provisions should be treated as guidance for complaints about sales conducted before FSA regulation began (14 January 2005) – see para 3.49.

5 See CP10/6 para 1.8.

- Annex 1 discusses our analysis of the costs and benefits of the Handbook provisions and our wider measures.
- Annex 2 contains a statement of the compatibility of our measures with our statutory objectives and the principles of good regulation.
- Annex 3 lists non-confidential respondents to CP10/6.
- Appendix 1 contains the final Handbook text on the assessment and redress of PPI complaints.
- Appendix 2 contains guidance, including examples, supporting the Handbook text.
- Appendix 3 contains material concerning the implications of the Consumer Credit Act for firms' implementation of our approaches to redress.
- Appendix 4 contains our open letter, a final version of its listing of common PPI sales failings, and a mapping of the failings to our Handbook provisions.

Next steps

1.17 We have extended the time available to firms for implementing our Handbook provisions concerning the assessment of PPI complaints (from one month, as proposed in CP10/6, to over three months from the publication of this PS). So firms need to have regard to the Handbook provisions from 1 December 2010.

1.18 We have also allowed that, unless there are particular imperatives to the contrary, any own initiative actions by firms toward non-complainants need not commence until six months after the publication of this PS (i.e. mid Q1 2011).[6]

6 Firms may of course choose to commence such actions sooner.

2 The rationale, cost and scope of our package of measures

Introduction

2.1 CP09/23 included:

- a consultation on proposed Handbook text and supporting material concerning the fair handling and, where appropriate, redress of PPI complaints; and
- statements on root cause analysis and firms' obligations toward non-complainants potentially affected by recurrent sales problems.

2.2 At the same time, to support these measures, we published an open letter listing common failings in PPI sales.[7]

2.3 Consumer representatives' responses to CP09/23 were very supportive, but those from industry were mostly negative (see CP10/6 para 1.13 for a summary).

2.4 Having considered these responses, and carefully evaluated the potential impact on the industry and the interests of consumers, in CP10/6 we put forward a somewhat amended version of our proposed complaint handling guidance, but also:

- further explained the need and justification for our proposed measures;
- set out a revised cost-benefit analysis of the proposed revised guidance and, in light of concerns about its cost to particular sectors of the PPI market, gave separate estimated redress figures for complaints about each of the main types of PPI;
- provided additional clarification and discussion of our statements on root cause analysis and firms' obligations toward non-complainants potentially affected by recurrent sales problems, and set out the costs that may arise from some firms potentially redressing mis-sold non-complainants;
- set out the main prudential impacts from our proposed measures; and
- re-cast our description of the failings in the open letter to align more closely with our Principles and rules, to avoid the misunderstandings (evident from industry responses) around the previous formulation, and to make it clearer to firms how such failings have arisen.

7 www.fsa.gov.uk/pubs/other/trade_associations_ppi.pdf

2.5 We then asked:

> Q1: Do you consider that, taken as a whole, our package of measures – the proposed complaint handling guidance as revised and supporting materials,[8] and our statements on root cause analysis and non-complainants,[9] in light of our open letter and its recast list of common PPI sales failings,[10] and our estimates of the costs and wider financial impact on industry[11] – is a justified, appropriate and proportionate response to a genuine problem of PPI sales and complaint handling,[12] whose costs are matched or exceeded by its benefits?

> Q2: Do you agree that the open letter and its appendix,[13] lists common PPI sales failings under the relevant FSA Principles and rules since 14 January 2005?

> Q3: Do you agree that the general principles of fair conduct when selling PPI before 14 January 2005 have much in common with our standards after this date?

> Q4: Do you agree that our statements about our expectations concerning firms' treatment of their PPI non-complainants are appropriate in the context of Principle 6 and DISP 1.3.5G? Do you think there are particular circumstances concerning PPI which mean it would be unreasonable for us to expect firms to act towards PPI non-complainants in the way we have set out in our statements?

> Q5: Do you consider that it would be helpful for our statements about our expectations concerning firms' treatment of their PPI non-complainants to be added to our proposed Handbook guidance concerning PPI complaints?

2.6 Given that many responses tended to range across and link the answers to these questions, this chapter does likewise and discusses the responses and our own views of them mainly in terms of themes and issues, namely:

a) The open letter and our view of common PPI sales failings.

b) The rationale for our proposed measures.

---

8 CP10/6 Chapter 3 and Appendix 1 and 2
9 In CP09/23 and CP10/6
10 CP10/6 Appendix 3
11 CP10/6 Chapter 4 and Annexes 2 and 3
12 CP10/6 Chapter 2
13 CP10/6 Appendix 3

c) Our approach to PPI sales made before we regulated general insurance mediation.

d) Our view of firms' root cause obligations toward PPI non-complainants.

e) The costs and benefits and wider impact of our proposed measures.

f) The scope and impact of our measures for specific firms or types of PPI.

g) The position of secured lenders and secured loan brokers.

h) Our consultation process.

a) The open letter and our view of common PPI sales failings

2.7 Consumer representatives' responses approved of the open letter and its list of failings. However, many industry responses (but not all) argued that our perception of a problem in the selling of PPI and handling of PPI complaints depended on an incorrect view of the relevant sales standards. The main general criticisms from industry were that:

- we had not explained the Principles,[14] ICOB[15] or ICOBS[16] rules (or other legal sources) behind the 'common failings', precluding proper consultation on their correctness;
- our view of fair PPI selling practices had evolved significantly over the last few years, and we were now using the Principles inappropriately and retrospectively to 'back fill' the gaps or the lower standards in the detailed insurance conduct rules of the time, and thus unfairly imposing standards firms could not have predicted or complied with;
- the open letter takes no account of there having been regulatory developments such as ICOB and ICOBS where we had not taken the opportunity to make rules about such failings;
- the standards discussed in our previous thematic reports are, in many cases, inconsistent with the failings in the open letter;
- firms could not have known what they were supposed to do under the Principles in the context of PPI selling, because we did not explain our expectations (e.g. of what 'clear, fair and not misleading' meant); and
- breaches of Principles do not give rise to any liability towards a complainant.

14 Principles for Businesses module of our Handbook.
15 Insurance: Conduct of Business (ICOB) module of our Handbook, in force until 5 January 2008.
16 Insurance: Conduct of Business sourcebook (ICOBS) module of our Handbook, in force after 5 January 2008.

Our response:

The consultation on the open letter failings

The onus is on regulated firms to understand (and abide by) the regulatory and legal system in which they operate. We do not accept that our interpretations are obscure or that regulated firms, which are required to be familiar with our rules, cannot readily understand the requirements placed on them. The perceived lack in our consultation of detailed mapping of the failings to our Principles and ICOB and ICOBS rules has not prevented firms commenting in detail on whether specific failings were appropriate, in general or for particular time periods (see for example the criticisms of specific failings discussed below). The failings are readily referable to ICOB and ICOBS rules and the Principles and these are publicly available and not information that only we hold. However, to assist industry going forward, **we include in the final listing of the failings a mapping of them to our Handbook provisions** (see Appendix 4).

FSA reliance on the Principles

We do not agree that our other rules and guidance should be viewed as exhausting the implications of the Principles themselves, or that it is inappropriate for us to rely on the Principles even where there are detailed rules, and we consider that we dealt with this point in CP10/6 (see p11).

The application of the failings over time and regulatory developments

We do not agree that the failings are being applied retrospectively. We remain of the view that for the period of relevant FSA regulation (January 2005 onwards) the open letter reflects standards that applied throughout the period, because of the operation of the general law, FSA Principles and/or rules (we discuss the pre-2005 period below). Where relevant, the open letter text reflects where the standards differed under ICOB and ICOBS (see e.g. failings 2 and 12).

We do not accept the criticism that because we did not take the opportunity of the introduction of new sourcebooks (ICOB, then ICOBS) to make rules against particular adverse behaviours, such behaviours cannot really have been failings at that time. It is a fundamental aspect of outcomes-focused and Principles-based regulation that the Principles apply in situations where the need for a detailed rule or guidance has not been established. The onus remains on firms to comply with the Principles.

The failings and thematic reports

We do not accept that our previous thematic reports on PPI are inconsistent with the failings in the open letter. The thematic reports published in November 2005, October 2006 and September 2007 consistently identified unacceptable outcomes now set out in the open letter. For example, all three reports identify pressurised sales (failing 1) as an example of poor practice. Also, in all three reports we identified as a key concern the fact that many firms were still not giving customers clear information during the sales conversation about whether PPI is optional (also failing 1). In all three reports, we said that firms needed to improve information given to customers about whether or not the sale was on an advised or non-advised basis (failing 9). Relevant poor behaviours (many of them now set out in the open letter) have also been flagged up by us in other published supporting material, such as

Dear CEO letters, speeches and enforcement final notices.

The fact that not all the failings were always set out in every general communication where they might have been relevant does not undermine their correctness or our assertion of them now in support of consumer protection. (See also the discussion at para 2.28.)

FSA expectations under the Principles

We assist firms in understanding the regulatory system, for example, by publishing supporting material (such as Dear CEO letters, results of thematic reviews etc), and by giving general or individual guidance. However, regulated firms have the primary obligation to understand the regulatory and legal systems in which they operate.

Using an example given in response to our consultation (that we did not explain 'clear, fair and not misleading'), on even a quick search firms would find a range of material on our external website regarding our interpretation of the 'clear, fair and not misleading' requirements.[17]

Principles and liabilities

We do not agree that breaches of the Principles do not give rise to liabilities, and consider that the complaints handling rules do require a firm to uphold a complaint and pay appropriate redress when the conduct in question was in breach of the Principles.

FSA Principles are vital, concerning PPI and more generally, in enabling our complaints rules to support the jurisdiction of the FOS in deciding cases on a "fair and reasonable" basis. Our complaint resolution rule (DISP 1.4.1R) provides that, in respect of a complaint it receives, '*a firm must assess fairly…whether the complaint should be upheld [and] what…redress… may be appropriate…taking into account all relevant factors.*' Guidance on the section (DISP 1.4.2G) provides that *'factors that may be relevant in the assessment of a complaint… include…relevant guidance published by the FSA…[and] the Financial Ombudsman Service… and appropriate analysis of decisions by the Financial Ombudsman Service.'* When determining a complaint, the Ombudsman must take into account relevant FSA rules, and therefore the Principles (DISP 3.6.4R).

Three key points can be derived from these provisions. (a) First, when resolving complaints, the test to be applied by firms is expressed in terms of what is fair and appropriate. That is a wide and flexible test. (b) Second, when resolving complaints, firms should have regard to all relevant factors, which clearly if not expressly include FSA Principles and also relevant guidance and decisions of the FOS. Complaints are not merely to be dealt with on the basis of an analysis of whether the firm had a legal liability to the customer. (c) Third, this is consistent with requiring firms to have regard to FOS decisions, because the FOS decides cases (at least in

17 For example: A speech (by Tony Katz) of 28 November 2007 titled '*Financial Promotions and More Principles-based regulation*' goes into how the FSA interprets the fair, clear and not misleading requirements. www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/1128_tk.shtml

In the financial promotions '*How we regulate*' sections, there is a heading 'Key issues for firms to avoid', which shortly goes into what 'not misleading' means. www.fsa.gov.uk/Pages/Doing/Regulated/Promo/regime/regulate/index.shtml#key

Report 'Fair, clear and not misleading – review of the quality of financial promotions in the structured investments products marketplace' (October 2009) www.fsa.gov.uk/pubs/other/fp_structured_review.pdf

'Communicating with clients, including financial promotions' section www.fsa.gov.uk/pages/Doing/Regulated/newcob/faqs/comms2.shtml

The TCF website also goes into the need to communicate / sell to customers in a way that is clear, fair and not misleading.

its compulsory jurisdiction) on the basis of what is, in the opinion of the Ombudsman, fair and reasonable in all the circumstances taking into account the Principles and not by reference to a strict analysis of whether the firm has a legal liability to the customer.

Although we chose, at N2,[18] to switch off the right for consumers to bring an action in damages for breach of the Principles, there was no intention to remove other regulatory aspects of the Principles, such as their relevance to complaints handling by firms or for restitution actions by the FSA to obtain redress for consumers under s.382/384 FSMA.[19]

<u>Conclusion</u>

We consider it right and important to see the Principles as creating obligations on firms to comply with them, and as vital to delivering fair consumer outcomes.

As we have repeatedly set out, the essence of the Principles-based approach is that the focus is on setting out the purposive 'what' that needs to be achieved (in the retail context this is typically a particular outcome for a consumer), not the 'how'. This approach lets firms and us focus on what is important, and it gives appropriate responsibility to firms to deliver and comply in a way that best fits their business. This view is fundamental to our being a Principles-based regulator. It has formed the basis of numerous supervision and enforcement actions, which in many cases entailed the payment of redress to consumers.

In the PPI context, omitting failings from the open letter because of industry criticisms of their relationship to the Principles could undermine our efforts to address many acts or omissions by which firms have potentially caused detriment to consumers and may continue to do so. If, as we believe, too many firms selling PPI have failed to live up to the responsibility of delivering fair and appropriate consumer outcomes under the Principles at the point of sale, then we need to hold them to account for this.

To step back from the Principles would be bad for current and future consumers because it weakens their protection against poor outcomes, and bad for firms because we would need to be more prescriptive in rules and thus leave them less scope for flexible approaches in light of their own evolving business models.

2.8 Further general criticisms of the open letter made by some industry responses were that:

- Some failings are drafted in the form of outcomes for the consumer, not as duties owed by the firm, elevating our desired outcomes to a status they do not have.
- Many of the failings leave unclear the practical requirements in particular sales scenarios (e.g. concerning what we consider 'clear, fair and not misleading' means in particular channels of PPI sales).
- There have been various revisions of the failings, which raises uncertainty about what standards apply, and should lead us to reconsider, against the revised version, the thematic work, enforcement notices and mystery shopping exercises that contribute to our rationale for intervention.

18 The commencement of the Financial Services and Markets Act (2000) in December 2001.

19 See CP13 (September 1998) para 21. Also our discussion of Consumer Redress Schemes in Guidance Note GN10 (2010) e.g. paras 7.10-11.

Our response: We do not agree that some failings are drafted in the form of outcomes. They are drafted as common types of conduct that amount to a failure to comply with applicable requirements at the point of sale. They result in poor outcomes, and have been drafted in this way to remind firms of the appropriate standards. This has been recognised by some respondents.

We think the letter and failings are clear, and we have also detailed in the open letter examples of how the firm could have made a fair presentation of important information in the context of a face-to-face or telephone sale. However, for clarity, in the final listing of the failings (at Appendix 4), **we have amended the relevant text to more closely follow the wording of Principle 7.**

The revision of the description of some failings (in CP10/6 and the final version here) is a result of feedback received and our own further work. It demonstrates that we are open to representations, and where appropriate, have taken them into account and clarified the text. We do not consider that this revision impacts on our previous work in relation to PPI, such as our thematic work, enforcement actions and mystery shopping exercises. The failings are a summary of common types of conduct that we have observed during that work, and albeit the wording of some of the failings may have been slightly adjusted, the essence of the conduct we do not want to see in the sale of PPI remains unchanged.

2.9 In addition to these general criticisms of the failings, a number of the individual failings were specifically criticised by various industry responses:

i) There has not always been an obligation to draw specific attention to price or refund terms or certain other information in every sale.

Our response: As we noted above, firms' obligations toward their customers extend beyond those set out in specific ICOB or ICOBS rules. In dealing with customers, firms have also to comply with obligations set out elsewhere, for example, in the Principles and the general law.

In particular, Principle 7 requires firms to pay due regard to the information needs of their clients and communicate information to them in a way that is clear, fair and not misleading. In sales primarily conducted orally, it is not enough just to provide important information in writing. There should be a fair presentation of the information to the customer during the sales discussion, by, for example, giving an oral explanation, or specifically drawing the customer's attention to the information on a computer screen or in a document and giving the customer time to read and consider it.

We have amended the text of the failing concerning the non-disclosure of cancellation terms to reflect the fact that for most sales under ICOB, firms were specifically required to disclose to the customer before the sale was concluded the existence or absence of the right to cancel the policy and the duration of the cancellation period, and did not have to disclose that cancellation during the cooling-off period is without penalty. (In this context, we do not believe that the Principles alone required this latter information to be disclosed before the sale.) We have also changed 'contract' to 'sale', for consistency with the rest of the open letter.

ii) Firms did not have to consider the likelihood of a customer repaying their loan early or re-financing when advising on suitability – flexibility is not a relevant 'demand' or 'need' for the insurance and so there was no obligation to take it into account.

Our response: The suitability requirement is about taking reasonable steps to ensure that the product recommended by the firm is suitable for the customer's demands and needs. In order to be able to do so, the firm should seek all information about the customer's circumstances and objectives as might be reasonably expected to be relevant in enabling the firm to identify the customer's demands and needs. There are detailed rules under ICOB and ICOBS concerning the suitability assessment which are applicable to this situation. The requirement under Principle 9 to take reasonable care to ensure the suitability of advice is also relevant.

For single premium PPI, where the entire premium is paid upfront and where, for many customers, they would not get a pro-rata refund on cancellation, we consider that as part of the suitability assessment, the firm should establish a customer's need for flexibility and whether they might repay or refinance the loan before the end of its term. That is, we take the view that considering the likelihood of a customer repaying their loan early or re-financing, or more generally having the need for flexibility in exiting the contract, should be part of the firm's assessment of the suitability of single premium PPI for the customer.

iii) Disclosure of non pro-rata refund terms was never a regulatory requirement, and the agreement with the industry we reached in 2007 is the standard against which firms should be assessed. (Conversely, some consumer representatives' responses said that the failing concerning the disclosure of non pro-rata refund terms did not go far enough to protect consumers since there is *always* the prospect that a consumer will refinance a loan or choose to cancel a PPI policy, irrespective of their intention when the loan is taken out.)

Our response: As noted above, firms' obligations towards their customers extend beyond those set out in specific ICOB or ICOBS rules. For example, Principle 7 requires firms to pay due regard to the information needs of their clients and communicate information to them in a way that is clear, fair and not misleading. When considering a customer's information needs, the firm should take into account customers' general behaviour and information on that particular customer available to the firm at the point of sale.

We think this failing remains fair and appropriate because of the potentially significant financial consequences for the consumer of early cancellation. We would note that, as some industry responses have emphasised, many customers who buy this type of loan do refinance and cancel their policy before the end of its term when they do so.

However, we have decided, in light of responses and for the sake of clarity, to amend the text relating to this failing to reflect more closely the wording in the agreement reached with industry in 2007. The agreement reached with industry and accompanying statement by Clive Briault set out that '*Firms should consider whether they must draw the refund term to the customer's attention as a significant limitation of the policy as required in the policy summary*'.

If the firm concludes that information on non pro-rata refund is relevant, then the firm should disclose it to the customer. But if the information is not relevant at the time the policy is taken, then there is no need for it to be disclosed at the point of sale by the firm as it will not add to the customer's ability to make an informed decision.

In the context of a complaint about the sale of a single premium PPI policy, the onus is on the firm to show that it did give consideration to the information needs of the customer, and that it had good grounds for considering, in the case of each customer, that oral or other fair presentation of the term at the time of the sale was not required.

iv) There was never a rule that required the difference in the loan and policy terms to be disclosed and the consequences of this mismatch.

Our response: PPI policies are sold alongside loans with the intention of protecting the consumer from the risk of not being able to repay the loan. If the consumer is going to be protected only for some time rather than throughout the lifetime of the loan, then this should be made clear to him so that he can make an informed choice as to whether to buy the policy or not. This is particularly relevant where the cost of the cover is spread over the lifetime of the loan. We consider this is required under Principles 6 and 7 and, for advised sales, also Principle 9 and the ICOB and ICOBS rules on suitability. In addition, for ICOBS period sales, ICOBS 6.1.5R (ensuring customers can make an informed decision) and 6.4.9R (price information) are particularly relevant.

v) The failing relating to the inadequate transfer of risk under the policy should not discount life cover as it is widely recognised by consumers as a real benefit.

Our response: The cost of some Life Accident Sickness and Unemployment (LASU) single premium policies (particularly those added to a loan with a high interest rate and over a longer term) is higher than the benefits the customer can receive under the policy (or at least will in all probability receive under the ASU aspects of the cover). Firms argue that the life cover element of the product shows that actually the potential benefits payable under the contract are higher than the cost and therefore this is not an issue. Our view is that if a customer had truly understood the total cost of the cover compared to the extremely limited benefits from some policies (unless they die), they would not have purchased the product. We think that the fact that the balance between ASU cost and benefits is so finely balanced that a firm should use the inclusion of Life cover (which can usually be purchased separately much more economically) to justify the cost of the policy and its sale, supports our view.

vi) There was no previous indication that we expected oral disclosure of the main elements of the loan (i.e. the original loan and interest, the loan for the PPI premium and interest and the total amount payable).

Our response: We do not impose requirements on disclosure of the main elements of the loan. However, where the premium of the PPI policy is paid by way of a credit agreement taken out for payment of the premium or added to the main loan, then the customer should be told – or otherwise have brought to his attention – the interest that he will be paying on it; see in particular Principle 7, ICOB 5.5.14R and ICOBS 6.4.9R.

vii) It is unfair to expect firms to have provided total premium quotations before 2008 as this only became a regulatory requirement then; it cannot be required by reference to Principle 6, because we only gave specific guidance on it for sales made after 2008.

Our response: It has always been a requirement that firms should provide total premium quotations – see ICOB 5.5.14R and ICOBS 6.4.7G and 6.4.9R(2). The clarification we provided in 2008 concerning these rules does not change them or firms' obligation to the consumer, and so does not undermine the position of a consumer who complains to a firm or to the FOS (or in court) that they should have been told the total premium.

viii) The open letter should clearly differentiate between regular premium PPI and PPI charged as a percentage of an outstanding balance (e.g. credit card PPI and retail PPI).

Our response: Unless otherwise stated, the failings in the open letter apply across all types of PPI sales. Where we thought it appropriate, we have grouped the failings. As such, failing 9 applies only to non-advised sales; failings 10 and 11 apply only to advised sales; and failings 10 (in part), 13, 14 and 15 apply only to single premium policies. But we consider that the applicability and implications of the relevant failings for different regular premium structures are sufficiently clear as they stand.

2.10 In summary, we stand by the open letter and the failings it sets out (as amended).

b) The rationale for our proposed measures

2.11 Consumer representative responses strongly supported our rationale for action and urged us to proceed swiftly. However, many industry responses, in addition to their criticisms of the content of the open letter and its role in our proposed measures, made a number of other criticisms of our stated rationale in CP10/6. The main lines of this industry criticism were that:

a) we had not adequately made out the case for there being a widespread PPI sales problem, as even if the sales failings in the open letter are correct, they were found among firms subject to enforcement and mostly prior to ICOBS, which does not necessarily demonstrate that those failings were widespread or a current problem;

b) we had not adequately made out the case for there being a link between PPI selling practices and large and growing PPI complaint numbers; and

c) our proposals try to remedy problems in conduct of business via complaint handling, which is inappropriate, and do so, moreover, without having shown that there is a genuine problem with complaints handling, since:

   i) none of our mystery shopping, thematic work or enforcement actions relate to complaints handling, only selling, and our own analysis of PPI complaints decisions made by firms is inadequate;

ii) the high overturn rates at the FOS were not universal across all market participants; and

iii) our reliance on FOS decisions is under-researched and flawed, as FOS decisions themselves are flawed, both in the standards they apply and their inconsistency over time.

Our response:

Is there a widespread problem with PPI sales?

Since 2005 we have gathered, over several years and phases of work, wide and deep evidence of weaknesses in PPI sales practices across the market – see the table and text on p 9 of CP10/6 concerning our firm visits and findings, our mystery shopping exercises, and enforcement actions. We would add that the November 2005 mystery shopping exercise saw 52 shops completed across 19 firms, and the September 2007 exercise saw 114 shops completed over a smaller number of firms. A majority of the shops in both exercises had at least one failing identified and many of them had more.

We would also note (and have had regard to) relevant findings from the Office of Fair Trading (OFT) and Competition Commission (CC). For example, the CC report of January 2009[20] noted among other things that the cost of PPI was being presented in a way which was having a detrimental effect on consumers' ability to understand pricing information, and also that significant numbers of consumers perceived either that PPI take-up would have a positive influence on their credit application or that it was a condition for taking the credit. More generally, the CC report noted its survey findings from 2007[21] which concluded that there was a considerable amount of customer confusion on product features and benefits. These findings from the CC give weight to our view that identified weaknesses in PPI sales practices were translating into actual poor outcomes for a significant number of consumers.

Is there a link between large and growing PPI complaint numbers and PPI selling practices?

As noted above, our extensive work on PPI sales has provided extensive evidence of poor sales practices across the PPI market, and other bodies have independently also expressed concern about and criticisms of the PPI market and its practices. In that context, it is not unreasonable for us to have reached our own view that there is a prima facie link between growing complaints and a widespread problem with sales of this product.

We disagree with some firms' efforts to lay rising complaint numbers solely at the door of third party claims management companies (CMCs). That complaints may often have been prompted by the adverse publicity about PPI does not mean they are spurious. It may well mean instead that adverse publicity has made consumers more clear and informed about PPI than did firms' (often deficient) disclosures, and so aroused consumer concern and dissatisfaction, leading them to complain (see CP10/6 p 9-10). Our experience indicates that CMC involvement tends to proliferate where there are consumer doubts about the fairness of firms' complaint handling, as with mortgage endowment and bank charge complaints previously.

We would have been less concerned about the PPI complaint numbers if most of them had turned out to be unfounded, either because no sales failing had taken place, or because such failings as had occurred had not caused the consumer any detriment. However, the

20 *Market investigation into payment protection insurance*, Competition Commission (29 January 2009)

21 Survey conducted by British Marketing Research Bureau

FOS has considered over 60,000 PPI sales complaints and has upheld the great majority of them (over 80%) in favour of the consumer, nearly always with an award of redress. In our view, this demonstrates that there is a genuine link between widespread weaknesses in sales practices, poor consumer outcomes, and actual consumer detriment.

Further, as we noted in CP10/6: *Dialogue and correspondence with firms and trade bodies about their views of sales standards has only strengthened our view that there is an underlying problem with many firms' PPI selling practices,...and that rising PPI complaint numbers are symptomatic of this problem.*

One industry response objected to this weight we had given to statements made by firms in dialogue with us, seeing it as inappropriate and as likely to reduce candid exchanges of views between industry and regulator in the future. However, we do not see how or why we ought not to take into account what industry has said to us about likely non-compliance. Moreover, firms have an obligation to deal with us in an open and cooperative way under Principle 11. (We recognise that firms' statements in this regard reflect their view that their sales only fail against the inappropriate standards they believe we are imposing, views we have considered as part of the consultation.)

Overall therefore, responses have given us no cause to depart from our view that:

- there are genuine widespread weaknesses in sales practices across the PPI market;
- much of the large volume of PPI complaints about such sales reflects sincere consumer dissatisfaction, not opportunism (which is not to say dissatisfaction necessarily means there was a mis-sale); and
- some significant proportion of this dissatisfaction reflects genuine poor outcomes and detriment to consumers caused by many firms' sales practices.

Does there need to be a problem with complaints handling?

We have been concerned to address the significant potential consumer detriment caused by weaknesses in firms' PPI selling practices. Some consumer stakeholders have called for an industry-wide review of past PPI sales under s404 of FSMA ('Review of Past Business') to do this. But we have followed a strategy that we consider swifter and more proportionate, consisting of the package of measures discussed in this PS and various other actions (set out in paragraph 1.5).

By their nature, problems in the conduct of business will generally cause potential detriment to consumers. We are also clear, despite what the industry says, that using a complaints-led approach as a key part of remedying such detriment is a reasonable regulatory approach, and that sales and complaints about sales should not be perceived as two separate and unrelated domains. A complaints-led approach to addressing mis-selling is one we have taken before (e.g. with mortgage endowments) and, as noted, it is an alternative to other tools for addressing mis-selling such as a s404 review of sales.

We would assert therefore that, *in principle*, a complaints-led approach could reasonably be deployed by us as an appropriate and reasonable regulatory tool even absent any evidence of unfair complaint handling.[22] If, instead, we had always to establish separately

22 For example, we can envisage situations in which we identify early, through our own work and/or intelligence from the FOS or other sources, and before many consumers have actually complained, some significant extent of mis-selling, and decide to set out complaint handling guidance in anticipation of future complaints about the issue, as the best and most proportionate tool for redressing that mis-selling and ensuring consistent consumer redress outcomes.

that in addition to an apparent mis-selling problem, there was a crystallised problem with relevant complaint handling, then this would potentially prevent us from deploying such a complaints-led approach in a swift and timely way.

Is there a genuine problem with complaints handling?

In practice, for a complaints-led approach to remedying potentially widespread mis-selling to be *effective*, and for consumers to get fair outcomes from it, it is clearly *of the essence* that firms act fairly, effectively and consistently when handling complaints and considering non-complainants.

We have serious concerns that many firms have not been doing this for PPI complaints, even as their number grew rapidly. Despite industry criticisms, we remain of the view that we do have strong evidence of complaint handling failings, not just of sales failings.

One important ground for our serious concern about firms' PPI complaint handling, to which we have attached weight, is the difference between firms' decisions on PPI complaints (majority rejected) and the FOS's decisions (most upheld for consumers), and the consequent inconsistency in complainants' outcomes. While it is true that the proportion of firm decisions over-turned by the FOS was not equally high for all firms or all sectors of the PPI market (which we discuss further below), the proportion was very high for many firms covering a significant proportion of the market. In our sample of reporting firms, covering over 80% of the market (by gross written premium), over-turn rates at the FOS ranged from 33% to 99% in the period January-September 2009, but averaged 87% (in line with the FOS's overall over-turn rate of 89% for PPI sales complaints to firms in general).

In spring 2008, we wrote a 'Dear Compliance Officer' letter to 22 groups (covering 26 regulated entities) for whom PPI complaint numbers were significant. In each letter, we presented to the firm (from the statistical data available to us) its position relative to the rest of the peer group in terms of over-turn rate at the FOS, speed of handling and success in resolving PPI complaints (as opposed to building up a backlog of them). We also set out a number of considerations concerning the fair assessment of such PPI sales complaints, including about the assessment of evidence and of the firm's own behaviour at point of sale. We highlighted particular concerns to those firms who were weaker on the statistical measures, and we asked them to provide us with action plans for improvement. These were discussed and, where appropriate, challenged, during the summer of 2008.

During 2008/09, we also reviewed 131 PPI sales complaints files from four firms, of which 52 complaints were handled unsatisfactorily, results which further contributed to our ongoing concerns.

In addition, we would note:

- the intelligence we received from the FOS and other sources (e.g. Citizens Advice Bureau, Consumers Association), and from firms themselves (through dialogue, correspondence and complaints reporting), about firms' deficient approaches to PPI complaint handling (including their flawed view of applicable sales standards); and
- our findings on weaknesses in the handling of other types of complaints by some major banks, most of whom sold PPI.

There has been little sign of improvement in practice across the industry, or of improved consumer outcomes, as PPI complaint numbers continued to grow, firms' rejection rates remained high, and their 'overturns' at the FOS likewise remained high.

We would further note that we proceeded initially on the basis that industry (a number of trade bodies) had itself proposed PPI complaint handling 'industry guidance' as an appropriate solution to the concerns being expressed by various public bodies about poor sales practices and poor complaint handling. We proceeded to propose Handbook text when it became clear that industry could not agree on details or on an approach that was sufficiently robust and wide ranging to address our and other public bodies' concerns and to support a complaints-led approach to addressing PPI sales failings.

<u>Concerning FOS decisions</u>

We have had extensive discussions and correspondence with the FOS,[23] and these have helped us to understand the key themes that run through many of its PPI complaints decisions and its approach to assessing PPI sales.

We have looked at a sample of examples of FOS decisions, which confirm that the FOS has been making its decisions in a way generally compatible with the approach we have consulted on and finalised here. We have also examined the FOS policy and other materials on PPI complaints handling which it published in November 2008 and subsequently, which are consistent with and reflect the approach taken by the FOS in the decisions we have seen.

In addition, firms have criticised FOS decisions to us, and we have considered and discussed firms' concerns, both bilaterally with some and in the industry group discussions, and such discussions gave further intelligence about the FOS's approach.

We have not seen any convincing evidence to support the industry claim that the FOS significantly changed its approach after that published policy of November 2008. And in any case, we had evidence of, and were concerned about, the high rate of overturns firms were already experiencing at the FOS at end 2007 and through 2008, so it is clear the FOS's approach at that time was already identifying a high incidence of poor complaint handling and of consumer detriment from PPI sales.

The consistent tenor of our extensive discussions with the FOS, the industry criticisms of FOS decisions, and the FOS decisions on cases we have seen, is entirely consistent with the FOS's stated approach, which we have been able to evaluate in the round. We thus remain confident in our statement in CP10/6 that: *'our view of the relevant regulatory standards and conduct which falls short […] and the FOS's conclusions about individual cases […] are compatible.*[24] As such, we are confident that we are right to treat data and intelligence from the FOS as *one* important source of evidence (among others) for our concerns that firms are not handling PPI sales complaints fairly and as *one* of a number of factors to which we have attached some weight (alongside our own work) when deciding on our proposed measures.

<u>Conclusion</u>

Overall therefore, we consider that the rationale for the finalised measures we set out in this Policy Statement is sound and robust.

23 From time to time between November 2006 and spring 2008 (mostly in the context of discussions about what the FOS was seeing in the growing number of PPI complaints referred to it), and then intensively from summer 2008 to summer 2010, when we held detailed exchanges of views as we considered proposals from the industry and developed our own approach.

24 Note that we continued: '*Whereas there are a number of material differences between our view and much of the industry's view of 'point of sale' conduct and consideration of consumer needs and circumstances.*'

c) Our approach to PPI sales made before we regulated general insurance mediation (i.e. before 14 January 2005[25])

2.12 Consumer representative responses agreed that our measures certainly should cover complaints about these earlier sales. However, some industry responses variously argued that:

- it was especially inappropriate and retrospective to seek to apply the failings in the open letter to these sales;
- we should not seek to rely on thematic and other work done since January 2005 to cite a problem with sales made earlier;
- it was otherwise inappropriate and ultra vires for us to include in the scope of our measures complaints about these sales; and
- complaints about these sales should anyway be rejected as 'time barred'.

Our response

The open letter and pre-2005 sales

Prior to January 2005, the General Insurance Standards Council (GISC) Code and, prior to the GISC Code, the Association of British Insurers (ABI) Code, constituted the industry codes of good practice in relation to the sale of insurance. In addition, the provisions in common law such as the general duty of utmost good faith in insurance contracts and misrepresentation would also have been relevant at that time.

GISC members signed up to a series of commitments set out in the Code, which in our view had a similar effect to the obligations set out in the current regulatory system. For example, paragraph 1.1 of the Code set out that GISC members promise to '*act fairly and reasonably*' when dealing with customers. This is similar to FSA Principle 6 (treating customers fairly). Applying pressure to a customer to take PPI (failing 1) is undoubtedly a failure to act fairly and reasonably and as such is contrary to paragraph 1.1 of the Code as well as a breach of FSA Principle 6.

Another example is paragraph 1.3 of the Code which set out the GISC members' promise to '*give customers enough information and help so customers could make an informed decision before they made a final commitment to buy an insurance policy*.' This is similar in effect to FSA Principle 7, and also ICOB 2.2.3R, ICOBS 2.2.2R (which are the clear, fair and not misleading rules) and ICOBS 6.1.5R (ensuring customers can make an informed decision). Providing misleading or inaccurate information about the policy to the customer most likely would be in breach of GISC paragraph 1.3 in the same way that it would be a breach under the relevant provisions after January 2005. In addition, this could also amount to a misrepresentation under the general law, for example.

There will, however, be more specific failings that will *not* have a corresponding commitment in the GISC Code, for example, the failure to disclose '*price information calculated in a way to enable the customer to relate it to a regular budget*'. The GISC Code has commitments regarding provision of information on costs. However, they do not descend to this level of detail. The same applies for the general law, which may not necessarily require information on price in the specific manner described in this failing.

---

25 For brevity we refer to these sales as 'pre-2005 sales'.

We agree that the GISC Code in force before January 2005 only applied to GISC members, but a majority of firms selling insurance at that time were signatories to it. In any event, all firms were subject to the general law.[26]

Overall therefore, we consider that it remains appropriate for us to say in the open letter that the general principles of fair conduct when selling PPI before FSA regulation have 'much in common' with our standards.

As a further recognition of the particular position of pre-2005 sales, where we have now finalised much of our proposed complaint handling Guidance as Evidential Provisions instead, we say that the latter should be treated as Guidance for complaints about pre-2005 sales (see Chapter 3).

Is there a widespread problem with PPI sales before January 2005?

We did not regulate the mediation of PPI before January 2005, so we did not carry out thematic work on earlier sales and our *own* evidence about PPI sales practices before this date does not match the depth and breadth of our evidence about sales after this date. However, there was extensive evidence from other sources of poor PPI sales practices in the earlier period.

Already in 2004, before we had assumed regulatory responsibility for general insurance mediation, we had identified PPI selling as an area of concern and a priority for work by us as soon as we did assume responsibility. By 2005, the FOS, consumer bodies and the media had all expressed concerns about aggressive sales practices, poor value products and excessive product margins, unsuitable products, and small print and complex terms, where products are sold to consumers on the back of another transaction. We were aware of these various concerns and reports, which were factored into our risk assessment and policy work on general insurance, including in CP160 (2002) and CP187 (2003).

For example, in CP187 we referred[27] to a report by the Department of Trade and Industry's Over-indebtedness Task Force[28] and to the National Association of Citizens' Advice Bureaux super-complaint report to the OFT.[29] These reports date from 2003 and highlighted what these bodies perceived as problems with the sale of PPI, in particular that:

- terms and conditions of policies, including limitations and exclusions, are not explained to customers so they buy products they are not eligible to claim on;
- customers are not told the price of the insurance, because it is bundled into the cost of the loan;
- customers are not made aware that they have a choice whether to buy the insurance when taking out a loan; and
- staff are not trained to sell insurance.

26 If a firm was not a member of GISC at the time (and not already FSA authorised), then in most cases complaints about that firm's pre-2005 business will not be within the scope of DISP (and thus our finalised PPI complaint handling provisions) anyway. The existing complaints handling rules apply to the pre-January 2005 mediation of policies where the firm is FSA authorised post-Janaury 2005 and was covered by GISC at the time of the sale and the subject matter of the complaint would have been covered by GISC.

27 See paragraphs 4.12 to 4.14 of www.fsa.gov.uk/pubs/cp/cp187.pdf

28 *Taskforce on Tackling Overindebtedness: Second Report*, Department of Trade and Industry, January 2003 (www.dti.gov.uk/ccp/topics1/overindebtedness.htm).

29 *In Too Deep*, National Association of Citizens' Advice Bureaux, May 2003

CP187 also referred[30] to the results of the Consumers' Association mystery shopping exercise on PPI[31] which found that:

- unless prompted, none of the sellers asked about customers' pre-existing medical conditions;
- only a third of customers were asked about their employment details, despite the fact that part-time, contract and self-employed workers were generally not eligible to claim; and
- in 58% of cases PPI was automatically included in quotations for personal loans and in 33% of these cases the customer was not told that PPI had been included.

So the evidence at least suggests that there was a problem before January 2005 and a risk of poor consumer outcomes similar to those in later sales – which is consistent with our stance in the open letter that the general principles of fair conduct when selling PPI before FSA regulation had much in common with our standards. And this evidence is clearly important for the consideration of the potential consumer detriment arising, given that two thirds of PPI sales were made before January 2005.

The FOS estimates around *half* of the PPI complaints referred to it concern pre-2005 sales, and we have no reason to think (and firms have provided none in their responses) that this is significantly out of line with the proportion of PPI complaints to firms more generally.

Is there a problem with handling complaints about pre-2005 sales?

There is no indication that complaints about these sales have been handled any better by firms than those about later ones. The FOS estimates that its uphold rate in favour of consumers for complaints about these sales is no lower than the (high) rate for complaints about later sales. Of the complaint cases that we have reviewed (as outlined above), a significant minority concerned pre-2005 sales, and the decisions on these by firms gave us no reason to depart, in respect of such pre-2005 sales complaints, from our concerns set out above about firms' approach to handling PPI sales complaints more generally.

The appropriateness of including pre-2005 sales within our measures

Complaints about pre-2005 PPI sales (or other general insurance sales) are already within the existing scope of our DISP rules on fair complaint handling for most firms, and our final Handbook provisions on PPI complaint handling are not changing this. So it is quite consistent and appropriate that such complaints *should* fall within the scope of the final provisions.

However, it remains the case, as stated in CP10/6, that limitations on our powers concerning most PPI sales made before 14 January 2005 mean we cannot necessarily expect most firms to consider the position of non-complainants who were sold PPI before that date and may have been affected by recurrent sales failings on the part of the firm (see next section).[32]

30 See paragraphs 2.61 and 2.66 of Annex 2 of CP187
31 *Protection Racket*, Which? Consumers' Association, July 2002
32 See CP10/6 page 28 and Annex 3 p3 fn 8

Time barring and pre-2005 sales

Some firms argued that complaints about pre-2005 sales should not be included in the scope of our Handbook provisions because they are all or mostly already out of time to be considered on their merits (i.e. they are 'time barred' under our existing DISP rules).[33]

We disagree with this view. Decisions concerning the time barring of individual complaints are ultimately for the FOS to make, but in general terms, our view (as set out in CP10/6 para 3.14), is that general media coverage of the PPI issue, including comments or publications by us, would *not* be enough to have given a consumer the kind of specific 'constructive knowledge' required by DISP's time limits.[34]

Accordingly, while *some* consumers who bought PPI before January 2005 may, on an assessment of their individual circumstances and events, be deemed to have had appropriate awareness before January 2008, such that they will be out of time by January 2011, our view is that this is unlikely to apply to consumers generally (though that is ultimately a decision for the FOS to make concerning complaints referred to it).

Conclusion on pre-2005 sales

There is nothing in firms' responses which leads us to consider it necessary to retract from our statement in the open letter concerning pre-2005 sales or to carve out complaints about these sales from the scope of our final provisions. To do either would leave substantially unaddressed the poor handling of a very significant proportion of PPI complaints, and thus the significant potential consumer detriment caused by many of these sales.

d) Our view of firms' root cause obligations toward PPI non-complainants

2.13 In CP10/6 (p27), we noted our expectation, in general, and for PPI, that:

> *…if a firm is aware, from its complaints handling experience or otherwise, that there have been deficiencies in its past selling practices (or other behaviours), we would see it as appropriate (from Treating Customers Fairly considerations under Principle 6) for the firm to further consider the position of non-complainant consumers who may have suffered detriment from such failings. We would expect the firm to take fair and sensible decisions about whether, and what, action would be appropriate concerning this group of consumers. And it may then be appropriate for such own initiative action by the firm to include taking steps that potentially lead to the redress of the non-complaining consumers who have suffered detriment.*

33 DISP specifies that complainants will have the longer of 6 years from the event giving rise to the complaint (in this case the sale) or 3 yrs from when they knew (or ought reasonably to have known) that they had cause for complaint, in which to complain to the FOS. Firms may reject a complaint without considering the merits if they receive a complaint outside these time limits.

34 In our view, for a customer to be aware for the purposes of starting the three year time limit running for a potential PPI mis-selling complaint, they would need to have become, or been made, aware of both a potential problem with the sale of their policy and potential financial loss resulting from that. This is consistent with the approach we took to, for example, the time barring of mortgage endowment complaints.

2.14 Such statements (in CP09/23 and CP10/6) concerning firms' obligations (under Principle 6) towards non-complainants who may have been affected by any recurring sales failings that firms have identified through root cause analysis, are an important part of our complaints-led strategy for dealing effectively but proportionately with the consumer detriment caused by PPI mis-selling. As such, they have been mainly welcomed by responses from consumer representatives.

2.15 Industry responses, however, have variously raised three main objections to our statements:

- we are trying to use the provisions in DISP around root cause analysis and Principle 6 in lieu of a redress scheme under s404 of FSMA (a 's404 review'), which amounts to using them for a purpose other than those that were intended; or
- while our statements may be reasonable concerning Principle 6, they are inappropriate and disproportionate in the context of PPI because our retrospective application of new sales standards means most sales are non-compliant; and
- there is need for flexibility around firms' own initiative actions and it should be for firms to consider whether to (say) contact all non-complainants, in the light of Principle 6 obligations and considerations of proportionality.

2.16 We also consulted in CP10/6 on whether our statements concerning PPI non-complainants should be rendered into Handbook guidance. Some firms opposed this as unnecessary and/or disproportionate, but other firms felt this to be formally appropriate (even where they continued to reject the substance of our statements).

Our response

We do not agree that our statements are inappropriate and disproportionate in the context of PPI, because we do not consider the failings in our open letter to be new or retrospective (see section A above).

We do not agree that our statements amount to a wrong use of Principle 6 because:

- we have long set out, in Treating Customers Fairly publications and enforcement final notices, our view that such consideration and potential action towards non-complainants is what fairness requires; and
- this is very different from a s404 review since a firm will only have to act towards non-complainants if it finds recurring shortcomings in its own sales in the course of its own root cause analysis (which must be diligent and robust) of such sales (and complaints about them), whereas in a s404 review it would have to act towards non-complainants because it was included in the scope of the s404 review established in response to a widespread or regular failure by firms.

We agree (and had indicated in our statements in CP10/6) that there is scope for a firm to consider for itself what action, if any, would be proportionate concerning relevant non-complainants. But such action (or inaction) needs to be fair as well as proportionate.

To make this clear we have added Handbook guidance (as we proposed – DISP App 3.4.3G).

As further guidance to firms, we recognise that fair and appropriate measures are likely to differ from firm to firm and across different products and sales channels, but in considering fair and appropriate own initiative action in relation to non-complainants where firms know, or have information suggesting, that problems could have occurred in a cohort of sales, firms should have regard to what is proportionate in all the circumstances including:

- *the number, nature and seriousness of the problem(s) identified;*
- *the proportion and number of sales in which the problem(s) may have occurred;*
- *the proportion and number of consumers whose decision to purchase the PPI may have been impacted by the problem(s);*
- *the nature and severity of the potential (or known) detriment to such consumers;*
- *whether it is possible for the firm to identify, from information already available to it, which customers within a given cohort have been affected in this way; and*
- *the effectiveness and cost of actions which involve some form of customer contact exercise, or other alternatives, including:*
  - *their likely effectiveness in ensuring that all such customers are treated fairly by being given appropriate redress or a proper opportunity to obtain it; and*
  - *the ability of the firm to carry out such actions (for example, given its permissions).*

Note that in having regard to the foregoing, firms should conduct robust and representative analysis.

By way of illustration of some of the foregoing, we set out below two examples, featuring two broad scenarios which we consider likely to be of relevance in the PPI market, where a firm provides to non-complainants proper opportunity to obtain redress.

Example A

Where a firm:

- knows that it is likely that there is a significant proportion of sales (or class of sales) with a problem(s);
- knows that the problem(s) is of a kind which is likely to have impacted the decision to purchase the PPI of a significant proportion of those customers, independently of their individual circumstances;

  (e.g. the firm pressured customers into buying the PPI);
- does not know (and cannot find out from the information currently available to it) *which* sales had the problem(s);

– then the starting position is that it is likely to be fair and proportionate for the firm to conduct a consumer contact exercise which contacts the generality of relevant customers to explain the problem(s) and to give them a fair opportunity to have their sale reviewed if they are concerned. When reviewing the sale, the firm should apply our PPI complaint handling Handbook provisions and treat customers fairly.

Example B

In some other circumstances, other less penetrative approaches may be fair and proportionate. For example, a situation may arise in which the firm:

- knows that within sales (or a class of sales) there is a smaller proportion of sales with a problem;

  (e.g. *some operatives sometimes failed to disclose appropriately to customers the impact on cover of pre-existing medical conditions*);
- knows that the problem is of a kind which is not likely to have impacted the decision to purchase the PPI of a significant proportion of customers, because of their individual circumstances;

  (e.g. *the non-disclosure of the importance of pre-existing conditions may be likely to be material to their purchase decision only for those consumers who actually did have a pre-existing condition*);
- does not know (and cannot find out from the information already available to it) *which* sales had the problem or the customers for whom this was relevant; and
- has good grounds for thinking the problem was not generally accompanied by other problems.

In this case, and provided all of the particular facts of the situation are properly taken into account, the starting position may be that the firm may fairly consider that it would be more proportionate for it, instead of a customer contact exercise, to, for example:

i) adapt its complaint handling processes to ensure that, in assessing the complaint in accordance with our PPI complaint handling Handbook provisions, proper account is taken of the problem when considering customer complaints of a relevant type (see DISP App 3.4.2G.);

   (e.g. *by treating customer allegations that the pre-existing conditions were not disclosed as highly plausible and responding appropriately*);

ii) bring the problem to the attention of its claims departments, such that the problem is properly taken into account when handling relevant claims – compare DISP App 3.8.2E (though the scope for this will depend on the firm's permissions);

iii) provide a generic notification (e.g. on its website) concerning the potential failing and the firm's own initiative actions in response;

iv) take any other appropriate action.

Note that where a firm is not in a position, because of its permissions, to take some of the steps in these examples (e.g. it is not the insurer and so has no claims department), it will either need to come to some suitable arrangement with related firms party to the policy who do have suitable permissions, or else need to consider other approaches that would be fair and proportionate in all the circumstances.

Where a firm is pursuing an approach, it should monitor the results, and if these are less effective than anticipated in giving non-complainants proper opportunity to obtain redress, we would expect the firm to amend its approach or switch to a different, more appropriate one.

Note that the two examples above, and their scenarios, are by no means exhaustive, and in other scenarios that may arise in the PPI market, other stronger and more penetrative actions may be appropriate (for example moving directly to offers of redress to a specific set of non-complainants without a prior customer contact exercise).

2.17 We stated in CP10/6 that firms should communicate to us their conclusions on their assessment of failings and the potential need for own initiative action by them as soon as practicable, and that, where the firm considers that no redress or remediation exercise is required it should give us reasons for its conclusion.

2.18 However, we would prefer now to emphasise the importance of each firm's own responsibility to deliver fair outcomes and treat customers fairly. The primary responsibility for conducting this root cause analysis and identifying the appropriate course of own initiative action rests with each regulated firm. But we will assess the responses of firms in the course of our monitoring work and we will step in if a firm is not acting fairly on root cause analysis or not accurately assessing conduct risks.

2.19 Therefore, we would expect firms to retain records of:

- their root cause assessment of PPI sales problems and failings;
- their considerations and decisions about whether and what own initiative actions are required as a result;
- the scope, nature and results of the actions taken, including any dealings with individual consumers included in the scope of the firm's own initiative actions;

– and we will draw on these records in the course of our monitoring work (see Chapter 4).

2.20 Lastly, we would re-iterate the message in CP10/6 that:

> *Firms should be under no illusion about the importance we place on their obligations in this regard, and their ability to demonstrate and justify to us the relevant actions they have taken, and in particular, not taken. Where they cannot do this, they can expect tough action from us.*

e) The costs and benefits and wider impact of our proposed measures

2.21 Consumer representative responses did not raise criticisms of our assessment of the costs and benefits and wider impact. But many industry responses variously:

- queried how, in CP10/6, we could still deem the proposed Handbook provisions on complaint handling to be a proportionate response when our estimate of their costs had increased three-fold from CP09/23; and
- argued we had mis-stated in various ways the likely benefits to consumers, and underestimated the likely costs to firms and wider impact, arising from our Handbook provisions and package of measures.

Our response: PPI complaint numbers have increased dramatically over the last 2-3 years and in particular over the last 12 months, but there has not been evidence of any significant industry-wide improvement in firms' handling of them. For example, where complaints are referred to the FOS, the FOS continues to overturn in favour of the consumer the great majority of firms' decisions rejecting the complaints. These trends suggest that there is an even greater extent of mis-selling and potential consumer detriment than we had assumed in CP09/23, and that makes the need and case for an effective approach to addressing such detriment stronger, not weaker.

This consideration (among others) has led us to consider again whether a complaints-led approach (along with the other measures in our strategy) is adequate to deal with the scale of detriment, and whether our evidence of the scale and extent of detriment is such that it would now be proportionate to seek to establish a s404 review for the generality of sales. But on balance, we remain of the view that our complaints–led approach remains an effective and appropriate approach that is swifter and more proportionate than a s404 review of sales. From this perspective, the rise in the CBA cost estimate between CP09/23 and CP10/6, which mainly reflects this rise in complaint numbers (and its extrapolation over the next five years), does not undermine the proportionality of our proposals; rather, it reflects the large extent of the PPI problem and the size of the 'fairness driven transfer' that will potentially be delivered in the form of redress from mis-selling firms to mis-sold complainants in accordance with our final Handbook provisions.

The more detailed criticisms of our assessment of the benefits and costs are discussed in Annex 1, with our responses to them. Having taken these into account, where appropriate, and reflected the various amendments we have made in our final package of measures, we have concluded that we have made a reasonable analysis of the benefits, and a reasonable estimate of the costs and wider impact that may arise from our final measures, which remain largely in line with those in CP10/6 (see Annex 1 for details).

Overall, therefore, we conclude that our measures (as amended) are proportionate and appropriate, notwithstanding their large total cost to industry.

f) The scope and impact of our measures for specific firms or types of PPI

2.22 Aside from criticising the overall costs of our proposed measures, some industry responses argued that making Handbook provisions of general application is disproportionate and should be replaced by a concentration of regulatory effort on those individual firms with the worst PPI complaint handling.

2.23 Other industry responses argued that it is disproportionate for the proposed measures to apply to complaints about sales of certain types of PPI or sales through certain channels. Specifically, it was variously argued that it was disproportionate to include credit card PPI, home shopping revolving credit PPI, or regular premium first charge mortgage PPI, because the underlying sales breaches are less common and/or premiums are smaller, so there is less risk of consumer detriment. (Secured lenders and general insurance brokers who are not lenders expressed similar concerns, but also broader ones, and these are treated in detail in Section g.)

Our response:

General measures versus firm specific action

While we are not claiming all firms have been equally bad at PPI selling or complaint handling, we see no reason, in light of the evidence of poor complaint handling set out above, to alter our view in CP10/6 (pg. 22) that there is a widespread problem in PPI complaint handling which firm by firm action by us won't address adequately or swiftly enough.

Credit Card PPI

We remain of the view that this sector is one with significant weaknesses in sales processes, with significant potential mis-selling and potential consumer detriment likely to have arisen. Recent figures for complaints about this type of PPI continue to show significant complaint numbers (81k complaints in 2009), high firm reject rates (over 75% for many firms, though we note some other firms are now rejecting fewer than this), and high FOS overturn rates (averaging 85% according to firm data provided to us, in line with the average of 89% across all PPI types).

Home shopping revolving credit PPI

We found some evidence of sales weaknesses in this sector, with several firms rated as having medium-high or high risk sales processes, and one relevant enforcement action, leading to a fine of £270,000. Complaints have been less numerous than in other PPI sectors, but not negligible. We have seen some evidence of a high rate of rejection. Low premiums and redress in this sector may make it potentially uneconomic for firms to reject a complaint and potentially incur a FOS case fee, but this is not specific to our provisions. (See also Annex 1 para 20.) So we do not consider responses from this sector have made a persuasive case for excluding complaints about this type of PPI from our provisions.

Regular premium first charge mortgage PPI

We did say in CP10/6 (pg. 22/23), in the context of discussing the potential scope of our previously proposed rejected complaint review rule, that: *we have had fewer concerns about the sales of regular premium first charge mortgage PPI, and that so far, the number of complaints about this PPI, and the proportion of them rejected by firms but overturned by the FOS, is relatively lower than for other PPI types.*

We acknowledged this lower risk when:

- In our assessment of financial impact in CP10/6 we assumed that it would probably not be necessary for firms to undertake own initiative actions towards non-complainants for this type of PPI;[35] and
- In our CBA in CP10/6 we assumed that for complaints about this type of PPI, our guidance would only lead to an increase in firms' uphold rates from c.40% to 50%, rather than to the c.75%-90% we assumed for other PPI types.

Complaint numbers are lower than for the other main PPI sectors. Firms are rejecting over 60% of these. This might reflect appropriately the potentially lower risk sales practices mentioned above. On the other hand, the FOS is over-turning firms' decisions in around

35 See CP10/6 Annex 3 para 9b.

60% of relevant cases referred to it, which, while lower than the average for PPI as a whole (89%), is still quite high (and for example, higher than the average for non-PPI insurance products of c.40%). This potentially supports the view that regular premium first charge mortgage PPI selling, while of lower risk, has not necessarily been of low or no risk. We still take the view, therefore, that there are grounds for including complaints about this type of PPI in the scope of our provisions, to ensure that where complaints about it are rejected this does not happen without fair consideration and good reason.

Conclusion

The responses concerning the above firms and market sectors have not provided any significant new evidence to justify their being carved out from the scope of our finalised Handbook provisions.

While we are not claiming all firms have been equally bad at PPI selling or complaint handling, nor that all types of PPI have been sold equally badly, our poor sales findings and enforcement actions have covered all parts of the market, and we consider that for all sectors, we have sufficient evidence of sufficient potential mis-selling and/or of potentially unfair complaint handling to warrant their inclusion in our complaints-led approach to addressing consumer detriment.

But even if there has been relatively less mis-selling or poor complaint handling in some of the smaller sectors at the margin, the firms in those sectors have received and will likely continue to receive at least some complaints which they would in any case need to handle fairly under the existing requirements in DISP. We think it is entirely reasonable therefore to seek a consistent approach to PPI complaint handling for all types of firm and PPI.

We do not consider such inclusion to be disproportionate. We do not consider it likely that inclusion will of itself increase significantly the number of complaints about that type of PPI, and we do not consider that the Handbook provisions introduce anything that we did not think was already required under DISP. We note that firms which sold the three types of non-single premium PPI mentioned above will not, for example, need to employ the comparative approach to redress or incur the administrative and implementation costs that may accompany it (see Chapter 3).

Overall therefore, we remain of the view expressed in CP10/6 that: *If a particular type of PPI gives rise to relatively few complaints to relevant firms, and/or complaints about that type are already being fairly handled by firms according to their existing obligations under DISP, then those firms will feel little impact or additional burden from the proposed guidance when assessing complaints about that type of PPI.*

g) The position of secured lenders and secured loan brokers[36]

2.24 Responses from these sectors made a number of criticisms of our proposed measures' application to them, which we discuss in turn.

2.25 Some responses asserted that the secured loan approval process differed significantly from that for unsecured personal loans and credit cards and was fairer, because of

36 We use this term here to refer to firms who were directly authorised general insurance intermediaries, but who were not primarily lenders, insurers or insurance brokers, and whose PPI sales were mainly in respect of second charge mortgage loans.

the lengthy and staged nature of the Consumer Credit Act regulated loan approval process, and number of customer 'touch points' involved during this process, which gave consumers more time to reflect on buying PPI with the loan.

Our response: We have considered the CCA, but conclude that it does not in any way override or alter a firm's obligations concerning general insurance selling under our own Handbook requirements (nor does it alter our view of what would have been appropriate before our ICOB requirements). Our view is that in general, simply giving the customer detailed product documentation to read after the point of sale does not constitute fair presentation of the information. Hence the slower speed of loan completion and longer post-point of sale time a consumer may have under the CCA does not, so far as the sale of PPI is concerned, alter our view of the risks to the consumer of poor disclosure and poor outcome, or of this failing. So neither the CCA's requirements, nor the approach to complying with it that the secured loan firms have adopted, give us cause to qualify the application of the open letter (or Handbook text) to the secured lending sector.

We remain of the view that this sector of the PPI market is one with significant weaknesses in sales processes, with significant potential mis-selling and potential consumer detriment likely to have arisen. Recent figures for complaints about single premium secured loan PPI continue to show significant complaint numbers (c.10,000 in 2009), high firm rejected complaint rates (ranging from 65%-95%) and high FOS overturn rates (typically over 90%).

2.26 In their responses to CP09/23, secured loan brokers had said that the proposed measures weigh unfairly and disproportionately on them because:

- they received less commission than insurers and lenders from the sale of PPI, who had designed a product which could not be sold compliantly; and
- lenders had set commission targets based on volume and penetration for the sale of PPI with loans, and failure by brokers to meet these would have resulted in the withdrawal of the lenders' business from them;

– such that we should instruct insurers/lenders to meet some of the brokers' redress costs in line with *their* gain from (mis)sales.

2.27 In CP10/6 (at sections 2.15 and 2.22-24), we discussed the position of such loan brokers. We concluded that any failings by a product provider did not lessen the broker's own responsibilities to sell PPI in a fair and compliant way. We acknowledged that some loan brokers may fail as a direct result of the cost impact from our measures.

2.28 We received further criticisms in responses to CP10/6, namely that:

- Some of the failings in the open letter are inconsistent with messages from supervisors to some firms in the secured sector; and when certain loan brokers wrote to us, expressing concern about the single premium PPI policies they were required to sell alongside secured loans, we did not respond.
- Our revised proposals fail to acknowledge the role of insurers and lenders in the manufacture, design, promotion and sale of PPI, or the role of the broker who

may have been acting as their agent, and fail to lay any responsibility or liability for redress at the door of insurers and lenders for inherent product flaws, or for employing brokers as their agent.

- Brokers should have the right to use the complaint forwarding rules in DISP 1.7R to provide a mechanism for forwarding PPI complaints to relevant parties (e.g. lenders or insurers) and then having redress costs allocated among such 'co-defendants' in a similar way to court procedure.

Our response:

Dealings with the FSA

We reviewed a sample of supervisory correspondence and took what was said into account in considering whether changes to the package of measures were appropriate in the light of responses to the consultation paper.

Whatever messages from their supervisors may have expressly or implicitly been given to individual firms in the course of our thematic work, responsibility for complying with the regulatory requirements concerning the sale of PPI rested with the firms. This is the case notwithstanding that firms may claim that they continued with certain sales practices or continued to sell certain PPI policies in reliance on messages from their supervisors. In some cases firms were specifically warned that they should not rely on us to have identified each and every respect in which the firm's conduct failed to meet regulatory requirements, and that should in any event be clear to firms from the context of our supervisory work. In addition, we have always been clear that even formal individual guidance from supervisors cannot affect the rights of third parties (see for example SUP 9.4 in our Handbook).

The proposed Handbook text affects not only the firms in question but also the many consumers whom, by issuing the proposed Handbook text, we seek to protect and aims to draw an appropriate balance in the context of our regulatory objectives. We continue to take the view that the flawed practices we have identified may be detrimental to consumers. In our view, the objectives of protecting consumers by securing fair redress for them, and of promoting an orderly resolution of consumer complaints, are compelling reasons for proceeding irrespective of any reliance that may have been placed by particular firms on messages from their supervisors.

So we do not see any reason to qualify the application of the open letter (or Handbook text) to secured lenders or brokers.

The role of insurers and lenders in mis-selling PPI

Concerning provider/distributor responsibilities, where a firm is an authorised general insurance intermediary, it is not bound, unless by contractual terms, to offer a particular PPI policy provided by a lender. Indeed, in some cases, doing so may not be treating customers fairly.[37] Distributors are responsible for maintaining a compliant sales process, and therefore should be responsible for redress, where a failing arose from the manner in which the product was sold. If brokers feel that undue pressure was placed upon them by lenders or insurers, they may separately have recourse to the courts if they so choose.

37 See for example: www.fsa.gov.uk/pubs/other/ppi_thematic_update.pdf, page 11; and www.fsa.gov.uk/pubs/other/ppi_thematic.pdf, page 10

The issues in relation to agency law (e.g. whether the broker is acting (as agent) on the part of the insured or the insurer (as principal)) are complex and fact specific, depending on both the individual contractual arrangements between the parties and the specific facts surrounding a particular sale. Again, brokers may separately have recourse to the courts if they so choose.

Accordingly, we remain of the view that our Handbook text concerning PPI complaints and redress is appropriately positioned in its emphasis on the seller of the policy, and we are not making any changes to it in this regard.

<u>Brokers have the right under DISP to forward PPI sales complaints to other firms</u>

DISP 1.7.1R permits a firm to forward a complaint to another firm where it has reasonable grounds to be satisfied that that other firm may be solely or jointly responsible for the matter alleged in the complaint.

Insofar as a complaint is about the failings set out in the open letter and our Handbook text we take the view that the 'matter' complained of is about the sale of the PPI, as opposed to a complaint about the underlying product. In our opinion, such a complaint is properly directed at the firm who sold the PPI and therefore firms are unlikely to have grounds to forward that complaint on under DISP 1.7.1R.

2.29 Responses from some secured loan brokers and secured lenders asserted that our analysis of costs and benefits from our proposals:

- failed to assess properly the prudential impact on secured lenders and/or brokers;
- underestimated the consequent costs to be incurred by the Financial Services Compensation Scheme (FSCS); and
- underestimated the impact of these prudential issues on consumers' ability to access credit (especially for secured loans), where firms exit the market as a result of our proposals and the cost of any redress payable.

Our response: Relative to CP10/6, in our final CBA (see Annex 1), we have:

- updated our estimates of secured lenders' redress liability to reflect more recent available information; and
- reduced our estimates of the prudential impact on secured lenders and on GI intermediaries (including loan brokers), and thus the potential burden on the FSCS and its levy payers.

Given this reduced prudential impact, we do not expect a significant reduction in the supply of credit due to our measures (see Annex 1 para 48).

We do not believe that our final estimate of the prudential impact undermines the proportionality of our measures and their application to these sectors. And to the extent that it is the costs of consumer redress awarded in accordance with our final Handbook provisions which add to these firms' existing difficulties and potentially push some into insolvency, we consider this to be an unavoidable consequence of these firms' own mis-selling of PPI (and frequent undue dependence upon it in their business models), and not a reason to remove them from the scope of our provisions.

h) Our consultation process

2.30 Some industry responses to CP10/6 expressed a number of procedural criticisms of our consultation process, the main thrust of which are that we have not given enough time or requisite information for proper consultation, and have not taken adequate consideration of either pre-consultation or previous consultation responses in forming and revising our proposals.

Our response: We do not accept any of these criticisms. We consider that we have provided more than adequate information on our developing thinking and eventual proposals during the course of the two formal consultation papers and the extensive pre-consultation which preceded each of them, and thereby also provided ample time and opportunity for stakeholders to apprehend and comment upon our proposals.

We have made a number of amendments to our proposals (from CP09/23 to CP10/6 to the final measures in this PS) in light of responses, and consider that we have taken adequate and appropriate consideration of responses in forming and revising our proposals.

Therefore, we see no reason not to press ahead now with our finalised measures without any further consultation.

Overall conclusion

2.31 In light of all the foregoing, we remain of the view that the rationale for our measures is sound, their scope appropriate, and their likely cost impact necessary and proportionate, and we re-affirm our existing strategy, combining as it does firm specific action (e.g. Past Business Reviews) and the Handbook requirements made in this PS, as the most proportionate, timely and effectual way forward.

3 Our Handbook provisions on assessing and redressing PPI complaints

Introduction

3.1 The Handbook guidance we proposed in CP09/23 covered three main elements:

- how a firm should go about assessing a PPI complaint and relevant evidence in order to decide fairly *whether* there were failings in its behaviour towards the complainant during the sale;
- where a failing was found, presumptions outlining how a firm should determine fairly *whether* redress was payable; and
- two broad approaches to calculating fair redress: the payment of an amount equivalent to all the premium(s) paid by the complainant (plus interest); and redress to (in effect) put a single premium policy customer in the position they would have been in if they had instead bought a regular premium policy.

3.2 We further proposed a single referent regular premium price for firms to use under the second approach to facilitate consistency and transparency in its application.

3.3 In light of some of the concerns expressed in responses to CP09/23, we revised some aspects of our guidance and consulted on these in CP10/6. We asked a number of specific questions in CP10/6, to which we received detailed responses. We have carefully considered these and we set out our responses and final decisions below.

The fair assessment of evidence

3.4 In CP10/6, we largely retained the proposed guidance on the fair assessment of evidence about a PPI sales complaint that we put forward in CP09/23. In light of some of the concerns expressed in response to CP09/23, we made some adjustments to clarify some of the points about fair evidential assessment, in particular to make clearer the balanced nature of our guidance on the consideration of customer testimony and other types of specific and general evidence. We then asked:

> Q6: Do you agree with our revised proposed guidance on the approach to considering evidence?

3.5 Responses from customer representatives remained supportive of our proposals concerning the consideration of evidence. Some responses from industry welcomed the amendments we had made as more balanced, saying for example that they clarified that firms were not expected to automatically assume, on receipt of a complaint, that there had been a breach or failing during the sale.

3.6 Other industry responses continued to object to the revised proposed guidance, arguing variously that our proposals:

- reversed the burden of proof, by not requiring a customer to make enough of a case;
- discounted valid and probative evidence, thereby creating obstacles to the fair assessment of customers' complaints;
- ought instead to allow firms to place a greater reliance on their own sales procedures, training and compliance monitoring;
- were incoherent, as our own previous research on disclosure documents showed customer memory about what had been disclosed to them as unreliable;
- were inappropriate, because we ought not to set out assumptions about the weight to be given to particular types of evidence, as it will inhibit the ability of firms to take due account of all evidence that is available; and
- will, in sum, leave firms unable to reject even spurious mis-selling complaints.

Our response: Concerning 'burden of proof', we see nothing in the responses that gives us reason to change the view expressed in CP10/6.[38]

The proposed Handbook text did not have the effect of discounting evidence and we see no reason to change it in light of responses. The focus of our proposals was mainly to warn firms against placing too much weight on some types of evidence and giving too little weight to other evidence, for example by failing to recognise that a consumer's oral evidence can be good and sufficient evidence. We remain of the view that credible specific evidence about the individual sale is more persuasive than general evidence about the firm's systems and controls in place, and we do not see that this offends balance or normal practice around settling disputes. This in no way precludes the firm assessing, fairly and in good faith, the weight of the customer's oral testimony as evidence specific to the sale, and any conflict it implies with the firm's own account and own specific and general evidence.

We see no incoherence or inconsistency in this stance as compared to some of our previous findings on consumers' responses to some disclosure documents. We are clear that a firm is entitled under our proposals to consider the quality and plausibility of customer evidence alongside other evidence it has.

It is appropriate for us to give guidance on the respective weight of types of evidence. Many of the approaches to considering evidence build on our previous messages (for example the Tiner letter regarding firms' handling of mortgage endowment complaints).[39] Firms are entitled to weigh and balance the evidence and consider its value in the particular complaint.

38 See paragraph 3.10 pg. 37
39 www.fsa.gov.uk/pubs/ceo/ceo_letter_4apr02.pdf

So overall, we do not consider that these responses raised any valid objections or points that require a change to our proposals concerning the assessment of evidence.

3.7 Further criticisms in some industry responses were that our proposed guidance should:

- allow that complaints that come from CMCs should have less evidential weight than those raised directly by the customer; and
- cover a customer's responsibility to reply to a firm's reasonable requests for information.

3.8 Some industry responses argued that the FOS Payment Protection Insurance Questionnaire (PPIQ) was not sufficiently detailed to elicit the information that firms need from the customer. The industry also raised operational concerns, querying how the PPIQ should be used and what a firm should do if a customer does not respond. But some responses from consumer representatives were concerned that firms will use the PPIQ to delay the assessment of complaints.

Our response: Neither the fact of a CMC's involvement, nor the fact that the complaint may have been made on a generic template letter, lessens a firm's obligation to treat the complainant fairly and assess the complaint in line with DISP. Firms are not precluded from seeking additional information from consumers where relevant (for example through the PPIQ – see below).

We agree that it is reasonable to expect customers to reply to reasonable requests for additional information from a firm, though a firm should not request information it could source itself from internal records, or create barriers for complainants. Where a consumer does not provide adequate information, and the 8 week DISP time limit is approaching, the firm is entitled to make a fair assessment of the complaint on the basis of the information it has available, assuming that it has given the customer a reasonable opportunity to respond. As noted above, the detail and quality of a customer's recollection is something that may reasonably be weighed by the firm in assessing the plausibility of the customer's evidence and concern.

Comments on the design and use of the PPIQ should be directed to the FOS. We believe that used properly, it should serve to provide firms with useful evidence. We understand that, prior to accepting cases, the FOS generally requires customers to complete the PPIQ. Given this, it might be appropriate and helpful, and avoid delay, for a firm to use the PPIQ as part of its own PPI complaint handling process. Firms can request information additional to that covered by the PPIQ where that information is genuinely needed.

3.9 Some industry responses argued our proposals were not workable insofar as they require firms to assess the clarity of documentation from the perspective of a reasonable customer.[40]

Our response: Our view is that the 'reasonable person test' is a fair test, and one which firms should be accustomed to applying in their general complaint handling functions and in their design of product literature. So firms should be well able to apply it appropriately to PPI complaints.

40 See DISP App 3.3.12 (3) of the Handbook text in CP10/6

Considering multiple sales of PPI in a sequence of refinanced loans

3.10 In light of concerns expressed in response to CP09/23 about the ostensibly wide scope of our guidance concerning taking into account previous PPI sales to a complainant, in CP10/6 we revised the proposed guidance to clarify that:

- our specific concern was that, where a consumer refinanced their loan and with each refinancing the firm sold (and potentially mis-sold) a new single premium PPI policy, the consumer is then bearing the cost within their loan of one or more previous single premium policies; and
- the seller should thus review only those sales it made *to the customer in the course of this successive refinancing* and take them into account, including their cumulative impact, when assessing a complaint and, where appropriate, providing redress.

3.11 We then asked:

> Q7: Do you agree with our revised proposed guidance in respect of re-financed loans?

3.12 Most responses from consumer representatives and the industry agreed with the guidance as revised, and its importance in addressing potential cumulative consumer detriment of this kind. But some industry responses raised concerns that it will lead to more sales being reviewed and so will increase the application of what these firms see as our 'retrospective' common sales failings (see Chapter 2).

3.13 Some industry responses argued that a firm should also be able to use evidence from previous sales when considering a complaint. For example, if a customer has previously bought single premium PPI, the firm should be able to use this as evidence that the customer would have had knowledge of the product.

Our response: We do not agree the common sales failings set out in our open letter are retrospective – see our responses in Section a of Chapter 2.

In applying our guidance, firms should approach each sale in such a sequence on its own merits. Clearly it would be unfair and inappropriate to use an earlier sale which had shortcomings to defend a subsequent sale or to make strong claims about the consumer's knowledge of or attitude towards the product.

The rebuttable presumptions concerning consumer action 'but for' firms' sales failings

3.14 Our proposals included two presumptions that a firm should apply in the event that a breach or failing was found: that the customer would not have bought the PPI they bought if there had not been such a failing; or, in the case of some failings specific to single premium PPI, that the customer would have still bought PPI but that it would have been a regular premium policy instead.

3.15 In light of some of the criticisms made in CP09/23, in CP10/6 we made some adjustments to the proposed guidance so as to:

- clarify the meaning and implications of the two presumptions; and
- limit the presumptions' application to 'substantial flaws' in the sale.

3.16 We then asked:

> Q8: Do you agree with the revised proposed guidance on determining the effect of a breach or failing? Do you agree that it is appropriate to have both presumptions or should either of them not be included?
>
> Q9: Do you agree with the list of significant flaws that lead the firm to presume that the customer would not have bought the PPI? Do you think that any of these should be removed or amended and/or lead to a different presumption, or that the presumption should apply for all sale flaws identified in the open letter?

3.17 Most consumer representative responses, and some industry responses, agreed with our revised proposals. The majority of the industry's responses were negative, arguing that:

- the presumptions remained inappropriate and narrow, as a mis-sale can give rise to a range of potential effects with differing consequences, but these are not recognised by the presumptions; and
- the 'but for' test underpinning the presumptions remained inappropriate, because it is difficult to assume retrospectively what the customer would have done (or not done), especially where a claim is made via a CMC.

3.18 Some industry responses also viewed it as unreasonably difficult to produce evidence to rebut the presumptions even in compliant sales, believing that the practical result will be that redress would automatically be due. One firm argued that it did not record all telephone sales and so will not have evidence to rebut the presumptions. Some consumer responses took a different view, arguing that, notwithstanding the correctness of our guidance, firms would likely seek to use evidentially weak arguments to rebut the presumptions.

3.19 Most industry responses were not supportive of the examples of 'substantial flaws' set out in our proposed guidance and their link to the presumptions, viewing them as based on retrospective and incorrect sales standards and/or as not substantial. Whereas some consumer representatives' responses believed the number of substantial flaws should be increased to include all the common failings included within our open letter.

3.20 Some responses, from both the industry and consumer representatives, stated that the presumptions should make some allowance for the materiality of breaches. Some industry responses further argued that the presumptions should distinguish between matters of disclosure and matters of suitability and that those disclosure failures that do not affect suitability should not result in the presumption that the customer would not have taken the policy.

Our response: Our position is that, in setting out how firms should handle complaints under the DISP rules, we are not restricted to taking an approach that corresponds exactly with the way disputes between parties are determined in a court. However, we have taken as a starting point the typical approach in law (which we understand also to be the FOS's general approach) that the customer should be put in the position they would have been in if there had been no failure to comply with its obligations on the part of the firm. Typically that involves considering what the customer would have done 'but for' the firm's breach or failing. Firms have also been making such 'but for' judgements for many years, it being the basic tenet of complaint handling. Complaints about PPI are not new or unusual in this respect. We are satisfied that the 'but for' test is a reasonable one in the circumstances.

The presumptions represent a way of judging what a customer would generally have done, in our view. Having given due consideration to responses concerning the presumptions we remain of the view that the presumptions we have set out are reasonable ones fully in the tradition of, and informed by, the kinds of judgements that courts and ombudsmen have long and often been making when assessing claims and complaints and the potential need to put the claimant, as far as practicable, back in the position 'they would have been in' had the breach not occurred.

We also recognise that it would not be possible to establish in every case what a customer would have done in every individual circumstance and that there has to be scope for a firm to depart from the presumptions. So, the presumptions are rebuttable – that is, it is open to the firm to evidence that the customer would have bought the policy notwithstanding the breach or failing, in which case no redress will then be required.

Some responses indicate a misunderstanding of our proposals. Our proposals imply three stages. First, the firm should consider whether there was a breach or failing by weighing up the evidence and coming to a fair conclusion. Second, if (and only if) the firm concludes there was a breach or failing, the firm should consider what the customer would have done 'but for' the failing. If the failing was a substantial flaw, examples of which are provided in our Handbook text, the presumptions will be relevant. Third, the firm may consider whether in the particular circumstances of the complaint there is evidence to rebut the presumption.

A recording of the sale is not essential to rebut the presumptions. Where it is not available, firms must fairly assess the available evidence to make a decision about what they think would have been likely to have happened, but for the failing, given the circumstances and the evidence about the sale. For example, if the firm failed to disclose the existence of an exclusion relating to pre-existing medical conditions, then it may be reasonable for the firm to rebut the presumption that the customer would not have bought the policy if it can be shown that the customer did not have a pre-existing medical condition. It is unlikely that a recording of the sale would elicit this information. The PPIQ, if properly completed, will however provide this information.

We have carefully considered, in light of responses, the proposed list of 'substantial flaws' in the proposed Handbook text. We are satisfied that the rebuttable presumptions cover substantial flaws and that our proposals are appropriate because in each case the nature of the failing raises serious doubts over whether the customer would have proceeded with the purchase if there had not been such a failing.

It is true that the presumptions do not make allowance for the materiality of the failings. We consider that the failings amount to substantial flaws irrespective of their materiality to particular consumers, and that it is reasonable and simpler for our guidance not to differentiate the failings in terms of materiality. In practice, firms are likely to be able to factor in considerations of materiality when potentially rebutting the presumptions in the case of a particular complaint. For example, if a firm failed to disclose an exclusion, and if that exclusion did not apply to that customer at the time of the sale (something which can be evidenced relatively straightforwardly with reference to the policy), it may be reasonable for the firm to conclude (assuming there are no other failings) that the exclusion was not material to that customer and that he would have bought the policy anyway, notwithstanding the firm's failure to disclose the exclusion.

We considered the point that presumptions should differentiate between matters of disclosure and matters of suitability, but we see no reason to make this distinction. For example, failing to disclose to a customer a significant exclusion which was relevant for that customer would produce much the same customer outcome as a failure to take into account the exclusion when providing advice to that same customer: in both cases the customer has a policy under which he is excluded from the cover.

Overall therefore, we have seen no reason to change the proposed Handbook text in CP10/6 concerning the presumptions and the examples of substantial sales flaws which link to them. But **we have made one technical amendment to recognise that some refund terms provided by firms were pro-rata.**

Principles of redress

3.21 Our proposals for redress, as revised in CP10/6, were essentially as follows:

- if the firm concludes that, notwithstanding any failing, the customer would still have bought the PPI they did, then no redress will be due;
- if the firm concludes that the customer would not have bought the PPI then the firm should reimburse the customer for the amount of premium paid (plus interest); and
- where the firm concludes (for particular failings related to single premium PPI) that the customer would have bought a regular premium policy instead then the firm should give redress that, as far as possible, puts the customer in the position they would have been in if they had done so (we called this a 'comparative approach').

3.22 Industry responses mainly criticised our approach to redress, as revised in CP10/6, arguing that it remained flawed, irrational, disproportionate, and likely to deliver inappropriately large redress to customers. Some such responses further suggested that other general approaches (which these responses describe as 'proportionate') are more appropriate and closer to what a court would determine. So, for some breaches or failings, it is appropriate for a firm to provide a different form of redress to that described in our proposed guidance.

Our response: We have considered these matters very carefully and concluded that the approaches proposed in CP10/6 (an amount equivalent to a full return of premiums or, where appropriate, comparative redress) are:

- more likely to provide a fair and reasonable outcome for relevant customers in most circumstances (in part because they are less susceptible to potential misapplication by firms); and
- closer to established law and ombudsman practice (being grounded in restoring the customer to the position they would have been in 'but for' the firm's failing).

Therefore we do not consider it necessary to change the substance of our approach and Handbook text in CP10/6 concerning the return of premium and comparative approaches to redress (though we consider questions of its workability below.)

However, **we have amended the Handbook text (see DISP App 3.8) to make clear that the remedies we have set out are not exhaustive**. Our guidance to firms is those remedies represent considerations and remedies that may be appropriate in a number of common scenarios. It is open to a firm to apply other remedies where it considers it would provide an effective and fair remedy for its customer and represents a reasonable outcome in all the circumstances of the case. Firms may, for example, consider alternative redress such as the following:

a. Where the firm failed to disclose an exclusion or limitation or failed to properly account for these in its advice and the policy remains live: In such a case the firm may consider whether it is appropriate to ensure, for the duration of the payment protection policy, that in the event of a claim, the customer will promptly be paid the amount of the claim that would have been payable under the policy had the exclusion or limitation in question not applied;
b. Where the firm failed to disclose that the PPI did not give a pro-rata refund when cancelled or failed to properly account for this in its advice: In such a case, the firm may consider whether it is appropriate:
   - for live policies: in the event that the contract is cancelled by the customer before the end of its term, to ensure that the customer promptly be paid an extra amount equal to the difference between the actual refund from the insurer under the policy and a pro-rata refund; and
   - for cancelled contracts: to pay an extra amount equal to the difference between the actual refund from the insurer under the policy and a pro-rata refund (plus interest).
c. Where the firm failed to disclose that the term of the policy was shorter than the period of the loan, and the consequences of this, or failed to properly account for this in its advice: In such a case, where the policy and loan are both still in force when the complaint is first made then the firm may consider whether it is appropriate to arrange that for the remaining duration of the term of the loan, and at no additional cost to the customer, a payment protection contract is provided to the complainant that would be equivalent to cover having been provided for the full term of the loan.

We consider that it is unlikely to be fair to customers to take such an approach where a complaint involves multiple breaches or failings or where it is clear that the failing was particularly significant for that customer. Consequently, we anticipate that such different approaches are unlikely to be appropriate in the majority of cases and will be the "exception not the rule" for firms when dealing with a complaint satisfactorily.

The Referent Price used in the comparative approach to redress

3.23 Following various criticisms made by industry responses to CP09/23, and our own further analysis in light of these, in CP10/6 we increased the proposed referent regular premium price to be used in the proposed comparative approach to redress from £6 to £9 per £100 of benefit. We then asked:

> Q10: Do you agree with our proposal to increase the referent price from £6 to £9?

3.24 Responses from industry and from consumer representatives generally disagreed with our proposal, though for different reasons, and felt there was inadequate analysis of how the £9 figure was reached.

3.25 Consumer representatives' responses variously viewed the new price as:

- too high, and as thus unfairly reducing the sum of redress and value of the forward cover;
- diverging too far from the price of PPI products available in the market; and
- failing to allow for the fact that the lender generally benefits from the insurance as it reduces the risk of default.

3.26 Some industry responses felt the price was fair, but only if applied to a full Life, Accident Sickness and Unemployment (LASU) policy, rather than a product with less cover. Other industry responses argued variously that:

- the referent price remained too low;
- the variations in the quality of cover mean a single price is inappropriate;
- the price does not factor in the more expensive life cover costs in the secured loan sector as compared to the unsecured loan sector;
- the referent price amounted to price fixing and was therefore inappropriate; and
- it was not clear whether the referent price is a net or gross rate or what the position is on Insurance Premium Tax.

Our response: In CP10/6 we explained that at £6 the proposed referent price results, for some complaints about some products in certain circumstances (e.g. where the complaint was early in the life of the policy and the cancellation term's refund is pro rata) in a higher cost to firms than a redress payment equivalent to a return of the premium. This was not our intention, and is highly likely to dis-incentivise firms from applying the comparative approach at all (with the result that many people would lose cover they might wish to keep).

These conclusions were reached on the basis of a detailed scenario analysis, which showed that the effect of a £6 referent price would be disproportionate, unfair to firms, and undermine the consumer protection policy intention behind the comparative approach, but also that such distortion could be largely corrected by raising the referent price to £9.

We accept that the consequence of correcting most (but still not all) of this distortion is that the £9 price is further away from the prices that were available (albeit from a very few suppliers and from different distribution channels) on the market at the time or that are available now.

However, as we noted in CP10/6, the figure is intended to be neither the lowest price that was or is available in the market, nor a reflection of what firms might have charged had more of them offered a regular premium PPI product. Rather, as we said in CP10/6: '*the referent price is a very specific tool concerning the calculation of fair redress, deployed in the context of our efforts to establish a fair approach that is workable for large complaint volumes*'.

We again considered whether a single price was appropriate and whether our intervention would potentially distort the pricing of cover in the market. In particular, we considered the argument that the cost of providing life cover for second charge mortgages is generally higher than providing life cover for other types of loan.[41] However, on balance the arguments put forward did not alter our view from that set out in CP10/6 (see page 48).

So, in summary, having considered the arguments put forward we remain of the view that a £9 referent price is appropriate.

However, in light of the concerns from the consumer side, we have amended the proposals concerning firms' communications to customers about an offer of comparative redress to emphasise that firms have to make clear, when offering such maintained cover, that the consumer could well be able to source it more cheaply elsewhere (see also our response to Q12 below).

In addition, we are aware that a small number of firms sold single premium products providing more tailored, less comprehensive benefits (i.e. not full LASU), and charged a correspondingly lower premium, such that a rigid application of a £9 referent price may cause a complainant who had been mis-sold such a policy to be given unfairly little redress under the comparative approach. We would expect firms in such cases to consider whether it may be fairer to use an alternative lower price.

The query about whether the referent price represents a net or gross price shows a misunderstanding of our proposals. The regular payments by the customer going forward are not really a premium (because the single premium has already been paid). Rather, they should be considered as a balancing payment in light of the comparative redress, which reflects the fact that the customer has chosen to retain the single premium policy's cover. To recognise the value the customer has had from the policy, the selling firm is able to deduct from the amount that would otherwise be payable to the customer an amount reflecting this value. The customer will also derive value from the policy in future. However, because it cannot be known how long the customer will wish to continue to derive this value (he may cancel the policy) this cannot be deducted from the compensation figure at the time of the offer. So, some sort of regular payment mechanism is set up to account for this future value. The fact that the payment is not a premium means it is neither a net or gross rate. It follows then, that the fact that we do not view the payment as a premium means that there should be no Insurance Premium Tax impact for firms.

41 This is due to the fact that second charge mortgage loans tend to be over a longer term than personal loans and therefore tend to have a higher balance for the period of PPI cover. Cost has a direct relationship to liability.

The menu of options for implementing comparative redress

3.27 In light of industry concerns expressed in response to CP09/23 about the workability of our redress proposals, in particular for firms that do not both underwrite and sell the insurance and/or provide the loan, in CP10/6 we revised the proposed guidance setting out a menu of different ways (Approaches A to D) in which firms can fairly implement the comparative approach to redress and, in particular, maintain the cover on a new regular payment basis for relevant complainants who wish it. This menu was intended to enable all types of firms to deliver the comparative approach. We also provided worked examples and illustrations concerning this menu.

3.28 Further, given concerns expressed about the comprehensibility to consumers of the comparative approach, in CP10/6 we proposed additional guidance to emphasise that a firm offering comparative redress in one of these ways should provide a number of specific key messages to relevant consumers.

3.29 We then asked:

> Q11: Do you agree with our four approaches to implementing the comparative approach to redress?
>
> Q12: Do you agree with our proposed customer communications concerning offers of comparative redress?

3.30 In response to the four approaches, some industry responses variously argued that:

- we ought not to be identifying preferred approaches to implementation at all, as firms are in the most appropriate position to make this judgement;
- we still underestimated the administrative and technical difficulties involved in comparative redress, and (in the view of some) the proposals remained unworkable; and
- some important technical aspects remained unclear (including the status of the customer's payments to maintain the insurance cover, the Consumer Credit Act (CCA) implications, the reliance on third parties for information and data protection issues).

3.31 Consumer representatives were mainly concerned that:

- firms will choose the options that produce less favourable customer outcomes;
- Approach D in particular makes for expensive forward cover for the consumer.

Our response: We understand that the four approaches outlined in the proposals are more complex than cancelling the policy and providing an amount equivalent to a return of premium, but we do not view them as too complex to operate. We have reviewed the specific operational concerns firms have raised and do not view any of them as insurmountable. We continue to view the proposals as flexible and workable, though accept there may be some challenges for some firms in delivering some of the possible approaches.

The finalised Handbook text concerning comparative redress is framed as evidential provisions (see discussion below), but this does still give firms a degree of flexibility in *how* to implement it (since the menu of implementation options is guidance that does not have the status of evidential provisions). We would expect that, if firms do use different approaches, they treat customers fairly.

If firms do not wish to adopt the comparative approach to redress at all, then they may cancel the policy and make awards equivalent to a return of the premium. We expect that firms will already be using this approach, so there should be minimal impact.

It is true that under all the approaches and particularly Approach D, the cost to the consumer of the maintained cover may exceed what he could find for a standalone policy from another provider. In respect of Approach D, we view this as an unavoidable consequence of designing an approach that can be implemented where it is not possible for a firm to restructure the underlying insurance or loan or to collect regular payments going forward. Such relatively more expensive cover will be of benefit mainly to consumers who might struggle to get new cover elsewhere e.g. because their health circumstances have declined since the original sale. But in light of this concern about cost, we have, as noted above, **amended the final Handbook text so as to emphasise that firms have to make clear when offering such maintained cover that the consumer could well be able to source it more cheaply elsewhere (see DISP App 3.7.15 E (2))**.

Regarding the status of the payments, we have addressed this in Appendix 2 (and also above in our response to Q10). More generally, **we have amended the drafting in the redress examples so as to no longer refer to the referent price payments as 'premiums'. We also make some technical points, to assist firms, in Appendix 3 in response to the points made about the CCA**. We do not believe any of these CCA points undermine the appropriateness and workability of our proposals.

It is true that the approaches require the firm to be in possession of certain information (such as interest rates and previous paid claims) which may not be available from its own records. However, our proposals are no different from firms' current obligations in this respect: if a firm currently finds it has mis-sold PPI sold alongside a loan, then one remedy is for the firm to reschedule the loan to remove PPI. This does, and will continue to, require some sharing of information between firms. We would expect all firms to behave reasonably in applying our proposals and not, for example, make unreasonable charges for the information. Where a firm requires personal data from a third party, it should ensure that it has the customer's authority to request that data. Firms may find it useful, for example, to enclose a letter of authority with the PPIQ.

3.32 Concerning messaging to consumers, most responses from the industry and from consumer representatives agreed with the proposed customer communications, though concerns were raised that the approaches to redress were increasingly complex and thus hard for consumers to understand and for firms' communications to make clear. Other industry responses variously:

- suggested alternative messages they considered easier to grasp;
- raised concerns that providing information about the possibility of future eligibility being impaired under a new policy (because of changed circumstances) may appear to be a personal recommendation; and

- sought assurance that the proposed messages are non-exhaustive and that firms have the freedom to add further messages if appropriate.

Our response: The menu of approaches is for firms, not for consumers. We expect firms to choose one approach to implementing comparative redress and then adopt that approach consistently towards all relevant consumers (and not offer different approaches to different consumers). Given this, our view is that firms should be capable of presenting their approach to comparative redress clearly and fairly in letters to relevant consumers. We provide guidance (at Appendix 2) on the types of messages that should be included in the final response letter to the complainant and we will, if requested, engage with firms and consumer groups during the implementation period on the design of appropriate redress communications.

The examples of redress calculations

3.33 In CP09/23 we included several worked examples of redress. Following feedback, and in light of changes to our Handbook text on redress, in CP10/6 we set out further examples to illustrate the four approaches to implementing comparative redress, and to illustrate some particular aspects of PPI redress more generally which responses had asked about. We then asked:

> Q13: Do you agree with the redress calculation examples?

3.34 Responses from industry and from consumer representatives agreed that the calculation examples were consistent with the proposals, save for some minor errors and clarifications.

Our response: We have retained the examples but corrected the relevant errors and provided relevant clarifications.

Complaints and claims

3.35 Some responses challenged the appropriateness of our proposed guidance in CP09/23 which indicated that a firm, as part of its redress, should now pay a claim that would not otherwise have been covered under the terms of the policy. Other responses from industry expressed concern at the practical difficulty involved, when the seller was not the insurer, in deciding and assessing claims whose previous rejection had been linked to deficiencies at point of sale.

3.36 In CP10/6, we accepted the industry argument that it may be disproportionate to require firms to pay a previously rejected claim solely because an exclusion or limitation later relied upon was not disclosed to the customer. So we amended the proposed guidance to state that this redress should only be considered where the complainant may have reasonably expected that the claim would have been paid. A reasonable expectation could be created where, for example, a firm sold the customer the policy and failed to disclose an exclusion or limitation, and it should have been clear to the firm that such an exclusion was relevant for that particular customer. If a reasonable expectation was created, we do not consider it to be unduly difficult for the seller to obtain relevant information and views from the underwriter. We then asked:

Q14: Do you agree with our approach to the position where a customer was mis-sold the PPI and subsequently made a claim which was rejected?

3.37 Most industry and consumer responses agreed with our proposals, but some industry responses argued that it is inconsistent to presume that the customer would not have bought the policy, but then require firms to potentially pay an amount equivalent to settling a relevant claim under that policy.

3.38 Some consumer representative responses raised concerns about the 'reasonable expectation' test. They argued that a reasonable expectation would always be created if, for example, the firm failed to disclose any exclusion, whereas our proposals suggest that a reasonable expectation will only arise where the firm had knowledge about the complainant's circumstances at the time of the sale and the relevance to them of that exclusion.

Our response: We believe that our proposal is the most likely to achieve the appropriate redress for most consumers in the context of a mis-sale of this nature. We do not believe it is inconsistent with the 'but for' test or potential outcomes under the general law. If a customer brought a case through the courts under the general law and/or the right to damages under s150 FSMA, the level of redress would depend on the precise circumstances of the case, including the cause(s) of action, the agency relationships and an assessment of the customer's likely actions if the failing had not occurred. For example, if the claim was in misrepresentation and the distributor was the agent of the insurer, then the customer might well have a choice between seeking rescission of the policy and return of premiums or damages amounting to the value of a claim (plus interest in either case). However, as described above (pg. 46), we have amended the Handbook text more generally to make it clear that a firm may provide alternative approaches where these would provide an effective and fair remedy. One example of this concerns a failure to disclose an exclusion or limitation, where it may be appropriate to arrange that the amount of any claim is paid to the customer as an alternative to return of premiums. It is open to firms to apply such an approach (in appropriate cases as explained above) where the claim occurred in the past.

Turning to the consumer concern, we were not satisfied that the failure to disclose would always create an automatic obligation on a firm to pay a claim, though we accept in some circumstances it might (for example, where it should have been clear to the firm that that exclusion or limitation was relevant to the complainant).

For all these reasons the final Handbook text is largely as proposed in CP10/6, though **we have clarified our intended policy position with some additional text at DISP App 3.7.6E(2)**.

3.39 We also asked in CP10/6:

Q15: Should the guidance also address the position of a customer who was mis-sold the PPI but did not subsequently claim because he knew the claim would be rejected (for example, because he subsequently reviewed the detailed policy documentation)? If so, how?

3.40 Consumer representatives' responses believed the guidance should address this scenario. Most industry responses felt additional guidance was unnecessary, arguing that the issue would be picked up by a firm's root cause analysis if it was a recurrent problem, and that if it was not recurrent, then addressing the position of these customers would be disproportionate. Other industry responses argued that if a customer found that the PPI did not meet their expectations, they would tend to make a sales complaint and so be picked up by the complaint processes and our guidance anyway (particularly as a customer who had spent time examining the detailed policy terms and conditions would be likely to be aware of their right to complain and to make eventual recourse to the FOS).

Our response: We were, on balance, persuaded by the industry's arguments that explicitly addressing the position of people who had not claimed was not necessary. We would, however, expect firms to consider this scenario when applying their general complaint handling processes and when considering the position and fair treatment of non-complainants where root cause analysis suggests, as a recurrent failing, that appropriate disclosures were not made at the point of the sale (see Section d of Chapter 2).

Other redress matters

3.41 A number of other points were made about our proposed guidance concerning redress, which we consider in turn.

3.42 Some firms responded that if a customer makes a claim under the policy, then this should be treated, from the perspective of the law, as affirming the PPI contract, such that it should not be open to the customer to make a subsequent complaint about the sale, and firms should not be required to uphold such complaint or offer redress.

Our response: We have explained above that we do not consider that we are restricted to taking an approach that corresponds exactly with the way disputes between parties are determined in a court, and so contract law principles need not determine how we frame our rules or guidance. However, in any case we do not accept that general contract law principles mean that a customer who was mis-sold a policy but who was not aware, or had no knowledge, of any breach or failing should be regarded as having affirmed the contract even if he had made a claim under the policy. More broadly we do not believe it would be fair for a firm to seek to do this. So, we have not amended our proposals in response to this point.

3.43 Following concerns expressed in some consumer bodies' responses to CP09/23, in CP10/6 we added guidance that firms should 'consider whether there are any further losses' flowing from its failing, and stated that it would be 'fair and appropriate in many circumstances' for the firm to pay redress covering any consequential losses the consumer suffered as a result of the mis-sale (see pg. 54 of CP10/6).

3.44 Consumer responses agreed with this additional proposed guidance. Industry responses generally disagreed, arguing that our proposals were disproportionate and incompatible with the law. Some industry responses were more specific, arguing that losses must be limited to losses likely to flow from a breach of contract in the contemplation of the parties at the time they made the contract.

Our response: Our intention was not to introduce any new and substantive obligation on firms over and above what we expect they would already be doing if treating their customers fairly. We consider that it should be uncontroversial that a firm should address any losses clearly flowing from a firm's mis-sale which ought to have been foreseeable or contemplated at the time of mis-sale. We agree that there should be a causal link between such losses and the firm's sales failings, and consider that consequently such loss is likely to be appropriate in only a small minority of cases. Our concern is that firms consider and apply their wider obligations when addressing such potential losses. W**e have amended the drafting in the finalised Handbook text to make clear that firms need only pay redress for any further losses that were 'reasonably foreseeable as a consequence' of its sales failing (see DISP App 3.9.2G)**.

3.45 Many responses from the industry felt that the 8% simple interest rate set out in our guidance as appropriate was too high and that we should consider the outcome of the Ministry of Justice (MoJ) consultation on the rates used by the courts.

Our response: We responded to these points in CP10/6 (see paragraph 3.37 pg. 57). Since then the consultation by the MoJ has ended, but did not result in legislative change. So 8% remains in line with the approach of the courts and the FOS and we see no good reason to depart from it.

Guidance vs Evidential Provisions vs Rules

3.46 Some consumer representatives' responses to CP09/23 queried whether our proposed guidance would change firms' behaviour and suggested instead that we make our provisions as rules. In light of this concern, in CP10/6 we discussed the respective natures and consequences of guidance, rules and evidential provisions (a particular type of rule), explained that we could change our proposed guidance into various combinations of these, and outlined our view of the advantages and disadvantages of doing so.

3.47 Specifically we suggested:

- leaving the proposed provisions at: 3.1 (Introduction), 3.2 (The assessment of a complaint) and 3.3 (The approach to considering evidence) as guidance; and
- re-positioning most of the remaining provisions as Evidential Provisions (EPs).[42]

3.48 We then asked:

> Q16: Do you think that we should make the key provisions in the proposed Appendix 3 to DISP as guidance, or alternatively as (a) a combination of guidance and evidential provisions or (b) as a combination of guidance, rules and evidential provisions?

42 Namely: 3.4 (Root cause analysis); most of the provisions in 3.5 (Re-assessing rejected claims); most of the provisions in 3.6 (Determining the effect of a breach or failing); most of the provisions in 3.7 (Approach to redress) and most of the provisions in 3.8 (Other matters concerning redress).

Q17: If preferring alternative (a) do you agree with the designation of EPs and guidance described above and, if not, which ones would you change? If preferring alternative (b) are there any provisions which currently say a firm "should" act in a particular way that you would not make as rules; what would they be instead, guidance or EPs?

3.49 Firms' responses were unanimous that the provisions should all remain as guidance, viewing the introduction of EPs (or Rules) as being disproportionate and inflexible. Consumer responses remained sceptical that guidance would change firms' behaviours and preferred a format that would provide most certainty that firms will comply and best enable us to enforce against non-compliance.

Our response: We considered carefully the arguments put forward. Our conclusion is that:

- the substance of the proposed provisions concerning presumptions about failings and appropriate redress is already quite prescriptive in character, and so sits better as EPs than guidance, but this is not true of the necessarily more discursive and general provisions concerning the assessment of evidence;
- as EPs, rather than guidance, these provisions will be more likely to change firms' behaviour (not least because they are more likely to be successfully enforceable by us because failure to comply with them may be taken as tending to establish that the firm has contravened the complaints resolution rule in DISP) and thereby deliver better consumer outcomes, including remedying detriment caused by PPI mis-selling; and
- unlike rules, EPs still leave it open to firms to demonstrate to us that any alternative approach taken by them is fair and we think this much flexibility is appropriate given the varied nature of possible complaints and outcomes.

So, **in the final Handbook text, DISP App 3.5 to 3.8 are EPs (though DISP App 3.5.2G remains as guidance reflecting the more subjective nature of this provision). DISP App 3.4, on root cause analysis, remains as guidance, which is consistent with the status of the existing root cause guidance at DISP 1.3.5G.**

These finalised EPs should still be treated by firms as guidance for complaints about pre-2005 sales (see Chapter 2, Section c). This is because we take the view that the relevant pre-2005 sales standards had much in common with the later standards, some of which are closely linked to the presumptions in the Handbook text, and that the degree of flexibility associated with Handbook guidance is appropriate when handling complaints about these sales.

4 Implementation and monitoring

Implementation

4.1 In CP09/23 we proposed to implement immediately our proposed measures. However, this timeframe was criticised in industry responses as unreasonably short and unworkable. In light of this, we proposed in CP10/6 that firms should implement the Handbook provisions concerning evidential assessment of PPI complaints one month after they came into force, and the provisions concerning redress two months after that (i.e. three months after the Handbook provisions came into force). We then asked:

> Q18: Do you agree that this proposed (staggered) implementation period for the complaint handling guidance is reasonable and practicable?

4.2 Consumer responses criticised this change as a further unwarranted delay in improving PPI outcomes. However, industry argued that the revised period proposed was still unreasonably short (and proposed e.g. six months instead), due in particular to:

- the implementation timetable's likely overlap with:
  - o the summer holiday season; and
  - o implementing of the Consumer Credit Directive[43] and Irresponsible Lending Guidelines.[44]
- there being inadequate time (especially given the level of competing demands likely to be placed on a small number of suppliers and consultancies) to:
  - o change IT systems to support the new Handbook requirements (and in particular to deliver the comparative redress approach); and
  - o recruit new staff, and train up new and existing staff, to deal with complaints in accordance with the new Handbook requirements.

---

43 Directive 2008/48/EC, implemented in the UK through The Consumer Credit (EU Directive) Regulations 2010 www.opsi.gov.uk/si/si2010/uksi_20101010_en_1

44 Irresponsible lending – OFT guidance for creditors March 2010 www.oft.gov.uk/shared_oft/business_leaflets/general/oft1107.pdf

Our response: We have considered these responses carefully, balancing the need for urgency in delivering improved consumer outcomes, against rushing firms and potentially undermining compliant implementation.

On the one hand, we consider that:

- Although the summer may be a popular time for annual leave, it is unlikely that a firm would permit key staff to be out of the office simultaneously in a manner that would hinder the running of its operations in an appropriate and compliant way.
- Firms have been aware of the Consumer Credit Directive since May 2008 and the Irresponsible Lending Guidelines since August 2008 and should already have prepared for implementation of these requirements accordingly and in good time.
- We recognise that IT development will vary between firms, but we have not seen convincing evidence that many months are really required (e.g. to deliver comparative redress) and we have seen evidence which suggests that a lead time of three months would be sufficient for the necessary IT changes.
- PPI complaint volumes have already been at a high level for many firms for some time now, and firms should already have ensured that they have sufficient quantity and quality of staff to handle these fairly at all times in accordance with the existing Handbook requirements in DISP concerning complaint handling.
- Firms have not provided evidence to support their contention that implementation will result in such a large increase in demand for outsourced suppliers (presumably including software systems, IT providers and agency staff) that it will create shortages of these and delay implementation.

On the other hand, we do not wish to undermine the intended impact of the finalised Handbook provisions as a consequence of some firms genuinely having insufficient time to train staff adequately or to provide adequate IT support.

Overall, we conclude that there is an argument for giving firms more time (than the proposed one month) to implement the Handbook provisions concerning evidential assessment of complaints.

Therefore, we have decided to amend the implementation period so firms have until **1 December 2010** to comply with all parts of the Handbook provisions (i.e. over three and a half months from the publication of this PS, which also allows for the fact that implementation work during August may be limited).

While firms should also implement by this date the guidance on root cause analysis and firms' obligations to consider the position of non-complainants who may have been affected by recurrent sales problems, we would not expect firms (absent specific imperatives to the contrary) to commence any own initiative actions they consider required as a result (e.g. consumer contact exercises) until six months after this PS is published i.e. until mid **Q1 2011** (though firms may of course choose to commence such actions sooner). This will give firms time to prioritise initially the efforts required to implement the fair and compliant handling of PPI complaints.

Monitoring

4.3 We will maintain our focus on ensuring improved outcomes for PPI consumers by undertaking a risk-based approach to monitoring firms' behaviours. As our Handbook provisions apply to complaints concerning sales of all PPI types, firms in all sectors can expect to be monitored. But we do intend to pay particular attention to complaints about single premium PPI policies on unsecured personal loans, as this is a sector where we have previously seen significant sales failings and potential consumer detriment, and where our comparative redress approach can potentially apply. We will also attend closely to the handling of complaints about single premium PPI policies on secured personal loans, where the comparative redress approach may also feature.

4.4 Firms will need to be able to provide us with ongoing evidence about the robustness of their PPI complaint handling processes, the extent to which our provisions have been successfully embedded, and their success in generating fair and compliant assessments of (and where appropriate redress for) PPI complaints, and fair and clear communications with PPI complainants. As we noted in CP10/6, we are likely to seek assurance on these aspects through requests for information, including (but not limited to):

- samples of the firm's PPI complaint files;
- details of its governance structures, internal procedures and guidance, and quality assurance in place for PPI complaint handling (including e.g. any checklists or questionnaires used by the firm's staff when assessing PPI complaints and, where appropriate, calculating redress);
- papers and minutes from its senior management meetings discussing the handling of PPI complaints; and
- detailed information supplied to its senior management on PPI complaint handling operations and quality (e.g. about the firm's complaint volumes, the nature of its responses and the proportion it is upholding or rejecting, the redress it is paying out, and its experience at the FOS and the lessons it has learned from this).

4.5 More specifically, and in terms of timelines, we anticipate that our monitoring of PPI complaint handling will run along the following lines:

Stage 1 (Q3 2010): we will very shortly ask (as we flagged in CP10/6 p80) the 28 firms who have been reporting PPI data to us over the last three years to start providing more granular standardised information on PPI complaints to help us assess their compliance with our new Handbook provisions.

Stage 2 (Q4 2010): we will write to several firms (selected on a risk/impact basis) asking them for a detailed self-report on what steps they are taking to prepare for implementing the Handbook provisions (which we will then assess and, where appropriate, challenge).

Stage 3 (Q1 – Q3 2011): we will carry out (and/or potentially ask skilled persons to report on) detailed and intensive reviews (likely to include significant samples of recent PPI complaint files and responses) of the PPI complaint handling of several firms (selected on a risk/impact basis, including in terms of their self-reporting in Stage 2 and our other data and intelligence about them).

4.6 We will also undertake a staged approach to monitoring the robustness of firms' root cause analysis of PPI (see also paragraphs 2.18–2.20), but we will run this work one quarter year behind the complaint-focused work, that is:

Early Q1 2011: we will write to several firms (selected on a risk/impact basis) asking them for a detailed self-report on what root cause analysis they have done, the results of this, and what steps they are planning as a result concerning changing sales practices going forward and/or treating non-complainants fairly.

Q2 – Q4 2011: we will carry out (and/or potentially ask skilled persons to report on) detailed and intensive reviews of the approach to root cause analysis of several firms (again selected on a risk/impact basis) and, in particular, their consideration of, and where appropriate the scope and fairness of, their own initiative actions towards non-complainants, and the effectiveness of these actions in giving relevant non-complainants redress or proper opportunity to obtain it.

4.7 Meanwhile, we will also be monitoring the progress of the past business reviews we have already agreed (and of any others that we find to be necessary in due course as a result of our ongoing targeted sales assessment work).

4.8 In all these areas, where we find a firm cannot demonstrate it is delivering fair outcomes, it can expect tough action from us, including potential referral for further investigation and potentially enforcement action where appropriate, and steps to ensure it revisits all complaints and/or sales that it has failed to assess and address fairly.

Annex 1

Our cost-benefit analysis and assessment of other costs and benefits of our measures

Introduction

1. In this Annex, we present and respond to the main comments received on our cost-benefit analysis (CBA) of the proposed Handbook text and our assessment of the other costs and benefits of our measures.[1] We also present the impact on our CBA of responding to the comments we received, the further information these comments provided and the additional data that became available after the publication of CP10/6. We also discuss the impacts on the CBA resulting from the amendments to our proposals discussed in Chapters 2 and 3.

2. CP10/6 presented a revised CBA of our proposed complaint-handling guidance, as well as an assessment of the other costs and benefits associated with our measures. It presented further refinements to the CBA that had accompanied CP09/23, and recognised that the costs (and benefits) and the wider industry impact implied by our proposals would be significantly higher than those we set out in CP09/23. The key points of the CBA in CP10/6 were:

   - The main benefit of our proposals was an expected increase in redress paid to PPI complainants whose policies were mis-sold. We estimated that firms would incur additional costs over five years[2] of c.£583m to £1.0bn in redress costs, and administrative costs of c.£166m if we introduced the proposed Handbook text. This implied a total cost of our proposals to industry of c.£700m to £1.2bn over five years.

   - From our wider package of measures we anticipated further benefits, most notably to consumers who were mis-sold but who would not receive redress without these measures. We also noted that any reviews of past sales which firms may conduct in response to the measures might also lead to further benefits, through improvements in sales standards. We noted that the costs to industry of our wider package of measures would depend primarily on the extent to which firms decide, based on their root cause analysis of complaints and other information, to launch customer contact exercises for past PPI customers. We estimated that, if between

1 See Annex 2 and 3 of CP10/6 for the CBA and the assessment of the other costs and benefits of our measures.

2 We estimated that our proposals would lead to an incremental cost to firms (that is, costs above those which they would have borne without our proposals) over five years; see paragraphs 34-40, Annex 2, CP10/6.

25% and 75% of non-complainant customers who bought PPI policies since January 2005 were contacted and c.20% of these responded, this would lead to total industry redress costs of c.£0.9bn to £2.7bn and total administrative costs of c.£116m to £315m. This implied total costs of the wider package of measures of c.£1.0bn to £3.0bn.

- Finally, we assessed the possible prudential impact of our proposals on three sectors where concerns were raised to us in response to CP09/23: building societies, general insurance intermediaries and secured lenders. Assuming industry costs were at the top end of our ranges, we estimated that over five years, up to c.£40m and c.£120m of the total costs borne by general insurance intermediaries and secured lenders respectively could fall on the FSCS, and thus to levy-paying firms. We concluded that this was unlikely to lead to further prudential issues.

Summary of our final assessment of costs and benefits

3. This Annex incorporates additional information and responds to comments we received, as follows:

As a result of incorporating additional information reported to us by firms since CP10/6 was published:

- the total number of PPI complaints which we would expect firms to receive in our baseline case (i.e. before considering the impact of our package of measures) is now estimated to average c.500,000 per year for five years (from c.450,000 per year in CP 10/6) – reflecting the fact that the number of complaints received by firms in 2010 has been greater than anticipated. Accordingly, we now estimate that after our provisions come into force, the total number of PPI complaints to firms will average c.550,000 per year for five years (from c.500,000 per year in CP10/6);
- the ratio of single premium complaints to firms to regular premium complaints to firms is now 55% to 45% (instead of 58% to 42%), based on updated firm data on the mix of complaints which they currently receive; and
- our estimate of the average uphold rate for regular premium complaints in the baseline case is now 48% (from 33%); this is driven in particular by an increase in some firms' uphold rates for credit card PPI complaints.

As a result of responding to comments received on CP10/6:

- in the baseline case, the average firm redress for single premium complaints is now estimated to be c.£1,800 (instead of c.£2,000) (see paragraph 23 below);
- in the baseline case, the average firm redress for regular premium complaints is now estimated to be c.£900 (instead of c.£735) (see paragraph 23 below); and
- we have now quantified the expected impact of our guidance on refinanced sales; as a result of this, our estimate of redress costs over five years (including FOS referral costs) for second-charge mortgage PPI complaints is now greater by c.£50m to £60m, or c.12% (see paragraph 24 below).

We have updated our assessment of the prudential impact of our provisions, based on the above changes to our cost estimates and further information on the sectors where prudential concerns were raised to us. As a result of these updates:

- our estimate of the number of general insurance intermediaries that may fail as a direct result of our proposals is now c.35 (instead of c.100 in CP10/6), and the associated costs that may pass through the FSCS to levy firms is now c.£35m (compared to c.£40m in CP10/6); and
- the estimated cost that may pass through the FSCS to levy firms from secured lenders (where these lenders fail as a direct result of our proposals) is now c.£80m (compared to c.£120m in CP10/6).

4. We have considered the changes made to our Handbook text (as explained in Chapter 3) and we do not consider that these changes are 'significant' within s.155(6) of the Financial Services and Markets Act 2000 (FSMA).[3] We have considered each of the changes and have concluded that none would materially change the costs presented in CP10/6.

   The main Handbook amendments and our consideration of their impacts on the CBA are:

   - The Handbook text clarifies that the redress remedies we set out in CP10/6 are not exhaustive. We provide some examples where alternative remedies to the comparative redress approach might be appropriate and fair – see paragraph 3.22 of Chapter 3 for details. We anticipate that such different approaches will be the 'exception not the rule' for firms when dealing with a complaint satisfactorily. Therefore, we expect the impact of this clarification on the CBA to be small.
   - We have changed some Handbook provisions from Guidance to Evidential Provisions. Since our CBA in CP10/6 assumed that all firms would follow the proposed guidance, the CBA in CP10/6 does not need to be revised to take this change into account.

5. Finally, we have also considered the regulatory costs to us that may arise from monitoring and enforcement measures related to these proposals.[4] We conclude that our current measures should not cause additional regulatory costs to us above those which would be incurred if we were not to proceed with these measures, and therefore we have not increased the cost estimates in our CBA to reflect these costs.[5]

6. Based on the above, our estimate for the cost of our complaint-handling proposals to industry is now between c.£0.8bn and £1.3bn over five years (from c.£0.7bn to £1.2bn in CP10/6), and the estimated total cost of our wider package of measures is now between c.£1.1bn and £3.2bn (from c.£1.0bn to £3.0bn in CP10/6). We would reiterate the point made in CP10/6 that these costs are not strictly additive.[6]

---

3 And so we are not required by FSMA to publish details of the changes together with a cost benefit analysis.

4 See Chapter 4 for further discussion.

5 Costs to firms of monitoring were included in our estimates of administrative costs in the CBA in CP10/6; see paragraph 21, Annex 2, CP10/6.

6 See paragraph 4.7, p.63, CP10/6 for further details.

In addition, since the increase in cost is largely due to an increase in redress costs, which are a transfer from firms to consumers, the total benefit to consumers also increases.

Responses to our CBA and to our assessment of the other costs and benefits of our measures

7. The remainder of this Annex discusses the main comments received on our CBA and on our assessment of the other costs and benefits of our measures. We also discuss how we have reflected these comments in our final assessments of costs and benefits. A significant number of responses touched on the CBA and wider impacts – some addressing these directly, others addressing issues closely related to them. Here we present the substantive comments and our considered responses to these.

8. It should be borne in mind that the purpose of a CBA is to assess (in quantitative terms where possible and in qualitative terms where not) the economic costs and benefits of a proposed policy. Specifically, under FSMA[7] a CBA is 'an estimate of the costs together with an analysis of the benefits'. In line with this, we have estimated costs wherever possible. We have done this using the data reasonably available to us from a range of sources including: information received from individual financial institutions, including comments raised by firms in response to CP10/6 and CP09/23; past enforcement cases related to complaint handling; and discussions with specialist consultancies with experience of PPI complaint-handling projects.

Analysis of the benefits of our complaint-handling provisions

9. In CP10/6 we asked:

> Q18: Do you agree that our proposed complaint handling guidance will bring the benefits described in this CP (including in the cost-benefit analysis at Annex 2)?

10. Responses from consumer representatives were supportive of our assessment of the benefits of our proposals. Some industry responses agreed that the proposed guidance would bring about the benefits we anticipated, notably redress for consumers whose policies have been mis-sold. However, on the whole responses from industry disagreed with our assessment of the benefits of our proposed Handbook text. The main comments received are discussed below.

11. Several responses reiterated comments made in response to CP09/23 that a significant part of redress will go to Claims Management Companies (CMCs). They argued that this undermines our claim that redress paid is a fairness-driven transfer to mis-sold consumers and thus, that our CBA overstates the benefits of our proposals.

Our response: We set out in CP10/6[8] why we do not agree with this argument and responses to CP10/6 did not present new arguments in support of it. Where customers pay for a policy that was mis-sold, the payment of redress is a transfer driven by fairness. In

7 Section 155(10).
8 Chapter 4, para.8 (b) response.

cases where a customer has complained through a CMC, this choice has been made to serve their interests.[9] Hiring a CMC is a secondary transaction, which is a matter for customers (i.e. it is up to consumers to decide how to spend redress they may receive). In our view it does not alter the fairness of the redress paid by firms to consumers.

12. Some industry responses argued that, since some redress will go to customers whose policies were not mis-sold, the benefits in the CBA are overstated.

Our response: This argument stemmed in some cases from the assertion that our view of sales failings is retrospective, and that our proposals would lead to complaints being upheld which were compliant according to regulatory requirements at the time of the sale. Other industry responses argued that our evidential standards are unfairly weighted in favour of the consumer, and so do not allow firms to reject complaints even where the sale was compliant. We do not agree with these assertions, and we deal with these points in Chapters 2 and 3.

In CP10/6 we estimated the costs and benefits of redressing complainants on the assumption that firms will investigate complaints carefully against the standards outlined in the CP. As such, our assessment of redress costs (and resultant benefits) reflected redress on mis-sold policies only. Even if some firms make a commercial decision to uphold complaints without investigation (notwithstanding our comments on evidential standards above), this does not imply that our assessment of benefits is overstated, since this does not reduce the benefits which we anticipate from redressing mis-sold policies.

For these reasons, we do not think that the possibility of customers receiving redress whose policies were not mis-sold undermines our assessment of the benefits of our provisions.

13. A number of responses argued that our proposals would lead to additional customers being encouraged to complain, which would lead some of these customers to lose valuable protection cover if their policies are cancelled when receiving redress. These responses suggested that this diminishes the benefits stated in the CBA.

Our response: This argument stems partly from the industry's assertion that our provisions will lead to a large increase in the number of spurious complaints. We do not agree with this view, as we discuss in paragraph 17 below.

We also addressed this point in CP10/6.[10] As we stated there, we do not consider that a consumer who has been mis-sold in a way which, based on our Handbook provisions, warrants redress equivalent to the return of all their premiums, can really be said to have lost a benefit if their policy is cancelled. Moreover, our measures should ensure firms explain to customers the consequences of accepting any redress offer. Also, for single premium policies the comparative approach specifically ensures that consumers have the opportunity to maintain their cover where it is appropriate and the customer wishes to do so (see Chapter 3). Based on these points, we do not accept that the risk of customers losing protection reduces the benefits we reported in the CBA.

---

9 For example, where the customer perceives that using a CMC facilitates the receipt of redress and/or relieves them of the work and effort they would otherwise need to expend.

10 See paragraph 4.8, CP10/6.

Estimated redress costs to industry of our complaint-handling provisions

14. In CP10/6 we asked:

> Q19: Do you agree that our underlying assumptions about redress costs for PPI complaints are appropriate? Do you agree with our resultant estimates of these redress costs? What additional data can you provide to support any further refinements to these assumptions and/or estimates?

15. Responses from consumer representatives did not comment in detail on our redress cost estimates. However, responses from industry were generally critical of our assessments. The main comments received are discussed below.

16. Many responses expressed concern that our proposals regarding consequential loss could lead to significant additional costs for firms, and that these costs were not quantified in the CBA in CP10/6.

> **Our response:** Some industry responses on this implied a misunderstanding by respondents of the scope and intention of our draft guidance on consequential loss. To remedy this, we have clarified the (limited) application and scope that we had in mind – see Chapter 3 (paragraph 3.43) for further discussion of our response and DISP App 3.9.2 G of the final Handbook text.
>
> We have also assessed the potential impact of awards of consequential loss on the estimated redress costs faced by firms, through discussions with the FOS and by reviewing a number of FOS cases that were upheld in favour of the customer. Based on this sample, we consider it likely that redress for consequential losses will be awarded in less than 5% of cases, and also anticipate that awards will generally be low relative to the overall redress to be paid. Given this, we believe that redress related to consequential losses should not materially increase costs over those estimated in CP10/6. The likely low incidence of awards for consequential loss, and the low amounts of redress involved, should also avoid incentivising additional complaints or complaints for inflated amounts from CMCs or other parties – a further concern that was raised in some of the responses.
>
> For these reasons, we have not revised our cost estimate in our CBA in response to these comments.

17. A number of industry responses argued that the CBA underestimates the impact of our proposals on complaint volumes. In particular, responses claimed that the proposals incentivise spurious complaints, for example through CMCs, because they unduly raise the evidential standard required of firms to reject a complaint.

Our response: CP10/6 stated that complaint volumes have increased significantly since 2008, in part due to ongoing CMC activity and publicity on PPI. We noted that we would expect this increase to continue in the short term at least, even without our complaint-handling provisions. We also explained that our proposals may lead to a small increase in complaint volumes, arising from any publicity surrounding our proposals.[11]

We believe that the CBA in CP10/6 appropriately estimates the impact of our proposals on complaint volumes. As discussed in Chapter 3, we do not accept that our provisions prevent a firm from making a fair assessment of a PPI sales complaint (indeed the purpose of the provisions is to encourage firms to make a fair assessment), or from fairly rejecting such a complaint where that is appropriate. So we do not believe that our provisions increase incentives for complainants (through CMCs or otherwise) to submit spurious complaints. If increased numbers of spurious complaints were to be submitted, we would expect firms (and later the FOS, if these cases were referred to it) to reject these complaints. As a result, it should become widely recognized that it is not in complainants' interests to submit unmeritorious complaints. Given this, we do not believe that our proposals would encourage spurious complaints and lead to a material increase in the redress or administrative cost estimates we provided in CP10/6.

18. In the CBA to CP10/6 we assumed that 50% of upheld single premium complaints would receive redress following the comparative approach rather than receiving full redress. Some responses argued that this underestimates the proportion of cases that would receive full redress and so underestimates costs to firms.

Our response: In view of these responses, we have re-visited our original assumption of 50% to assess whether this remained an appropriate assumption on which to base our cost estimates. We recognise that this assumption is subject to some uncertainty – in particular, the proportion of complaints for which comparative redress is appropriate will depend on the nature of the complaints received, and ultimately on firms' historical sales practices, including the frequency of multiple failings in sales. As a proxy for the cases that would be received by firms, we analysed a sample of 46 single premium PPI cases (across 10 firms) that were considered and upheld by the FOS.[12] While recognising that this sample is limited and may not be entirely representative of firms' experience, our analysis of these cases supported our assumption that up to around 50% of single premium cases could be appropriately redressed using the comparative redress approach. Consequently, we have not revised this assumption in our CBA.

19. Some responses argued that the CBA should be revised so that firms' uphold rates for complaints after implementing our provisions are in line with current FOS uphold rates.

11 See paragraph 12, Annex 2, CP10/6.
12 We note that these cases were adjudicated on by the FOS before we published CP09/23 and CP10/6.

Our response: In CP10/6 we estimated redress costs associated with implementing our proposed Handbook text for two scenarios, low-impact and high-impact. Under the low-impact scenario, firms' uphold rates are estimated to be 75% and 70% respectively for single premium and regular premium products (excluding first charge mortgages). Under the high-impact scenario, firms' uphold rates are estimated to be 90% and 85% respectively for single premium and regular premium products (excluding first charge mortgages). The uphold rates used for our high-impact scenario are very close to current FOS uphold rates, which for the last two financial years averaged 89% across all PPI products.

As explained in CP10/6[13], we do not believe that current FOS uphold rates are necessarily a direct benchmark for future firm uphold rates, as cases going to the FOS may not be fully representative of the cases received by firms. In particular, it is reasonable to assume that customers with more meritorious complaints are more likely to persist with them, making it plausible that complaints considered by the FOS are more likely to be meritorious and so upheld, than those from the whole population of complaints received by firms.[14] As a result, we have not revised our uphold rate assumptions in the CBA.

20. One response argued that, given the evidential standards outlined in CP10/6, it may be uneconomic for some firms to assess complaints; some firms may therefore offer full redress on all complaints independent of merit, thereby increasing costs to industry beyond those set out in the CBA. Similarly, another response suggested that firms who sold retail credit PPI would be disincentivised from defending mis-selling complaints on these sales, as the average premium is lower than the £500 FOS case fee; the response suggested that this may lead to uphold rates and redress costs higher than estimated in our CBA.

Our response: We address the issue of evidential standards elsewhere in this Policy Statement (see Chapter 3). Beyond this, it is up to firms to determine the most cost-effective approach to take in responding to the proposed measures. We would only anticipate firms' automatically upholding complaints where this lowers their total costs (including the cost of cases referred to the FOS). For this reason, we believe that the relevant redress and administrative cost estimates in CP10/6 remain reasonable.

21. One response expressed the concern that the firm uphold rates in the CBA could become targets.

Our response: The uphold rates in the CBA in CP10/6 (which we have retained in the present CBA) are not targets, but represent our estimates of the average uphold rates which firms may experience after implementing our provisions. Treating these as targets would not necessarily ensure firms are meeting the standards set out in this Policy Statement. We have made it clear that firms should review each individual complaint in the round, in line with their obligations, including with reference to the standards we outline in this Policy Statement. We would also reiterate that our monitoring work

13 See paragraph 4.13, CP10/6.

14 We also note that in the first three months of the current financial year, FOS uphold rates across PPI products averaged 81% (see http://www.financial-ombudsman.org.uk/publications/ombudsman-news/87/87-quarterly-account.htm) which falls within the range of firm uphold rates that we have modelled.

will focus on whether firms are assessing complaints fairly, rather than simply testing whether uphold rates are in line with our estimates (see also Chapter 4).

22. Two responses questioned our assumption that the uphold rate for PPI cases received by the FOS would decrease to 40% after our provisions come into effect.

Our response: In the last two financial years, on average 89% of the PPI complaints referred to the FOS were upheld in the complainant's favour. In CP10/6, we estimated that after the implementation of our proposals, 40% of complaints referred to the FOS will be upheld.[15] We explained in CP10/6 that this is because, when firms are assessing and redressing complaints properly against our complaint-handling provisions, we expect a significant reduction in the number of complaints wrongly rejected by firms. This is also likely to significantly reduce the FOS uphold rate for referred complaints over time. In CP10/6, we assumed the uphold rate on cases referred to the FOS would be likely to fall into line with that of other insurance products, which lies between 30% and 50% – 40% was taken as an average uphold rate from this range. We remain of the view that this is an appropriately conservative estimate.

23. One response questioned the accuracy of our estimate of the average redress currently paid by firms on upheld complaints.

Our response: The estimates for current average redress included in CP10/6 were based on data submitted by 28 distributors, which we requested having reviewed responses to CP09/23. These represent average redress paid for complaints upheld by firms (i.e. excluding cases referred to, and upheld by, the FOS).

On rechecking our previous estimates, we also identified some firm data that we had omitted from our previous calculations. We have now revised our estimates taking this additional data into account. Based on this we have revised our estimates of average redress in the baseline case from c.£2,000 to c.£1,800 for single premium policies, and from c.£735 to c.£900 for regular premium policies.

24. One response commented that our CBA in CP10/6 did not quantify the cost of firms assessing previous sales of PPI, where the cost of these was later rolled up into another loan through refinancing, and where the sale of the PPI policy attached to this later loan was the subject of a complaint.[16]

15 See A2:5, Annex 2, CP10/6.
16 See DISP App 3.2.7 G of the final Handbook text.

Our response: We now include an estimate of these costs for second-charge mortgage PPI (as set out in paragraph 3 above). We focused on second-charge mortgage PPI as we understand that refinancing for this product is more common than for other single premium products. This is for three reasons: the longer average term for second-charge loans compared to other loan products on which single premium PPI was sold; the customer demographic to which the product is sold; and the fact that some secured lenders insist on loans being refinanced when a customer requests further funds, rather than making a second, separate loan that would run in parallel to the first. Since other single premium products do not generally share these features, we do not expect our provisions on refinancing to materially change our cost estimates for these other products.

Making the revision for second-charge mortgage PPI increases our redress cost estimates for second-charge mortgage PPI by between c.£50m and £60m (or c.12%) over five years. We have also taken this into account in updating our prudential assessment for the secured lending sector, and our estimates of the costs that might potentially be borne by the FSCS (see paragraphs 45 to 50 below).

25. One response suggested that the regular premium presumption is not appropriate for sub-prime consumers because regular premium PPI is unsuitable for them. This is because sub-prime customers tend to miss more loan repayments than prime borrowers and would therefore also miss regular premium payments, resulting in the regular premium policy being cancelled by the insurer. The response indicated that our redress cost estimates should be increased to reflect the fact that sub-prime customers are more likely to be offered full redress than prime customers.

Our response: DISP App 3.7.7E sets out when we believe it is reasonable for a firm to presume that the complainant would have bought a regular premium payment protection contract. If firms follow this provision, then it is the nature of the firms' failings and the evidence that the firms have to rebut the presumptions that will determine which customers should be offered comparative redress.

Consequently, we do not believe it necessary to change our assumptions on the proportion of customers offered comparative redress.

26. One response, from an insurer, argued that where firms offer consumers a choice (as part of the comparative approach to redress) of whether or not to maintain ongoing cover, they will face issues with adverse selection that will increase their costs.

Our response: We understand the risk of adverse selection as high risk complainants opting to retain cover while low risk complainants elect not to maintain cover (perhaps deciding to obtain cover through a standalone PPI provider).

Having considered this point, we believe that adverse selection issues arising as a direct result of our proposals should be limited. This is because, for those consumers who choose to continue their policies under comparative redress, our policies should make no difference to insurers' positions, as the single premium policies were originally intended to carry on for the duration anyway (without our proposals). The customers who will create a risk of adverse selection are expected to be a limited subset of the total insurance book – this group comprises only those customers who have complained and had their complaint upheld, and who have been offered comparative redress, accepted this and opted to maintain cover (notwithstanding cheaper cover available elsewhere), and did so mainly because they believed they may struggle to get cover afresh, e.g. because of changed circumstances since the original sale. We do not view this population as sufficiently large in the context of the industry's overall insurance sales to create material adverse selection; hence we do not believe that adverse selection would have a material impact on our industry-level cost estimates.

27. Some responses mentioned that setting a referent price at £9 for comparative redress would have adverse competition effects, since it sends a regulatory signal as to what the 'correct' price should be for PPI products.

Our response: We set out in CP10/6 our position on this question,[17] and in particular we explained that the proposed referent price is not an intervention in, or a 'fix' of, the pricing of insurance cover. It is a specific tool designed to help the calculation of fair redress to establish a fair approach that is workable for large complaint volumes. From this perspective, the referent price should certainly not be considered as our view of a 'fair price' in this market.

Some responses also suggested that this 'fixing' of prices in the PPI market may occur as an unintended consequence of our measures, even if this was not our intention. Responses, however, did not provide any detailed assessment of why this might occur. We see little reason why a firm would set its PPI price to the referent price rather than pricing by taking into account the risks of claims, other costs and competitor activity in the market. We also do not expect (or intend) consumers of PPI to think of the referent price as the 'fair price' for a PPI product. Given this, we do not expect market pressures to materialise that would lead to a convergence of the price of PPI products to the referent price.

Consequently, having considered this point we do not think it necessitates a revision to our CBA.

28. In addition to considering the comments raised in consultation responses, we have also reviewed our redress cost assumptions to reflect additional monthly data (from 18 major distributors of PPI) received since we completed the CBA in CP10/6. This more recent data has led us to reassess our estimate of firms' current uphold rates for PPI complaints. Based on firms' most recent returns to us, our estimates of firms' current uphold rates now average 54% (from an average of 46% in CP10/6). Most of this difference is due to increased uphold rates on credit card PPI complaints, which have increased from c.25% to c.50% at present.[18] We have made two other revisions to redress costs from incorporating more recent data: we revised the expected complaint volumes upwards by 50,000 and updated the ratios of single premium to regular premium complaints to firms, reflecting updated information on the mix of complaints currently received by firms (see paragraph 3 of this Annex for further details).

17 See paragraph 3.33 of CP10/6 for further details.

18 In 2009, complaints on credit cards represented c.30% of all complaints received by firms (based on data reported to us by 18 major PPI distributors).

Estimated administrative costs to industry of our complaint handling provisions

29. In CP10/6 we asked:

> Q20: Do you agree that our underlying assumptions about administrative costs for PPI complaint handling are appropriate? Do you agree with our resultant estimates of these administrative costs? What additional data can you provide to support any further refinements to these assumptions and/or estimates?

30. Responses from consumer representatives did not comment in detail on our estimates of administrative costs. Responses from industry included some disagreement with our assessment of administrative costs, although we received fewer comments on this compared to our estimates of redress costs. The main comments we received are discussed below.

31. Several responses stated that administrative costs may be higher than we estimated because firms will be fighting for the same, potentially limited resources.

Our response: We do not expect firms fighting for the same resource pool to have a significant impact on costs for several reasons. First, our estimates of staff costs are unlikely to be affected by competition for resources. Most of the work required does not require highly specialist skills; given this, the number of additional FTEs[19] required (c.491 for distributors, and c.153 for other firms) is not large enough to drive up wages, since this is small relative to the available supply of adequately qualified staff, especially in the current economic environment.[20]

Second, many firms' IT costs are likely to be limited by existing contractual agreements or by having some existing in-house IT resources that can be devoted to this. Firms that use specialist IT providers may experience some increase in costs. For these firms, the extent of any cost increase will depend on the extent of competition between IT providers, and on individual negotiations between firms and IT providers. The impact of these factors is inherently difficult to predict (and responses to CP10/6 did not provide detailed information which would allow us to quantify any likely cost increases); given this, and given that these additional costs may only apply to a limited proportion of the PPI market, we have decided not to revise our estimates of firms' IT costs in light of the comments received.

Finally, any additional costs arising from firms implementing our provisions at the same time should be partly mitigated by the extension to our implementation timetable, which we discuss in Chapter 4.

For these reasons, we do not believe that a revision to our estimates of administrative costs is required.

32. Several firms responded that administrative costs attached to the implementation of comparative redress would be higher than we stated.

19 Full time equivalent staff.

20 Also, larger firms may be able to negotiate lower agency fees where they are recruiting significant numbers of new complaint handlers.

Our response: In some cases, this assertion appeared to stem from misunderstandings as to how the comparative redress approach would work in practice. We refer readers to Chapter 3 for further discussion.

Respondents did not give detailed information to support revisions to our estimates for administrative costs. Our initial estimates of administrative costs were based on discussions with firms and outsourcing experts, and we continue to believe that these are generally appropriate for the market. Also, as noted in Chapter 3, since the menu of implementation options retains the status of guidance rather than Evidential Provisions, firms may develop alternative ways of operationalising comparative redress if they consider these approaches more practicable or more cost-effective (so long as the outcomes are fair and commensurate with those in our final provisions).

33. Two responses argued that the time taken to handle complaints may be significantly longer than we indicated in our CBA.

Our response: Our estimates of the administrative time required for firms to deal with PPI complaints are based on data available to us: past enforcement cases related to complaint handling; discussions with specialist consultancies with experience of PPI complaint handling projects; and information received from individual financial institutions, including comments raised by firms on expected administrative costs in responses to CP09/23. It is to be expected that the length of time taken for firms to assess complaints may vary, based on e.g. the details of their complaint-handling processes and data storage/retrieval processes. We also note that the majority of industry responses did not comment on this assumption. Therefore, taking all of this into account, we continue to believe that the average times estimated in CP10/6 remain appropriate for the market as a whole.

34. Some responses commented that there would be administrative costs to third party firms to assist other firms in responding to a complaint, e.g. in providing information about claims, or in assisting in restructuring loans. These responses allege that these costs have not been adequately estimated in the CBA.

Our response: Generally, we expect only a small proportion of administrative costs relative to total costs to fall on third party firms, since most of the administrative cost of assessing and paying redress of complaints falls on firms receiving complaints.

As set out in CP10/6,[21] we have included an estimate in our CBA for the staff costs incurred by third party firms (we estimate that these third party firms would be required to take on c.153 additional FTEs as a result of our provisions). Respondents did not provide detailed information to substantiate claims that this estimate of staff costs was too low.

We also do not expect significant changes to third party firms' systems to be required to facilitate this exchange of information, since the information to be provided should be readily available. Where firms in a sales chain charge fees to other firms to cover the costs of the provision of information, this should not materially affect the

21 Annex 2, para.23, CP10/6.

overall cost to industry of our provisions, as (given their commercial and regulatory interests) the fee charged by the firm should be reasonable (see also Chapter 3), and we estimated the cost of the administrative burden to firms in our CBA.

Regarding the data protection implications of information sharing between firms in a sales chain, see the discussion of this in Chapter 3. We are satisfied that firms could share information in the way envisaged by our proposals in compliance with the Data Protection Act 1998 without incurring significant additional costs.

Therefore, we have not revised our cost estimates to reflect additional administrative costs for third party firms.

35. One response questioned our analysis of the Consumer Credit Act (CCA), and suggested that we had underestimated the administrative costs arising from firms' obligations under the CCA when applying redress to a loan.

Our response: We have assessed the potential administrative costs which may arise from the implications of the CCA. We do not believe that complying with the CCA will entail material administrative costs above those which we have already accounted for in our cost estimates. See also Appendix 3.

36. In addition to considering the comments received on our estimates of administrative costs, we have also updated our administrative cost estimates to reflect the increase in our estimates of future complaint volumes (see paragraph 3 of this Annex for further details).

Other costs and benefits of our measures

37. In CP10/6 we asked:

Q21: Do you agree with our assessment of the wider impact of our package of measures on industry?

38. Responses from consumer representatives generally agreed with our assessment of the benefits of our package of measures; these responses did not comment in detail on our cost assumptions. Responses from industry were critical of our assessment of the benefits of our measures. We received fewer comments from industry on the cost estimates for our wider package of measures than on our complaint-handling guidance – although where comments were received, these were again generally critical of our assessment, arguing that we had underestimated the potential costs to industry and therefore the prudential implications of our proposals.

39. A number of the comments made on the redress and administrative costs of our complaint-handling guidance also apply to our assumptions regarding the impact of our wider package of measures – we refer readers to our responses in the previous sections. As regards the administrative costs associated with our wider package of measures, we recognised in CP10/6 that additional staff would be needed were firms to conduct reviews of sales to non-complainants (c.1,600-4,800 FTE in total, each for a period of around one year). We reconfirm that this estimate includes additional

staff both for firms responding to complaints and for third party firms. As per our estimates of staff costs for future complaints (see paragraph 31 above), we believe that there remains a sufficient labour supply of adequately qualified staff to meet this demand, especially in the current economic environment. We also note that our estimates of staff costs in CP10/6 were conservative, and so do not believe that it is necessary to increase these estimates.

40. Responses also made comments specific to our assessment of the costs and benefits of our wider package of measures. We discuss the main comments received and our responses to them below.

41. Two responses suggested that the c.20% average response rate for customer contact exercises was too low. These responses suggested that any customer contact exercises stemming from our measures would take place under circumstances that would be materially different from the PPI sales reviews on which our estimates of response rates were based.[22]

Our response: We interpret respondents' primary concern to be that media attention, and the activities of CMCs in particular, may have a greater impact on response rates than in previous PBRs. We explained in CP10/6 why we believed a 20% response rate was appropriate.[23] The 20% average response rate was based on recent Past Business Reviews (PBRs) on PPI sales. We also took into account differences in expected response rates among PPI products, based as far as possible on data from previous PPI PBRs.

As discussed in Chapter 2 (part D) and in DISP App 3.4.3G of our final Handbook text, customer contact exercises are not the only action that firms may take to address recurrent issues they have found with their sales practices. Where firms do conduct these contact exercises, we do not expect response rates to be significantly different to those from previous PBRs: given the already widespread media attention[24] on problems with PPI sales at the time of previous PBRs, e.g. around FSA enforcement actions, reports by consumer groups and the Competition Commission's ongoing inquiry into PPI, we do not expect the current media focus on PPI to lead to significantly higher response rates. In addition, we do not expect CMC activity to play as significant a role with reviews of sales to non-complainants as in customer complaints (even though CMCs may launch additional marketing initiatives to encourage consumers to respond via CMCs rather than directly to the firm). This is because customer contact exercises are initiated by firms, and we expect firms' contact letters will outline the steps required for customers to respond in person; this is likely to limit customers' use of CMCs. For these reasons we think the existing response rate estimates remain appropriate and we have not revised these assumptions in our CBA.

42. Two responses mentioned that since PPI cross-subsidises loans, there will be costs to firms (which may be passed on to customers) if significant numbers of PPI policies are unwound.

22 See paragraph 4.31, p. 71, CP10/6.
23 See paragraphs 11 and 12, Annex 3, CP10/6.
24 See also paragraph 12, Annex 2, CP10/6 in the discussion of complaint volumes.

Our response: We acknowledged in CP10/6 that where firms incur additional redress and administrative costs as a result of our proposals, they may attempt to pass these through to customers, depending on the specifics of competition.[25] This also applies where sales of PPI have historically cross-subsidised loans. How and to what extent any cost pass-through occurs depends on multiple commercial factors and specifics of the market, which makes precise estimation of costs difficult. Also, since cross-subsidisation is a market distortion, to the extent that our provisions reduce it, prices of loans should more closely reflect undistorted supply and demand, to the general benefit of the loan market.

43. One response (from a distributor) argued that the reduction in the incentive to mis-sell does not apply to firms in the sales chain other than the distributor (because it is the distributor who is liable for redress). In addition, another response (from an underwriter) suggested that some costs would unfairly fall on firms not party to the (mis-)sale of PPI, both through administrative costs incurred by other firms in the sales chains, and from the costs passed through to levy funding firms where redress claims are met by the FSCS.

Our response: We deal with the issue of allocation of liability in Chapter 2 (see part G). Our proposals and our wider package of measures are aimed primarily at improving distributors' conduct at the point-of-sale and redressing consumers who were mis-sold.

Notwithstanding this, we expect that there may also be some indirect incentives for others in the sales chain flowing from our measures, even though they may not directly bear a significant proportion of the costs associated with redress. For example, distributors may exert influence on providers/lenders by choosing those whose products, sales processes or incentive mechanisms make it easier or more cost-effective to sell PPI compliantly. These indirect impacts should also contribute to an improvement in PPI sales standards, which would lead to further benefits from our proposals.[26]

We accept that underwriters and other firms in the sales chain may incur some administrative costs (notably staff costs, as discussed in paragraph 34 above) in providing information to distributors. However, we expect these to be generally small, and (as per current practice for some firms) these could potentially be recouped by agreements between distributors and other firms on appropriate fees for providing this data. Given the relatively low costs incurred by other firms in the sales chain, this does not alter or undermine our view that the package of measures we propose (including our specific proposals around redress) is the most proportionate response to the issues we are seeking to address in the PPI market.

We estimated in CP10/6 the level of costs that may fall to the FSCS,[27] and so to its levy funding firms. While some costs may thus be borne by firms who did not themselves (mis-) sell PPI, this is inherent in the FSCS funding model.

44. Several responses argued that our package of measures would cause further, unjustified damage to the reputation of PPI, and would therefore affect market confidence.

25 See Annex 2, CP10/6.
26 We allude to these benefits in CP10/6 at paragraph 4.48 and paragraph 8 of Annex 3; see also paragraph 1 of Annex 2 relating to the complaint handling proposals consulted on.
27 See CP10/6, in particular paragraphs 2.24 and 4.46 and paragraphs 2, 48 and 53-56 of Annex 3.

Responses also argued that this would reduce firms' willingness to compete in this market (so limiting consumer choice) and, by reducing future take-up of PPI, would leave future customers' protection needs unmet.

Our response: In many cases respondents attributed these effects to other elements of our proposals that they viewed as inappropriate, most notably the alleged retrospectivity of our list of sales failings (which some responses said may stop firms from participating in the market for fear of later retrospective action) and our evidential standards changing the burden of proof so that firms would be unable to reject complaints. We explain elsewhere in this policy statement why we do not agree with these assertions (see Chapters 2 and 3). Although we do not agree with the premise behind the comments made, there are additional points which flow from these comments that we address below.

Although the publicity surrounding our provisions may lead to some further reputational damage for PPI, for the reasons discussed above, we do not accept that any such reputational damage would be unjustified or that it in any way undermines the proportionality of our actions. Also, as discussed in CP10/6,[28] we do not expect the impact of this publicity to be significant, since it follows publicity already generated over several years, both from our own actions (including thematic reviews and Enforcement actions) and from the activities of, for example, CMCs and consumer activist forums.

To the extent that reduced take-up of PPI reflects a reduction in mis-sold PPI products, this is a benefit. As we noted in CP10/6, where firms improve their sales and complaint handling practices in line with our provisions, we would expect this to improve the reputation of PPI and to improve market confidence more generally.

We also discussed in CP10/6 the potential impacts of our measures on competition in the PPI market.[29] Here we would add that – as regards reputation – potential new entrants have the opportunity to enter the PPI market, or the market for other protection products which meet similar consumer needs and which have not received the same negative media attention as PPI.

Given all these points, we do not expect future consumer choice to be significantly reduced or consumers' protection needs to be unmet as a result of our provisions.

Assessing the prudential implications of our package of measures

45. Some responses claimed that the prudential implications of our proposals may be higher than estimated in the CBA in CP10/6, based on their views that the redress costs would be higher than estimated. Responses also asserted that, as a result, our CBA had also underestimated the costs which would flow to the FSCS and to levy firms.

Our response: For reasons set out above, we believe our estimates of the redress costs in the CBA remain reasonable, and we do not believe that our assessments of prudential impacts need to be revisited in light of changes to the estimated redress costs. We have, however, revised our prudential analysis in the CBA to reflect changes based on additional information received since we published CP10/6. These revisions are set out below (see in particular paragraphs 49 and 50).

28 See in particular paragraph 12, Annex 2, CP10/6.
29 See Annex 2, CP10/6.

46. Two responses asserted that the impact on the FSCS from redressing claims from specialist finance brokers who are no longer in business will be greater than we estimated in our CBA.

Our response: Of the c.50,000 additional annual complaints which we expect to result from our provisions, it is possible that some proportion of these may fall to the FSCS, where these are made against firms already out of business. However, the costs arising from these complaints are unlikely to be material compared to the other costs which may fall to the FSCS, as we outline in paragraphs 49 and 50 below. Moreover, for customer complaints received by the FSCS, we do not expect the FSCS to change its approach to handling cases based on our provisions, since the failures we identified in firms' PPI complaints handling practices should not generally apply to it.[30] Given this, we do not expect any material change in the proportion of complaints that the FSCS upholds or in the average redress paid out.

We also do not expect our provisions to result in significant additional costs for the FSCS from reviews of past sales, since we do not expect the FSCS to launch past sales reviews for exited firms over and above those which they might have launched in the absence of our provisions.

47. Two responses suggested that a higher proportion of smaller firms than we estimated may be declared in default because of the cumulative impact of our provisions and other measures, notably the Retail Distribution Review (RDR).

Our response: Our recent publications on the RDR have set out incremental cost estimates for RDR proposals.[31] Any combined impact (of our RDR proposals and our PPI measures) would only affect those financial advisers who provide investment advice as well as selling PPI. Only around a third of retail intermediaries hold permissions to sell both general insurance and investment products. Moreover, of those firms whose most recent annual returns indicate that they have sold PPI, the vast majority (more than 95%) do not hold an investment advice permission. This suggests that the additional impact of the RDR measures on the prudential effects of our PPI provisions on firms and the FSCS is likely to be limited.

48. Some responses argued that exit from the market by intermediaries and secured lenders would lead to reduced consumer choice and reduced access to credit, and suggested that our CBA had not provided sufficient explanation of why this would not occur.

30 This is supported by the FSCS's latest Annual Report and Accounts, which states (p.29) that in the year to 31 March 2010, the FSCS paid out compensation on 89% of PPI claims it receives. See www.fscs.org.uk/uploaded_files/Publications/Annual_Reports/annual_report_2009-10.pdf.

31 See p.9, '*FSA estimate of incremental compliance costs for Retail Distribution Review proposals*', March 2010. Also, see CP09/18 and PS10/6 for a more general discussion.

Our response: As discussed in CP10/6 and analysed in the CBA there, we expect our PPI provisions to have prudential impacts on General Insurance (GI) intermediaries and secured lenders. (The category 'General Insurance intermediaries' includes loan brokers, and also retailers who sell insurance alongside their core product, e.g. motor retailers who also sell PPI on car finance loans.) We have revised our estimates related to these sectors, as outlined below.

As discussed in paragraph 49 below, we now estimate that around 35-40 GI intermediaries may be required to raise additional capital or exit the market as a result of our provisions, rather than c.100 as estimated in CP10/6. Thus, only a small proportion of the total population of GI intermediaries is likely to exit the market.[32] This, and relatively low barriers to entry in this market,[33] should ensure consumer choice in the GI intermediary market is not significantly reduced by our measures.

Regarding secured lenders, we understand that some specialist secured lenders (representing up to half of specialist secured lenders' market share) sold PPI exclusively through independent secured loan brokers. Since it is the loan brokers who are liable for redress payable on their sales, we do not expect our provisions to lead to significant prudential risk for these secured lenders. Since prudential risks appear low for a number of secured lenders, this limits the likely impact of exited lenders on the overall supply of credit, as these firms and others should be able to expand their lending to meet demand. Where secured loan brokers do fail through paying redress in accordance with our measures, we expect lenders who sold through them to be able to sell their products through other loan brokers relatively quickly (because of the limited impact of our measures on the overall number of GI intermediaries, and the low barriers to entry for this market). Given this, we do not expect our provisions to materially affect consumers' access to credit.

We also do not expect our measures to lead to niche markets or geographical areas being less well served than previously. The secured lenders for whom we do not expect significant prudential risk cover a range of customer segments, from prime to sub-prime, and provide their loans through a range of channels, including telephone and online distribution channels. There is similarly a range of providers offering standalone PPI cover. Lending and protection products will also continue to be available through high-street bank branches, telephone and online channels. There will also be opportunities for firms in other sectors (e.g. mortgage brokers and investment intermediaries) to diversify to broker loans or to sell more protection products. Given this, we do not expect market segments to have their access to credit or protection products significantly impaired as a result of our provisions.

Based on the above points, we do not believe that the prudential impacts of our provisions on secured lenders or on GI intermediaries (including secured loan brokers) undermine the proportionality of our provisions.

32 We estimate this to be around 5% of those firms who have sold PPI and whose primary FSA-regulated activity is general insurance mediation. It is possible that there may also be prudential risks for some firms who have sold PPI but for whom general insurance mediation is not their primary FSA-regulated activity (for example, for mortgage intermediaries who have also sold personal loans and PPI on these loans). However, we understand that the proportion of firms doing so, and the value of their PPI sales, is small, such that the impact of these firms on our overall estimate of prudential risk is unlikely to be material.

33 In spite of recent market conditions, with many firms leaving the market or changing their business model, the overall number of intermediaries has increased over the last 2-3 years, suggesting low barriers to entry.

49. In addition to our consideration of comments received on our prudential assessments, we have also updated this assessment to reflect updated data that we have received since publishing CP10/6. In particular, we note the following:

a) For GI intermediaries, we have refined our approach for this sector, incorporating firms' latest data returns and other additional information allowing us to identify more accurately which firms had sold PPI, and so may be liable for redress as a result of our measures. The total redress and administrative costs which we expect to fall on GI intermediaries has not changed substantially since CP10/6 (this has increased from c.£430m to c.£470m). However, based on the additional data discussed above, the prudential risk that this amount may pose to industry appears lower than we estimated in CP10/6; whereas we previously estimated that up to around 100 GI intermediaries may fail unless they receive additional capital, we now estimate that this number has reduced to c.35-40 intermediaries, reducing the costs passing to the FSCS from c.£10m to c.£5m. We noted in CP10/6 that if one or more networks of appointed representatives is unable to meet its capital requirements, this might increase the total costs passing to the FSCS by up to c.£30m. We see no reason to change this assumption, and therefore we estimate that c.£35m of total costs from GI intermediaries may pass through to the FSCS (and to its levy funding firms).

b) For secured lenders, taking into account our updated cost estimates for second-charge mortgage PPI, and the comments in paragraph 48 above regarding the structure of the secured lending sector, our estimate of the costs that may pass through to the FSCS from secured lenders has also decreased, from up to c.£120m (as estimated in CP10/6) to up to c.£80m.

c) These estimates of the costs passed through to the FSCS, and from there to levy firms, have been reached through a number of industry-level assumptions. There is an inherent uncertainty around a number of these estimates, including: firms' own historical sales practices and complaints experience; the timing of a firm's default, and what costs are borne by the firm before it is declared in default; the extent of any past sales review commenced by the firm before it is declared in default; and the amount of any recoveries made by the FSCS. These factors may lead the final costs borne by levy firms to vary from the estimates above.

50. We noted in CP10/6[34] that any costs passing through to the FSCS would fall initially within the 'General insurance – intermediation' subclass. Since the maximum costs which we thought may pass through the FSCS to levy firms fell within the annual cap for this subclass (£195m), and since any levies would fall most heavily on the larger firms within the subclass (including the major retail groups), we concluded that we did not expect the cost of the levy to firms to trigger any further prudential issues. Given that our estimate of the costs that may pass through to the FSCS has decreased since our estimate in CP10/6, we see no reason to alter this view. Also, to the extent that the impact of our provisions will be spread over a number of years, this also limits the risk of further prudential issues for levy funding firms. As such,

34 Annex 3, paragraph 56

we remain of the view that the potential prudential implications of our provisions do not undermine their proportionality.

Regulatory cost of our proposed monitoring approach

51. We set out in Chapter 4 details of our planned monitoring approach. This approach entails administrative costs for us and, consequently, costs for funding firms. Costs to firms were incorporated in the CBA to CP10/6.[35] Also, as we noted in CP10/6,[36] had we not proceeded with our current provisions, we would have taken alternative action to address the market failures identified, such as firm-specific supervisory work and potentially enforcement action where appropriate. We view our current provisions as the most effective and resource-efficient means of correcting the market failures identified. Consequently, we do not believe that our current approach should entail additional regulatory costs to us above those that would have been entailed if we had not proceeded with our provisions, and so we have not increased the cost estimates in our CBA to reflect regulatory costs.

35 See paragraph 21, Annex 2, CP10/6.
36 Annex 2, paragraph 6

Annex 2

Compatibility statement

1. In CP10/6[1] we set out our updated assessment of the compatibility of our proposals with our general duties under section 2 of the Financial Services and Markets Act 2000 (FSMA) and with our regulatory objectives set out in sections 3 to 6 of FSMA. This revised compatibility statement reflected comments received in responses to CP09/23.

2. Responses to CP10/6 included no new objections specifically related to the compatibility of our proposals in relation to our statutory objectives and the principles of good regulation. Some consultation responses reiterated, or elaborated on, the objections to our compatibility statement which industry previously raised in responses to CP09/23; we discuss details of these comments elsewhere in this Policy Statement, together with the changes that we have made based on our consideration of them. We have reviewed our compatibility statement in light of the consultation responses received, and also in light of the updated data discussed in our cost-benefit analysis (see Annex 1). We remain satisfied that the compatibility statement in CP10/6 adequately assesses the compatibility of our proposals with the statutory objectives and principles of good regulation discussed in the Consultation Paper.

3. We have also considered the compatibility of our proposals with our new statutory objective of financial stability, as introduced by Section 1 of the Financial Services Act 2010. Since this objective was not in force when we published CP10/6, we include in this Policy Statement our assessment of the compatibility of our provisions with this objective, as set out below.

Compatibility with the statutory objectives:

Financial stability

4. Our measures are not aimed specifically at this new objective and there are aspects of this objective which are not relevant. However we have considered the impact on it and compatibility of our proposals with it more broadly.

5. This objective requires us to contribute to the protection and enhancement of the stability of the UK financial system; in doing so, we are required to have regard to: the economic and fiscal consequences for the UK of instability of the UK financial

1 See Annex 4, CP10/6.

system, the effects of any FSA actions done for the purpose of this objective on UK economic growth, and the impact of events or circumstances originating from outside the UK.

6. We acknowledge that a limited number of distributors may require a cash injection in order to meet costs arising from wider redress exercises; in the event that such firms fail we have concluded that the Financial Services Compensation Scheme will be able to meet legitimate claims. Our prudential analysis also suggests that such firms as may become insolvent as a result of our proposals are not core to the stability of the UK financial system.

7. We are also of the opinion that by handling complaints about PPI mis-selling in line with our handbook text, firms can begin to rebuild the trust of their customers, which may enhance long-term future financial stability. Therefore, overall we are satisfied that our measures are consistent with this new objective.

List of non-confidential respondents to CP10/6

Adam Samuel

Association of Finance Brokers

Association of Mortgage Intermediaries

Citizens Advice Bureau

Exasoft plc

Financial Services Consumer Panel

Freedom Finance plc

Genworth Financial

Money Health Check

PPI Claimline Ltd

Rod Revell

Renaissance Easy Claim

Royal and Sun Alliance Insurance plc

Stephen Atkins

Which? provided a response to CP09/23, but was omitted from the list of non-confidential respondents in CP10/6.

Final Handbook text

DISPUTE RESOLUTION: COMPLAINTS (PAYMENT PROTECTION INSURANCE) INSTRUMENT 2010

Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 138 (General rule-making power);
(2) section 149 (Evidential provisions); and
(3) section 157(1) (Guidance).

B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force on 1 December 2010.

Amendments to the Handbook

D. The Dispute Resolution: Complaints sourcebook (DISP) is amended in accordance with the Annex to this instrument.

Citation

E. This instrument may be cited as the Dispute Resolution: Complaints (Payment Protection Insurance) Instrument 2010.

By order of the Board
22 July 2010

Annex

Amendments to the Dispute Resolution: Complaints sourcebook (DISP)

In this Annex, underlining indicates new text, unless otherwise stated.

Introduction

…

Appendix 3: FSA's rules and guidance on handling payment protection insurance complaints

This appendix sets out the approach which *firms* should use when handling *complaints* relating to the sale of *payment protection contracts*.

…

1.4 Complaints resolution rules

…

1.4.6 G *DISP* App 3 sets out the approach which *respondents* should use in assessing *complaints* relating to the sale of *payment protection contracts* and determining appropriate redress where a *complaint* is upheld.

Insert the following new Appendix after DISP Appendix 2 (which is currently deleted). The text is not underlined.

Appendix 3 Handling Payment Protection Insurance complaints

3.1 Introduction

3.1.1 G (1) This appendix sets out how a *firm* should handle *complaints* relating to the sale of a *payment protection contract* by the *firm* which express dissatisfaction about the sale, or matters related to the sale, including where there is a rejection of claims on the grounds of ineligibility or exclusion (but not matters unrelated to the sale, such as delays in claims handling).

(2) It relates to the sale of any *payment protection contract* whenever the sale took place and irrespective of whether it was on an advised or non-advised basis; conducted through any sales channel; in connection with any type of loan or credit product, or none; and for a regular premium or single premium payment. It applies whether the *policy* is currently in force, was cancelled during the *policy* term or ran its full term.

3.1.2 G The aspects of *complaint* handling dealt with in this appendix are how the *firm* should:

(1) assess a *complaint* in order to establish whether the *firm's* conduct of the sale failed to comply with the *rules*, or was otherwise in breach of the duty of care or any other requirement of the general law (taking into account relevant materials published by the *FSA*, other relevant regulators, the *Financial Ombudsman Service* and *former schemes*). In this appendix this is referred to as a "breach or failing" by the *firm*;

(2) determine the way the complainant would have acted if a breach or failing by the *firm* had not occurred; and

(3) determine appropriate redress (if any) to offer to a complainant.

3.1.3 G Where the *firm* determines that there was a breach or failing, the *firm s*hould consider whether the complainant would have bought the *payment protection contract* in the absence of that breach or failing. This appendix establishes presumptions for the *firm* to apply about how the complainant would have acted if there had instead been no breach or failing by the *firm*. The presumptions are:

(1) for some breaches or failings (see *DISP* App 3.6.2E), the *firm* should presume that the complainant would not have bought the *payment protection contract* he bought; and

(2) for certain of those breaches or failings (see *DISP* App 3.7.7E), where the complainant bought a single premium *payment protection contract*, the *firm* may presume that the complainant would have bought a regular premium *payment protection contract* instead of the *payment protection contract* he bought.

3.1.4 G There may also be instances where a *firm* concludes after investigation that, notwithstanding breaches or failings by the *firm*, the complainant would nevertheless still have proceeded to buy the *payment protection contract* he bought.

3.1.5 G In this appendix:

(1) "historic interest" means the interest the complainant paid to the *firm* because a single premium *payment protection contract* was added to a loan or credit product;

(2) "simple interest" means a non-compound rate of 8% per annum; and

(3) "claim" means a claim by a complainant seeking to rely upon the *policy* under the *payment protection contract* that is the subject of the *complaint*.

3.2 The assessment of a complaint

3.2.1 G The *firm* should consider, in the light of all the information provided by the complainant and otherwise already held by or available to the *firm*, whether there was a breach or failing by the *firm*.

3.2.2 G The *firm* should seek to establish the true substance of the *complaint*, rather than taking a narrow interpretation of the issues raised, and should not focus solely on the specific expression of the *complaint*. This is likely to require an approach to *complaint* handling that seeks to clarify the nature of the *complaint*.

3.2.3 G A *firm* may need to contact a complainant directly to understand fully the issues raised, even where the *firm r*eceived the *complaint* from a third party acting on the complainant's behalf. The *firm* should not use this contact to delay the assessment of the *complaint*.

3.2.4 G Where a *complaint* raises (expressly or otherwise) issues that may relate to the original sale or a subsequently rejected claim then, irrespective of the main focus of the *complaint*, the *firm* should pro-actively consider whether the issues relate to both the sale and the claim, and assess the *complaint* and determine redress accordingly.

3.2.5 G If, during the assessment of the *complaint*, the *firm* uncovers evidence of a breach or failing not raised in the *complaint*, the *firm* should consider those other aspects as if they were part of the *complaint*.

3.2.6 G The *firm* should take into account any information it already holds about the sale and consider other issues that may be relevant to the sale identified by the *firm* through other means, for example, the root cause analysis described in *DISP* App 3.4.

3.2.7 G The *firm* should consider all of its sales of *payment protection contracts* to the complainant in respect of re-financed loans that were rolled up into the loan covered by the *payment protection contract* that is the subject of the *complaint*. The *firm* should consider the cumulative financial impact on the complainant of any previous breaches or failings in those sales.

3.3 The approach to considering evidence

3.3.1 G Where a *complaint* is made, the *firm* should assess the *complaint* fairly, giving appropriate weight and balanced consideration to all available evidence, including what the complainant says and other information about the sale that the *firm* identifies. The *firm* is not expected automatically to assume that there has been a breach or failing.

3.3.2 G The *firm* should not rely solely on the detail within the wording of a *policy's* terms and conditions to reject what a complainant recalls was said during the sale.

3.3.3 G The *firm* should recognise that oral evidence may be sufficient evidence and not dismiss evidence from the complainant solely because it is not supported by documentary proof. The *firm* should take account of a complainant's limited ability fully to articulate his *complaint* or to explain his actions or decisions made at the time of the sale.

3.3.4 G Where the complainant's account of events conflicts with the *firm's* own records or leaves doubt, the *firm* should assess the reliability of the complainant's account fairly and in good faith. The *firm* should make all reasonable efforts (including by contact with the complainant where necessary) to clarify ambiguous issues or conflicts of evidence before making any finding against the complainant.

3.3.5 G The *firm* should not reject a complainant's account of events solely on the basis that the complainant signed documentation relevant to the purchase of the *policy*.

3.3.6 G The *firm* should not reject a *complaint* because the complainant failed to exercise the right to cancel the *policy*.

3.3.7 G The *firm* should not consider that a successful claim by the complainant is, in itself, sufficient evidence that the complainant had a need for the *policy* or had understood its terms or would have bought it regardless of any breach or failing by the *firm*.

3.3.8 G The *firm* should not draw a negative inference from a complainant not having kept documentation relating to the purchase of the *policy* for any particular period of time.

3.3.9 G In determining a particular *complaint*, the *firm* should (unless there are reasons not to because of the quality and plausibility of the respective evidence) give more weight to any specific evidence of what happened during the sale (including any relevant documentation and oral testimony) than to general evidence of selling practices at the time (such as training, instructions or sales scripts or relevant audit or compliance reports on those practices).

3.3.10 G The *firm* should not assume that because it was not authorised to give advice (or because it intended to sell without making a recommendation) it did not in fact give advice in a particular sale. The *firm* should consider the available evidence and assess whether or not it gave advice or made a recommendation (explicitly or implicitly) to the complainant.

3.3.11 G The *firm* should consider in all situations whether it communicated information to the complainant in a way that was fair, clear and not misleading and with due regard to the complainant's information needs.

3.3.12 G In considering the information communicated to the complainant and the complainant's information needs, the evidence to which a *firm* should have regard includes:

(1) the complainant's individual circumstances at the time of the sale (for example, the *firm* should take into account any evidence of limited financial capability or understanding on the part of the complainant);

(2) the complainant's objectives and intentions at the time of the sale;

(3) whether, from a reasonable *customer's* perspective, the documentation provided to the complainant was sufficiently clear, concise and presented

fairly (for example, was the documentation in plain and intelligible language?);

(4) in a sale that was primarily conducted orally, whether sufficient information was communicated during the sale discussion for the *customer* to make an informed decision (for example, did the *firm* give an oral explanation of the main characteristics of the *policy* or specifically draw the complainant's attention to that information on a computer screen or in a document and give the complainant time to read and consider it?);

(5) any evidence about the tone and pace of oral communication (for example, was documentation read out too quickly for the complainant to have understood it?); and

(6) any extra explanation or information given by the *firm* in response to questions raised (or information disclosed) by the complainant.

3.3.13 G The *firm* should not reject a *complaint* solely because the complainant had held a *payment protection contract* previously.

3.4 Root cause analysis

3.4.1 G *DISP* 1.3.3R requires the *firm* to put in place appropriate management controls and take reasonable steps to ensure that in handling *complaints* it identifies and remedies any recurring or systemic problems. If a *firm* receives *complaints* about its sales of *payment protection contracts* it should analyse the root causes of those *complaints* including, but not limited to, the consideration of:

(1) the concerns raised by complainants (both at the time of the sale and subsequently);

(2) the reasons for both rejected claims and *complaints*;

(3) the *firm's* stated sales practice(s) at the relevant time(s);

(4) evidence available to the *firm* about the actual sales practice(s) at the relevant time(s) (this might include recollections of staff and complainants, compliance records, and other material produced at the time about specific transactions, for example call recordings and incentives given to *advisers*);

(5) relevant regulatory findings; and

(6) relevant decisions by the *Financial Ombudsman Service*.

3.4.2 G Where consideration of the root causes of *complaints* suggests recurring or systemic problems in the *firm's* sales practices for *payment protection contracts*, the *firm* should, in assessing an individual *complaint*, consider whether the problems were likely to have contributed to a breach or failing in the individual case, even if those problems were not referred to specifically by the complainant.

3.4.3 G Where a *firm* identifies (from its *complaints* or otherwise) recurring or systemic problems in its sales practices for a particular type of *payment protection contract*, either for its sales in general or for those from a particular location or sales channel, it should (in accordance with *Principle* 6 (Customers' interests) and to the extent that it applies), consider whether it ought to act with regard to the position of *customers* who may have suffered detriment from, or been potentially disadvantaged by such problems but who have not complained and, if so, take appropriate and proportionate measures to ensure that those *customers* are given appropriate redress or a proper opportunity to obtain it. In particular, the *firm* should:

(1) ascertain the scope and severity of the consumer detriment that might have arisen; and

(2) consider whether it is fair and reasonable for the *firm* to undertake proactively a redress or remediation exercise, which may include contacting *customers* who have not complained.

3.5 Re-assessing rejected claims

3.5.1 E Where a *complaint* is about the sale of a *policy*, the *firm* should, as part of its investigation of the *complaint*, determine whether any claim on that *policy* was rejected, and if so, whether the complainant may have reasonably expected that the claim would have been paid.

3.5.2 G For example, the complainant may have reasonably expected that the claim would have been paid where the *firm* failed to disclose appropriately an exclusion or limitation later relied on by the *insurer* to reject the claim and it should have been clear to the *firm* that that exclusion or limitation was relevant to the complainant.

3.6 Determining the effect of a breach or failing

3.6.1 E Where the *firm* determines that there was a breach or failing, the *firm* should consider whether the complainant would have bought the *payment protection contract* in the absence of that breach or failing.

3.6.2 E In the absence of evidence to the contrary, the *firm* should presume that the complainant would not have bought the *payment protection contract* he bought if the sale was substantially flawed, for example where the *firm*:

(1) pressured the complainant into purchasing the *payment protection contract*; or

(2) did not disclose to the complainant, in good time before the sale was concluded, and in a way that was fair, clear and not misleading, that the *policy* was optional; or

(3) made the sale without the complainant's explicit agreement to purchase the *policy*; or

(4) did not disclose to the complainant, in good time before the sale was concluded, and in a way that was fair, clear and not misleading, the significant exclusions and limitations, i.e. those that would tend to affect the decisions of *customers* generally to buy the *policy*; or

(5) did not, for an advised sale (including where the *firm* gave advice in a non-advised sales process) take reasonable care to ensure that the *policy* was suitable for the complainant's demands and needs taking into account all relevant factors, including level of cover, cost, and relevant exclusions, excesses, limitations and conditions; or

(6) did not take reasonable steps to ensure the complainant only bought a *policy* for which he was eligible to claim benefits; or

(7) found, while arranging the *policy*, that parts of the cover did not apply but did not disclose this to the *customer*, in good time before the sale was concluded, and in a way that was fair, clear and not misleading; or

(8) did not disclose to the complainant, in good time before the sale was concluded, and in a way that was fair, clear and not misleading, the total (not just monthly) cost of the *policy* separately from any other prices (or the basis for calculating it so that the complainant could verify it); or

(9) recommended a single premium *payment protection contract* without taking reasonable steps, where the *policy* did not have a pro-rata refund, to establish whether there was a prospect that the complainant would repay or refinance the loan before the end of the term; or

(10) provided misleading or inaccurate information about the *policy* to the complainant; or

(11) sold the complainant a *policy* where the total cost of the *policy* (including any interest paid on the premium) would exceed the benefits payable under the *policy* (other than benefits payable under life cover); or

(12) in a sale of a single premium *payment protection contract*, failed to disclose to the complainant, in good time before the sale was concluded, and in a way that was fair, clear and not misleading:

(a) that the premium would be added to the amount provided under the credit agreement, that interest would be payable on the premium and the amount of that interest; or

(b) (if applicable) that the term of the cover was shorter than the term of the credit agreement and the consequences of that mismatch; or

(c) (if applicable) that the complainant would not receive a pro-rata refund if the complainant were to repay or refinance the loan or otherwise cancel the single premium *policy* after the cooling-off period.

3.6.3 E Relevant evidence might include the complainant's demands, needs and intentions at the time of the sale and any other relevant evidence, including any testimony by the complainant about his reasons at the time of the sale for purchasing the *payment protection contract.*

3.7 Approach to redress

General approach to redress: all contract types

3.7.1 E Where the *firm* concludes in accordance with *DISP* App 3.6 that the complainant would still have bought the *payment protection contract* he bought, no redress will be due to the complainant in respect of the identified breach or failing, subject to *DISP* App 3.7.6E.

3.7.2 E Where the *firm* concludes that the complainant would not have bought the *payment protection contract* he bought*,* and the *firm* is not using the alternative approach to redress (set out in *DISP* App 3.7.7E to 3.7.15E) or other appropriate redress (see *DISP* App 3.8), the *firm* should, as far as practicable, put the complainant in the position he would have been if he had not bought any *payment protection contract*.

3.7.3 E In such cases the *firm* should pay to the complainant a sum equal to the total amount paid by the complainant in respect of the *payment protection contract* including historic interest where relevant (plus simple interest on that amount). If the complainant has received any rebate, for example if the *customer* cancelled a single premium *payment protection contract* before it ran full term and received a refund, the *firm* may deduct the value of this rebate from the amount otherwise payable to the complainant.

3.7.4 E Additionally, where a single premium was added to a loan:

(1) for live *policies*:

(a) subject to *DISP* App 3.7.5E, where there remains an outstanding loan balance, the *firm s*hould, where possible, arrange for the loan to be restructured (without charge to the complainant but using any applicable cancellation value) with the effect of:

(i) removing amounts relating to the *payment protection contract* (including any interest and charges); and

(ii) ensuring the number and amounts of any future repayments (including any interest and charges) are the same as would have applied if the complainant had taken the loan without the *payment protection contract*; or

(b) where the *firm* is not able to arrange for the loan to be restructured (e.g. because the loan is provided by a separate *firm*), it should pay the complainant an amount equal to the difference between the actual loan balance and what the loan balance would have been if the *payment protection contract* (including any interest and charges) had not been added, deducting the current cancellation value. The *firm* should offer to pay any charges incurred if the complainant uses this amount to reduce his loan balance; and

(2) for cancelled *policies*, the *firm should* pay the complainant the difference between the actual loan balance at the point of cancellation and what the loan balance would have been if no premium had been added (plus simple interest) minus any applicable cancellation value.

3.7.5 E Where a claim was previously paid on the *policy*, the *firm* may deduct this from redress paid in accordance with *DISP* App 3.7.3E. If the claim is higher than the amount to be paid under *DISP* App 3.7.3E then the *firm* may also deduct the excess from the amount to be paid under *DISP* App 3.7.4E.

3.7.6 E Where the *firm* concludes that the complainant may have reasonably expected that a rejected claim would have been paid (see *DISP* App 3.5) then:

(1) if the value of the claim exceeds the amount of the redress otherwise payable to the complainant for a breach or failing identified in accordance with this appendix, the *firm* should pay to the complainant only the value of the claim (and simple interest on it as appropriate); and

(2) if the value of the claim is less than the amount of the redress otherwise payable to the complainant for a breach or failing identified in accordance with this appendix, the *firm* should pay to the complainant the value of that redress.

Alternative approach to redress: single premium policies

3.7.7 E Where the only breach or failing was within *DISP* App 3.6.2E(9) and/or *DISP* App 3.6.2E(12), and in the absence of evidence to the contrary, the *firm* may presume that instead of buying the single premium *payment protection contract* he bought, the complainant would have bought a regular premium *payment protection contract*.

3.7.8 E If a *firm* chooses to make this presumption, then it should do so fairly and for all relevant complainants in a relevant category of sale. It should not, for example, only use the approach for those complainants it views as being a lower underwriting risk or those complainants who have cancelled their *policies*.

3.7.9 E Where the *firm* presumes that the complainant would have purchased a regular premium *payment protection contract*, the *firm* should offer redress that puts the complainant in the position he would have been if he had bought an alternative regular premium *payment protection contract*.

3.7.10 E The *firm should* pay to the complainant a sum equal to the amount in *DISP* App 3.7.3E less the amount the complainant would have paid for the alternative regular premium *payment protection contract*.

3.7.11 E The *firm* should consider whether it is appropriate to deduct the value of any paid claims from the redress.

3.7.12 E Additionally, where a single premium was added to a loan, *DISP* App 3.7.4E applies except that in respect of *DISP* 3.7.4E(1)(a) the cancellation value should only be used if the complainant expressly wishes to cancel the *policy*.

3.7.13 E The *firm* should, for the purposes of redressing the *complaint*, use the value of £9 per £100 of benefits payable as the monthly price of the alternative regular premium *payment protection contract*. For example, if the monthly repayment amount in relation to the loan only is to be £200, the price of the alternative regular premium *payment protection contract* will be £18.

3.7.14 E Where the *firm* presumes that the complainant would have purchased a regular premium *payment protection contract* and if the complainant expressly wishes it, the existing cover should continue until the end of the existing *policy* term. The complainant should pay the price of the alternative regular premium *payment protection contract* (at *DISP* App 3.7.13E) and should be able to cancel at any time. This pricing does not apply where *DISP* App 3.7.4E(1)(b) applies.

3.7.15 E So that the complainant can make the decision on the continuation of cover from an informed position, the *firm* should:

(1) offer to provide details of the existing *payment protection contract*;

(2) inform the complainant that he may be able to find similar cover more cheaply from another provider in the event that he chooses to cancel the *policy* and take an alternative but remind the complainant that if his circumstances (for example, his health or employment prospects) have changed since the original sale, he may not be eligible for cover under any new *policy* he buys;

(3) make the complainant aware of the changes to the cancellation arrangements if cover continues;

(4) explain how the future premium will be collected and the cost of the future cover; and

(5) refer the complainant to www.moneymadeclear.org.uk as a source of information about a range of alternative *payment protection contracts*.

3.8 Other appropriate redress

3.8.1 E The remedies in *DISP* App 3.7 are not exhaustive.

3.8.2 E When applying a remedy other than those set out in *DISP* App 3.7, the *firm* should satisfy itself that the remedy is appropriate to the matter complained of and is appropriate and fair in the individual circumstances.

3.9 Other matters concerning redress

3.9.1 G Where the complainant's loan or credit card is in arrears the *firm* may, if it has the contractual right to do so, make a payment to reduce the associated loan or credit card balance, if the complainant accepts the *firm*'s offer of redress. The *firm* should act fairly and reasonably in deciding whether to make such a payment.

3.9.2	G	In assessing redress, the *firm* should consider whether there are any other further losses that flow from its breach or failing that were reasonably foreseeable as a consequence of the *firm's* breach or failing, for example, where the *payment protection contract's* cost or rejected claims contributed to affordability issues for the associated loan or credit which led to arrears charges, default interest, penal interest rates or other penalties levied by the lender.
3.9.3	G	Where, for single premium *policies*, there were previous breaches or failings (see *DISP* App 3.2.7G) the redress to the complainant should address the cumulative financial impact.
3.9.4	G	The *firm* should make any offer of redress to the complainant in a fair and balanced way. In particular, the *firm* should explain clearly to the complainant the basis for the redress offered including how any compensation is calculated and, where relevant, the rescheduling of the loan, and the consequences of accepting the offer of redress.

3.10 Application: evidential provisions

3.10.1	E	The *evidential provisions* in this appendix apply in relation to *complaints* about sales that took place on or after 14 January 2005.
3.10.2	G	For *complaints* about sales that took place prior to 14 January 2005, a *firm* should take account of the *evidential provisions* in this appendix as if they were *guidance*.
3.10.3	E	Contravention of an *evidential provision* in this appendix may be relied upon as tending to establish contravention of *DISP* 1.4.1R.

Amend the following as shown.

Schedule 4 Powers Exercised

…

Sch 4.1G

The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the *rules* in *DISP*:	
	…
	Section 139(4) (Miscellaneous ancillary matters)
	<u>Section 149 (Evidential provisions)</u>

	…

Material (including examples) supporting the Handbook text

Introduction
The guidance in this Appendix is provided to supplement the text in Chapter 3 of the Policy Statement. It should also be considered alongside DISP App 3.7 and DISP App 3.9 in the Handbook text.

Examples of calculating PPI redress[1]

Examples	
Table of examples of typical redress calculations	
Example 1	The complainant would not have purchased any PPI policy. The loan and the PPI policy are live.
Example 2	The complainant would not have purchased any PPI policy. The loan and the PPI policy ran the full term.
Example 3	The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan and PPI policy are live, and the complainant has not previously claimed.
Example 4	A claim was rejected, where the complainant may have reasonably expected that the claim would have been paid. The loan and the PPI policy ran the full term.
Example 5	The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan and the PPI policy are live, and the complainant has previously successfully claimed on the single premium PPI policy.
Example 6	The complainant would not have purchased a PPI policy at the outset. The credit card and the PPI policy are live.
Example 7	The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan was redeemed and the PPI policy was cancelled 12 months ago, having run for three years at the point of cancellation.
Example 8	The complainant would have purchased an alternative regular premium PPI policy at the outset. The firm finds it mis-sold a previous single premium PPI policy to the complainant that was subsequently cancelled to consolidate or refinance the connected loan.

[1] The examples do not cover any potential tax liabilities arising from payment of PPI redress. Further general guidance on this point can be found at the Financial Ombudsman Service http://www.financial-ombudsman.org.uk/publications/guidance/comp_tax.htm or at Revenue and Customs http://www.hmrc.gov.uk/bulletins/tb72.htm#1

Example 1 The complainant would not have purchased any PPI policy. The loan and the PPI policy are live.

As described in DISP App 3.7.3E, the firm should pay the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on that amount).

In this example, this is the sum of the complainant's previous PPI policy payments made via the loan repayments. The simple interest is calculated on each monthly PPI policy payment, from the time each payment was made to the time the compensation is paid.

Loan and policy details:	
Monthly loan payment	£200
Monthly amount of PPI policy payments (including interest)	£50
Term of policy (in months)	60
Number of monthly PPI policy payments to date	20

Compensation calculation:

Compensation for total PPI policy payments (£50 x 20 months) £1,000

8% p.a. simple interest on each PPI policy payment since the month it was made, calculated as follows:

- Interest on first payment made = £50 x 8% x 20/12
  (8% p.a. simple interest on £50 payment over 20 months) plus
- Interest on second payment made = £50 x 8% x 19/12 (etc)
- Total interest = £50 x 8% x (20 + 19 + … + 2 + 1)/12

Total interest £70

Total compensation **£1,070**

As described in DISP App 3.7.4E(1)(a) the firm should, where possible, arrange for the loan to be restructured. For this example, in addition to the above compensation to be paid to the complainant, the loan balance must be adjusted as if the PPI policy never existed and the future loan repayments would be £200 for the remainder of the term of the loan.

Example 2 The complainant would not have purchased any PPI policy. The loan and the PPI policy ran the full term.

As described in DISP App 3.7.3E, the firm should pay the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on this amount).

In this example, this is the sum of the complainant's previous PPI policy payments made via the loan repayments. The simple interest is calculated on each monthly PPI policy payment, from the time each payment was made to the time the compensation is paid.

Loan and policy details:	
Monthly amount of PPI policy payments (including interest)	£50
Term of policy (in months)	60
Period to date (in months)	72

Compensation calculation:

Compensation for total PPI policy payments (£50 x 60 months) £3,000

8% p.a. simple interest on each payment, calculated as:

- Interest on first payment made = £50 x 8% x 72/12
  (8% p.a. simple interest on £50 payment over 72 months (time since payment was made)) plus
- Interest on second payment made = £50 x 8% x 71/12 (etc)
- Total interest = £50 x 8% x (72 + 71 + … + 14 + 13)/12
  (Final payment on the loan was made 13 months ago)

Total interest £850

Total compensation **£3,850**

It is not necessary for the firm to arrange for the loan to be restructured in this example, as the loan ran for the full term.

Example 3 The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan and the PPI policy are live, and the complainant has not previously claimed.

As described in DISP App 3.7.3E, and DISP App 3.7.10E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on that amount), less the amount the complainant would have paid for the alternative regular premium PPI policy.

In this example, this is the sum of the complainant's PPI policy payments made via the loan repayments less the price of the alternative regular premium PPI policy. The simple interest is calculated on the difference between actual PPI policy price and the alternative policy price for each payment, from the time each actual PPI payment was made to the time the compensation is paid.

Loan and policy details:	
Monthly loan payment	£200
Price of monthly PPI policy payments (including interest)	£50
Term of policy (in months)	60
Monthly PPI policy payments to date	20

Difference between the price of the actual PPI policy purchased and the price of the alternative policy:	
Price per £100 of alternative regular premium PPI policy	£9
Resulting monthly alternative regular premium PPI policy price for current loan (based on £200 monthly loan repayments)	£18
Monthly difference between actual (£50) and alternative (£18) monthly payments	£32

Compensation calculation:	
Compensation for the total difference in PPI policy payments (£32 difference x 20 months)	£640

8% p.a. simple interest on difference between actual and alternative price for each payment, calculated as: • Interest on first month's payment = £32 x 8% x 20/12 (8% p.a. simple interest on £32 payment over 20 months) plus • Interest on second month's payment = £32 x 8% x 19/12 (etc) • Total interest = £32 x 8% x (20 + 19 + … + 2 + 1)/12	
Total interest	£45
Total compensation	**£685**

As described in DISP App 3.7.4E,(1)(a) the firm should, where possible, arrange for the loan to be restructured. For this example, in addition to the above compensation to be paid to the complainant, the loan balance must be adjusted as if the PPI policy never existed and the future loan repayments would be £200 for the remainder of the term of the loan.

The customer should be given the option of maintaining regular premium PPI cover for the remaining term of the loan at the alternative cost of £18 (based on the reference price of £9 per £100 of cover, applied to the monthly loan repayments of £200).

Example 4 A claim was rejected, where the complainant may have reasonably expected that the claim would have been paid. The loan and the PPI policy ran the full term

As described in DISP App 3.7.6E, redress to the complainant should be the greater of:

(1) A sum equal to the amount payable to the complainant in accordance with DISP App 3.7.3E, i.e. the total amount paid by the complainant for the PPI policy including historic interest where relevant (plus simple interest on that amount); or

(2) The value of the claim, plus simple interest from the date each payment on the claim would have been made to the date the compensation is paid.

Loan and policy details:	
Monthly loan payment	£200
Price of monthly PPI policy payments (including interest)	£50
Term of policy (in months)	60
Period to date (in months)	72

<u>1. Calculation of the compensation otherwise payable in accordance with DISP App 3.7.3G (all payments made with 8% p.a. simple interest):</u>	
Total PPI policy payments (£50 x 60 months)	£3,000
8% p.a. simple interest on each payment since the month it was made (calculation as per Example 2)	£850
Total compensation representing PPI policy payments with interest	**£3,850**

Claim details:	
Time since the first payment that would have been covered by the claim (in months)	30
Monthly amount of claim	£250

2. <u>Calculation of the value of the claim (plus 8% p.a. simple interest):</u>	
Scenario 1: Duration of the claim is 6 months	
Unemployment/Accident/Sickness period (in months)	6

Total value of the claim (£250 x 6 months)	£1,500
8% p.a. simple interest on each payment, calculated as: • Interest on first month's claim = £250 x 8% x 30/12 (8% p.a. simple interest on £250 claim over 30 months (time elapsed since the first payment that would have been covered by the claim) plus • Interest on second payment made = £250 x 8% x 29/12 (etc) • Total interest = £250 x 8% x (30 + 29 + … + 26 + 25)/12 (Last claim on the policy would have been made 25 months ago)	
Total interest	£275
Total compensation representing the value of the claim	**£1,775**
Compensation representing the value of the claim is less than the compensation otherwise payable in accordance with DISP App 3.7.3E, i.e. the total paid by the complainant for PPI policy payments with interest.	
As described in DISP App 3.7.6E, the redress should be the greater of the above two types of compensation. In this scenario, the redress is the total paid by the complainant for PPI policy payments with interest.	
Total redress should be	**£3,850**

Scenario 2: Duration of the claim is 18 months	
Unemployment/Accident/Sickness period (in months)	18
Total claims on the policy (£250 x 18 months)	£4,500
8% p.a. simple interest on each payment, calculated as: • Interest on first month's claim = £250 x 8% x 30/12 (8% p.a. simple interest on £250 claim over 30 months (time elapsed since date of claim) • Interest on second payment made = £250 x 8% x 29/12 • Total interest = £250 x 8% x (30 + 29 + … + 14 + 13)/12 (Last claim on the policy would have been made 13 months ago)	
Total interest	£645
Total compensation representing the value of the claim	**£5,145**

Compensation representing the value of the claim is greater than the compensation otherwise payable in accordance with DISP App 3.7.3E, i.e. the total paid by the complainant for PPI policy payments with interest.

As described in DISP App 3.7.6E, the redress should be the greater of the above two types of compensation. In this scenario, the redress is the amount equivalent to that which would have been payable by the insurer had the claim been accepted plus interest at 8% p.a.

Total redress should be	**£5,145**

Example 5 The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan and the PPI policy are live, and the complainant has previously successfully claimed on the single premium PPI policy.

As described in DISP App 3.7.3E and DISP App 3.7.10E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on that amount) less the amount the complainant would have paid for the alternative regular premium PPI policy.

In this example, this is the sum of the complainant's PPI policy payments made via the loan repayments less the price of the alternative regular premium PPI policy. The simple interest is calculated on the difference between the actual PPI policy price and the alternative policy price for each payment made by the complainant outside the claim period, from the time each actual PPI payment was made to the time the compensation is paid.

The firm may deduct from the compensation an amount equivalent to those regular premiums paid during the claim period. This is because under the terms of an alternative regular premium product, the premiums would still have been payable by the complainant during the claim period.

Loan and policy details:	
Monthly loan payment	£200
Price of monthly PPI policy payments (including interest)	£50
Term of policy (in months)	60
Time since first payment (in months)	20

Alternative policy details:	
Price per £100 of alternative regular premium PPI policy	£9
Resulting monthly alternative regular premium PPI policy price for current loan (based on £200 monthly loan repayments)	£18
Monthly difference between actual (£50) and alternative (£18) monthly payments	£32

Claim details:	
Unemployment/Accident/Sickness period (in months)	6
Time since first payment covered by the claim (in months)	10

Compensation calculation:	
Difference between actual and alternative PPI payments (where the complainant made the premium payments and no claim was being paid), i.e. from T-20 months to T-11 months and from T-4 months to present, T being the calculation date)	£448
8% p.a. simple interest on the difference between actual PPI policy price and the alternative policy price for each payment made by the complainant outside the claim period	£35
Less the sum of:	
Regular premiums which would have been paid during the claim period under the alternative regular premium PPI policy contract (£18 x 6 months) and	£108
8% p.a. simple interest on the regular premium payments which would have been made by the complainant during the claim period under the alternative regular premium PPI policy contract	£5

Total compensation **£370**

As per DISP App 3.7.4E(1)(a), the firm should, where possible, arrange for the loan to be restructured. For this example, in addition to the above compensation to be paid to the complainant, the loan balance must be adjusted as if the PPI policy never existed and the future loan repayments would be £200 for the remainder of the term of the loan.

The customer should be given the option of maintaining the existing cover at the price of the alternative regular premium PPI cover for the remaining term of the loan at the alternative cost of £18 (based on the reference price of £9 per £100 of cover, applied to the monthly loan repayments of £200).

Example 6 The complainant would not have purchased a PPI policy at the outset. The credit card and the protection contract are live.

As described in DISP App 3.7.3E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on amounts where the credit account, but for the sale, would have been in credit).

In this example, this is the sum of the complainant's previous PPI policy payments (with interest) added to the credit account. The simple interest is applied for each month that the notional credit card balance would have been positive. The notional credit card balance for each month is calculated by adding the running PPI cost balance to the actual credit card balance for that month.

A detailed month-by-month example of how the compensation is calculated is shown on the following page.

Credit card and policy details:	
Calculation date	Month 20
Credit card APR	20%
PPI cost (per £100 of credit card balance)	£0.69
Interest is calculated monthly (not daily)	

Compensation calculation (see details on following page):	
Total PPI premiums for 20 months plus	£73.49
Historic interest paid on all these premiums (at 20% APR) plus	£9.97
8% p.a. simple interest on those PPI premiums paid that, if they had not been paid, would have made the customer's credit card balance, for those months, positive.	£2.62
Total compensation	**£86.08**

Month	Monthly Transactions A	Monthly payment B	Running actual credit card balance C (A+B)	Monthly cost of PPI D (based on C and price)	Running PPI balance on credit card at month start E (Cumulative D + cumulative F to previous month)	Compound interest on PPI accrued in month F (based on E and interest rate)	PPI balance carried over G (E+F)	Running PPI redress balance H (Cumulative total of D and F)	Notional credit card balance (if PPI had not been taken out) I (C+H)	8% simple interest (based on I where in credit)
1	-£500	£200	-£300	-£2.07	-£2.07	-£0.03	-£2.10	£2.10	-£297.90	n/a
2	-£900	£500	-£700	-£4.83	-£6.93	-£0.12	-£7.05	£7.05	-£692.95	n/a
3	-£400	£200	-£900	-£6.21	-£13.26	-£0.22	-£13.48	£13.48	-£886.52	n/a
4	-£500	£200	-£1,200	-£8.28	-£21.76	-£0.36	-£22.12	£22.12	-£1,177.88	n/a
5	-£300	£500	-£1,000	-£6.90	-£29.02	-£0.48	-£29.51	£29.51	-£970.49	n/a
6	-£400	£100	-£1,300	-£8.97	-£38.48	-£0.64	-£39.12	£39.12	-£1,260.88	n/a
7	-£800	£400	-£1,700	-£11.73	-£50.85	-£0.85	-£51.70	£51.70	-£1,648.30	n/a
8	-£200	£400	-£1,500	-£10.35	-£62.05	-£1.03	-£63.08	£63.08	-£1,436.92	n/a
9	-£100	£1,600	£0	£0.00	£0.00	£0.00	£0.00	£63.08	+£63.08	£0.42
10	-£300	£300	£0	£0.00	£0.00	£0.00	£0.00	£63.08	+£63.08	£0.42
11	-£500	£500	£0	£0.00	£0.00	£0.00	£0.00	£63.08	+£63.08	£0.42
12	-£250	£250	£0	£0.00	£0.00	£0.00	£0.00	£63.08	+£63.08	£0.42
13	-£300	£300	£0	£0.00	£0.00	£0.00	£0.00	£63.08	+£63.08	£0.42
14	-£400	£100	-£300	-£2.07	-£65.15	-£1.09	-£66.24	£66.24	-£233.76	n/a
15	-£400	£100	-£600	-£4.14	-£70.38	-£1.17	-£71.55	£71.55	-£528.45	n/a
16	-£550	£400	-£750	-£5.18	-£76.72	-£1.28	-£78.00	£78.00	-£672.00	n/a
17	-£250	£1,000	£0	£0.00	£0.00	£0.00	£0.00	£78.00	+£78.00	£0.52
18	-£400	£200	-£200	-£1.38	-£79.38	-£1.32	-£80.71	£80.71	-£119.29	n/a
19	-£300	£300	-£200	-£1.38	-£82.09	-£1.37	-£83.45	£83.45	-£116.55	n/a
				∑ -£73.49		**∑-£4.14**				**∑£2.62**

Example 7 **The complainant would have purchased an alternative regular premium PPI policy at the outset. The loan was redeemed and the PPI policy was cancelled 12 months ago, having run for three years at the point of cancellation.**

As described in DISP App 3.7.3E, DISP App 3.7.10E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI including historic interest where relevant (plus simple interest on that amount) less the amount the complainant would have paid for the alternative regular premium PPI policy.

In this example, this is the sum of the complainant's PPI policy payments made via the loan repayments less the price of the alternative regular premium PPI policy. The simple interest is calculated on the difference between the actual PPI policy payment and the alternative policy price for each payment, from the time each actual PPI payment was made to the time the compensation is paid.

As described in DISP App 3.7.4(2)E, the firm should also pay to the complainant the difference between the actual loan balance at the point of cancellation and what the loan balance would have been if no premium had been added (plus simple interest) minus any applicable cancellation value.

<u>Loan and policy details:</u>	
Loan amount	£4,700
PPI premium	£850
Total loan	£5,550
APR	10%
Monthly loan payment (without PPI)	£100
Monthly PPI payments	£18
Total monthly payment	£118
Term of PPI policy (in months)	60
Duration of payments before the loan was redeemed: (in months)	36
Duration since loan redemption and PPI policy cancellation: (in months)	12
Actual cost of redeeming the loan at 36 months (gross of any PPI rebate):	£2,555
Notional cost of redeeming the loan at 36 months (if PPI had not been added to loan):	£2,164
Difference between actual and notional loan balance at point of redemption:	£391

PPI rebate paid to loan at redemption (assuming that at 36 months the rebate is 14% of the original premium i.e. 14% of £850 in this example):	£119

Redress is calculated in two parts: the monthly overpayments and the overpayment on redemption of the loan.

Monthly overpayments calculation:	
Cost per £100 of alternative regular premium PPI	£9
Therefore, monthly cost for current loan	£9
Monthly overpayment (difference between actual PPI payments and alternative payments)	£9
Compensation for the total difference in PPI payments (monthly overpayment of £9 x duration of payments which is 36 months)	£324
8% p.a. simple interest on the overpayments (from the date of each actual PPI payment until the date of calculation):	£71
Total compensation for overpayments to the point of calculation:	**£395**

Overpayment on loan redemption calculation:	
Compensation for overpayment on loan redemption (differences in balances of £391 less PPI rebate of £119):	£272
Plus 8% p.a. simple interest over period since loan was redeemed which is 12 months:	£22
Total compensation for overpayment on loan redemption:	**£294**

Total compensation (£395 + £294):	**£689**

The firm need not provide future cover as the customer cancelled the PPI.

Example 8 The complainant would have purchased an alternative regular premium PPI policy at the outset. The firm finds it mis-sold a previous single premium PPI policy to the complainant which was subsequently cancelled to consolidate or refinance the connected loan.

As described in DISP App 3.2.7G and DISP App 3.9.3G, the firm should consider the sales of previous single premium PPI policies to the complainant in respect of re-financed loans that were rolled up into the loan covered by the PPI policy that is the subject of complaint. Where there were previous breaches or failings the redress to the complainant should address the cumulative financial impact on the complainant.

First loan and policy details:	
Loan amount	£9,400
PPI premium	£1,700
Total loan	£11,100
APR	10%
Monthly loan payment (without PPI)	£199.72
Monthly PPI payments	£36.12
Total monthly payment	£235.84
Term of loan and PPI policy (in months)	60
Duration of payments (in months)	12
Time since loan refinanced (in months)	36

Loan 1 – Redress is calculated in two parts for loan 1:

1. As described in DISP App 3.7.3E and DISP App 3.7.10E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI the PPI including historic interest where relevant (plus simple interest on that amount) less the amount the complainant would have paid for the alternative regular premium PPI policy.

   In this example, this is the sum of the complainant's PPI policy payments made via the loan repayments less the price of the alternative regular premium PPI policy. The simple interest is calculated on the difference between the actual PPI policy payment and the alternative policy price for each payment, from the time each actual PPI payment was made to the time the compensation is paid.

2. As described in DISP 3.7.4(2)E, the firm should also pay the difference between the actual loan balance at the point of cancellation and what the loan balance would have been if no premium had been added minus any applicable cancellation value. Note that it is not appropriate to add simple interest to this amount as it forms part of loan 2.

The above two parts are calculated as follows:

Historic monthly overpayments calculation for loan 1	
Cost per £100 of alternative regular premium PPI	£9
Therefore, monthly cost of alternative regular premium PPI for loan 1 (based on monthly loan repayment without PPI of £199.72)	£17.97
Monthly difference (actual PPI payment of £36.12 – alternative regular premium price of £17.97)	£18.15
Compensation for the total difference in PPI payments (monthly difference of £18.15 x duration of payments of 12 months)	£218
8% p.a. simple interest (on historic monthly payments for 12 months and the 36 months since loan 1 was refinanced)	£62
Total monthly overpayment compensation payable for loan 1	**£280**

Overpayment on loan redemption calculation for loan 1	
Actual redemption value of the loan after 12 months (without any PPI rebate)	£9,298.86
Notional redemption value of the loan after 12 months (if PPI had not been added to loan):	£7,874.70
PPI rebate paid to loan at redemption (assuming that at 12 months the rebate is 65% of the original premium i.e. 65% of £1,700):	£1,105
The overpayment value (actual redemption value - notional redemption value - PPI rebate):	**£319.16**
This figure is refinanced into loan 2 so any further loss is calculated with reference to loan 2's duration and APR. 8% p.a. simple interest is not added. The amount is carried over into the loan 2 calculation.	

<u>Second loan and policy details:</u>	
Loan amount	£14,200
PPI premium	£2,800
Total loan	£17,000
APR	10%
Total monthly repayment (based on £17,000) including the following monthly PPI payments:	£361.20
- monthly PPI payments for loan 2	£59.49
- residual monthly PPI payments for loan 1 (see below for calculation)	£6.78
Monthly loan payment without PPI from loan 2	£301.71
Monthly loan payment without PPI from loan 1 or 2	£294.93
Term of loan and PPI policy (in months)	60
Duration of payments (in months)	36

Loan 2 – Redress is calculated in two parts for loan 2:

As described in DISP App 3.7.3E, the firm should pay to the complainant a sum equal to the total amount the complainant paid for the PPI the PPI.

In this example, this is the sum of:

1. The monthly payments on the residual cost of PPI carried forward from loan 1 calculation (plus simple interest).

2. The total amount paid to the loan account in respect of the PPI policy for loan 2 including historic interest, less the amount the complainant would have paid for the alternative regular premium PPI policy (plus simple interest). The simple interest is calculated on the difference between the actual PPI policy payments and the alternative policy price for each monthly payment made by the complainant, from the time each actual PPI payment was made to the time the compensation is paid.

Monthly payments on the residual cost of PPI carried forward from loan 1 calculation	
The residual PPI on redemption of loan 1 as a % of loan 2 (Overpayment value of £319.16 / loan 2 amount of £14,200)	2.25% (rounded)
Loan 2 monthly payment used towards paying off residual cost of PPI on loan 1 (residual PPI of 2.25% x monthly payment without PPI on loan 2 of £301.71)	£6.78
Compensation for the overpayment on residual loan 1 PPI payments (loan 1 residual PPI of £6.78 x duration of 36 months)	£244 (rounded)
8% p.a. simple interest on historic payments	£30
Total monthly overpayment compensation payable for residual loan 1	**£274**

Historic monthly overpayments calculation for loan 2	
Cost per £100 of alternative regular premium PPI	£9
Therefore, monthly alternative regular premium PPI cost for loan 2 (based on monthly loan repayment without any PPI of £294.93)	£26.54
Monthly difference (actual PPI payments of £59.49– alternative regular premium PPI cost of £26.54)	£32.95
Compensation for the total difference in PPI payments (monthly difference of £32.95 x duration of payments of 36 months)	£1,186
8% p.a. simple interest (on historic monthly payments):	£146
Total monthly overpayment compensation payable for loan 2	**£1332**

Compensation payable on loan 2 (Monthly residual payments from loan 1 of £274 + Historic monthly overpayments for loan 2 of £1332) **£1606**

Total compensation payable on both loans (loan 1 of £280 plus loan 2 of £1606) **£1886**

In addition, as per DISP 3.7.4E(1)(a) the firm should, where possible, arrange for the loan to be restructured. For this example, in addition to the above compensation to be paid to the complainant:

1. any remaining residual PPI balance from the earlier refinanced loan should be removed; and

2. the future loan repayments would be £294.93 for the remaining term of loan 2; and

The customer should be given the option of maintaining the existing cover at the price of the alternative regular premium PPI cover for the remaining term of loan 2 at the alternative cost of £26.54 (based on the referent price of £9 per £100 of cover, applied to the monthly loan repayments of £294.93).

Implementing approaches for customers to pay for future cover

The four approaches for customers to pay for future cover

Approach A – set up a new arrangement for regular payments

1. The customer makes regular payments from a new payment arrangement. So, if the customer opts to maintain cover, the firm sets up a new payment arrangement, a direct debit for example, to collect a monthly payment based on the alternative referent price until the end of the single premium policy term. If the policy is cancelled before the end of the policy term, then the customer's payments stop.

Approach B – Withhold part of the redress to fund regular payments

2. In summary, the customer makes regular payments from part of the redress which the firm retains.

3. The firm compensates the customer for his previous PPI payments and removes the cost of the single premium PPI from the customer's loan balance in line with DISP App 3.7.3E, DISP App 3.7.4E. If the customer opts to maintain cover on a regular payment basis, the firm would calculate how much redress to hold back to cover the customer's future regular payments to the end of the original policy term. We would generally consider a fair offer should include some sort of discounting to reflect the fact that the firm, rather than the customer, holds the money. (This is particularly the case where the compensation payment for the customer's previous PPI payments is not sufficient to fund the future regular payments and so part of the loan balance effectively funds the future regular payments). If the customer cancels the policy before the end of the original term, the customer would, upon cancellation, be paid a pro-rata refund of the redress amount retained by the firm. An example of how this approach works in practice is provided below.

Approach C – Regular payments collected through loan repayment

4. In summary, the customer makes regular payments through the existing loan repayment mechanism.

5. The firm compensates the customer for his previous PPI payments and removes the cost of the single premium PPI from the customer's loan balance in line with DISP App 3.7.3E and DISP App 3.7.4E. If the customer opts to maintain cover on a regular payment basis, the firm would add an amount to the loan balance to collect the future regular payments. If the customer cancels the policy before the end of the original term, the loan balance would be adjusted so that post-cancellation the balance would not include any PPI cover. An example of how this approach works in practice is provided below.

Approach D – Non-referent price for maintaining cover

6. In summary, the customer does not make future regular payments.
7. The firm calculates compensation in line with DISP App 3.7.3E and DISP App 3.7.4E equal to:

- the sum of the customer's previous PPI payments plus
- the cost of removing the single premium PPI from the customer's loan balance less
- the current cancellation value.

8. This compensation would be offered to the customer. The customer can decide whether or not to apply it to his outstanding loan balance. If the customer decides to apply it to reduce the loan balance the firm should also pay any charges that arise (for example early repayment charges). The firm must also give the customer the option to cancel or retain the cover. If the customer cancels the cover, he would receive the cancellation value due to him according to the original policy terms (this value may well be automatically applied to the loan balance). If the customer opts to maintain cover, the cancellation value effectively becomes the price of the future cover. If the customer subsequently cancels before the end of the original policy term, the customer would receive, upon cancellation, a cancellation value in line with the policy's cancellation terms.

Worked examples

9. Consider Example 3 on page 4 above, which requires the firm to give the option of maintaining the cover at a cost of £18 per month. The following details should be considered supplementary to the information in Example 3.

Loan details	
Original total loan	£11,500
PPI premium	£2,300
APR	11%
Cancellation value of the PPI after 20 months	£1,035
Actual loan balance after 20 months	£8,342.12
Notional loan balance after 20 months (if single premium PPI was not added)	£6,673.66

	Loan balance with single premium PPI removed.	Loan balance (if cover continues and is added to the loan balance)	Difference in loan balances
After 20 months	£6,673.66	£7,272.50	£598.84
After 32 months	£4,921.14	£5,362.05	£440.91
After 44 months	£2,965.82	£3,230.54	£264.72
After 56 months	£784.25	£853.36	£69.11

10. The section below takes each of the approaches and explains how they work in practice.

Approach A – set up a new payment arrangement for regular premiums

11. As per Example 3, the firm must offer the customer £685 as compensation for the single premium PPI payments made. The firm must also offer to adjust the loan balance to £6,673.66, by crediting the balance with £1,668.46 (assuming that the customer incurs no further charges) to remove the PPI from the loan.

12. The firm must also offer the customer the option of retaining cover on a regular payment basis. If this approach is adopted it would require the firm to set up a new payment arrangement, such as a direct debit to collect the regular monthly payments of £18. If the customer subsequently cancels the PPI or stops making regular payments, then the cover ceases. No further payment is due to the customer at the point of cancellation (i.e. a rebate in accordance with the contract's cancellation terms) as this would over-compensate the customer. A value equivalent to the rebate amount should be paid by the insurer to the distributor of the single premium policy.

Approach B – Withhold part of the redress to fund regular premiums

13. As per Example 3, the firm must offer the customer £685 as compensation for the PPI payments made, unless the customer opts to retain cover (as discussed in the following paragraph). The firm must also offer to adjust the loan balance to £6,673.66, by crediting the balance with £1,668.46 (assuming that the customer incurs no further charges) to remove the PPI from the loan, unless the customer opts to retain cover (as discussed in the following paragraph).

14. The firm must offer the customer the option of retaining cover on a regular payment basis. If this approach is adopted it would require the firm to hold £720[2] of redress otherwise payable to the customer (i.e. the regular payment amount of £18 for the remaining term of the policy – 40 months), but discounted at a fair commercial rate. The impact of this is, if the customer accepts the offer, the customer would not receive the £685 compensation payment as this would be held by the firm to fund the future regular payments. The firm would credit the loan with £1,633.46 (i.e. £1,668.46 less (£720 - £685). If the customer subsequently cancels the PPI before the end of the policy term, the firm must pay the customer a pro-rata refund of the £720 held (plus any additional interest incurred by the customer if PPI was not fully removed from the loan balance)[3]. This should be clearly explained in any offer and the firm could include a table outlining the future cost of cover such as:

If you cancel after…	You will receive…[4]	And the equivalent monthly cost is…
…12 months from	£504	£18 per month

[2] If this figure is discounted by 4% the firm would actually hold £630, but here we have used £720 to better illustrate the impact on the loan balance redress.

[3] As per Approach A, no other rebate payment is due to the customer at the point of cancellationas this would over-compensate the customer.

[4] ie 720 x (60-32)/40 = 504
720 x (60 -44)/40 = 288
720 x (60-56)/40 = 72

the date of this offer[5]		
…24 months from the date of this offer	£288	£18 per month
…36 months from the date of this offer	£72	£18 per month

Approach C – Regular premiums collected through loan repayment

15. As per Example 3, the firm must offer the customer £685 as compensation for the PPI payments made. The firm must also offer to adjust the loan balance to £6,673.66, by crediting the balance with £1,668.46 (assuming that the customer incurs no further charges) to remove the PPI from the loan.

16. The firm must also offer the option of retaining the cover on a regular payment basis. If this approach is adopted it would require the future loan repayments to be adjusted to £218 (i.e. the monthly loan repayment without the single premium PPI of £200 plus the regular payment amount of £18). How this is achieved is up to the firm. We see two options (for which the firm would need to consider the Consumer Credit Act implications):

- First, the firm adjusts the monthly loan repayment amount to £218, but only credits the loan balance monthly with £200. The £18 reflects the regular payment for the retained PPI cover. If the customer subsequently cancels the PPI, then the firm must reduce the loan repayment amount back to £200[6].

- Second, the firm adjusts the customer's loan balance to drive a repayment amount of £218. Consider the table below. The second column shows what the customer's loan balance would be without any PPI. The third column shows what the loan balance would be if the firm was to adjust the loan balance to drive a repayment amount of £218. The fourth column shows the difference in the two balances and therefore is the amount that the firm would have to either add to or subtract from the loan balance if the customer opted to retain cover on a regular payment basis or subsequently cancelled the cover.

	Loan balance with PPI removed.	Loan balance (if cover continues and is added to the loan balance)	Difference in loan balances
After 20 months	£6,673.66	£7,272.50	£598.84
After 32 months	£4,921.14	£5,362.05	£440.91
After 44 months	£2,965.82	£3,230.54	£264.72
After 56 months	£784.25	£853.36	£69.11

17. So in relation to the second option above, in this example if the customer opts to maintain cover on a regular payment basis, the loan balance would increase from £6,673.66 to £7,272.50 to drive a repayment amount of £218 over the remaining term. If the customer subsequently cancels the PPI and **keeps** the loan, say after

[5] ie 32 months from beginning of policy term.
[6] As per previous examples, no rebate is payable to the customer at the point of cancellation.

44 months, the firm would reduce the loan balance to £2,965.82 which would lower the repayment amount back to £200. If the customer subsequently cancels the PPI before the end of the policy term and **redeems** the loan, the future cost of cover must be removed from the redemption amount. So, after 44 months this would be £264.72. This should be clearly explained in any offer and the firm could include a table outlining the future cost of cover and the impact on the loan balance, such as:

If you cancel after…	Your loan will be credited with…[7]	And the equivalent monthly cost is…
…12 months from the date of this offer	£440.91	£18 per month
…24 months from the date of this offer	£264.72	£18 per month
…36 months from the date of this offer	£69.11	£18 per month

Approach D – Non-referent price for maintaining cover

18. As per Example 3, the firm must offer the customer £685 as compensation for the PPI payments made. The firm must also offer to compensate the customer by the difference between the actual loan balance after 20 months and the notional loan balance after 20 months (if PPI had not been added), so £1,668.46; however, the firm may deduct from the compensation amount the current cancellation value, which is £1,035 on this example. So in summary, the firm's redress offer is: £685 + £1,668.46 - £1,035 = £1,318.46. The firm should explain to the customer that he has the option of using the redress to reduce his loan balance. If any fees are incurred as a result of the customer exercising this option, for example early repayment charges, the firm should also offer to pay these fees.

19. The firm must also explain to the customer that he has the choice of either retaining the policy, and therefore keeping the cover at the price implied by the original policy's cancellation terms, or, cancelling the policy and receiving the cancellation amount. If the customer does cancel the policy, then his future loan repayments should be as they would be if no PPI was added (i.e. £200 in this example).

20. If the customer chooses to retain the cover, then the cancellation amount would effectively become the cost of the future cover. This means that the cost of the future cover will not always equal to £9 per £100 of benefits. In this example, the policy has 40 months to run. The cancellation amount is £1,035. So, the monthly cost of cover would be £25.87 per month (assuming that the customer retains the policy for the full term of 40 months: 1035 ÷ 40), compared to £18 for the other three approaches.

21. We closely considered the impact of this in deciding whether this approach produced fair customer outcomes, which is discussed in detail below. In

[7] ie the differences in the loan balances above

summary, we believe the outcome for customers is fair; however, the offer must be presented fairly so that the customer is clearly able to understand the cost of the cover for the remaining term if this approach was adopted by the firm. The firm could, for example, include a table outlining the future cost of cover based on the cancellation value at the time of offer and the remaining term such as:

If you cancel after…	You will receive…[8]	And the equivalent monthly cost is…
…12 months from the date of this offer	£575	£38.33 per month
…24 months from the date of this offer	£115	£38.33 per month
…36 months from the date of this offer	£0	£28.75 per month

22. We include this option due to the difficulties that brokers (those that broker the loan and the insurance, rather than just the insurance) might have in implementing the previous three approaches, being unable to change the loan terms and hold redress payments due to client money requirements. As such, this approach is reserved for the broker segment of the industry. If other firms wish to apply this approach, they must be able to demonstrate why they were unable to implement the previous three approaches.

Do these options provide fair customer outcomes?

23. We considered whether the difference in the above approaches would provide different customer outcomes. Where these outcomes differed we considered whether we felt that the outcome remained fair for the customer. To test this risk we modelled the consumer outcome using each of the above implementation approaches, but changed variables such as the time of complaint, the policy and loan features, and the length of time the customer retains the cover on a regular premium basis. We found that:

   - Approaches A, B and C provide the same amount of redress throughout the period of the policy, though when the customer actually receives this redress varies for approach B (as some money is retained by the firm to pay for future regular premiums).

   - Approach D offers the same redress as approaches A, B and C at the point of complaint, but potentially a different amount if the customer chooses to retain the cover. The price of future cover will depend on three variables: the price of the original cover, the cancellation terms set out in the original policy and when the customer actually cancels.

[8] Assuming cancellation terms of: 65% in year 1, 45% in year 2, 25% in year 3, 5% in year 4 and 0% in year 5 equivalent monthly costs are calculated as:

(1035-575)/12 = 38.33
(1035-115)/24 = 38.33
(1035-0)/36 = 28.75

24. Given the above findings, we closely considered whether it was appropriate to allow firms to take Approach D. We felt it important to have an approach that could be implemented by brokers. We felt that the risks of a potentially different customer outcome for approach D from A, B and C could be sufficiently mitigated if firms clearly explain the nature and consequences of the offer. We have limited use of approach D to brokers because of the potential for different customer outcomes to approaches A, B and C.

25. In making any offer under any of the approaches, we expect firms to act reasonably, treat customers fairly and meet the spirit of these proposals. This is particularly the case when a firm intends to apply approach D where the price of future cover differs materially from the alternative regular premium PPI referent price.

The implications of the Consumer Credit Act for our redress approaches

The implications of the Consumer Credit Act for our redress approaches

Restructuring loans

Some industry responses stated that our provisions do not reflect the implications of the Consumer Credit Act 1974 (CCA), in particular that:

- we had not considered its impact on a firm's ability to restructure a loan to remove the finance of the single premium PPI;
- using a modifying agreement to restructure loans implied complexity and operational difficulties; and
- there are practical difficulties of aligning the modified loan with the existing loan (for example, the payment dates and the loan balance) while complying with CCA information disclosure requirements during the consideration period.

Some responses also asked for clarification as to whether we consider the use of modifying agreements as a solution for both the full 'return of premium' approach to redress and the four approaches to comparative redress, arguing that:

- while some lenders may wish to avoid the need to use a modifying agreement by cancelling the PPI credit without affecting the loan, this option calls into question whether the PPI and principal credit agreements can be regarded as multiple agreements under s.18(1)(a) of the CCA; and
- while some lenders may wish to avoid the need to use a modifying agreement by issuing a new credit agreement, this option will not be readily available for firms that no longer write new business.

Our response: As set out on page 54 of CP10/06, we have been informed by the Office of Fair Trading (OFT) that where credit to finance PPI is sold alongside a loan, this gives rise to a multiple agreement within sections 18(1)(a) and 18(2) CCA. The principal credit agreement and the agreement financing the PPI are treated as separate agreements for the purposes of the CCA.

We do not, therefore, believe that a modifying agreement will always be necessary. It should be possible to cancel the PPI agreement without affecting the principal credit agreement, provided that the implications of this (including for the periodic repayments) are made clear to the consumer. Whether or not this is practicable and appropriate would be for each individual firm to decide in the light of its own business circumstances. Some of the other methods we believe firms may consider using are discussed below.

We contacted the OFT to provide us with further understanding on the use of modifying agreements. It responded that, whilst using a modifying agreement may be more complicated than simply cancelling the PPI credit agreement (as explained on page 54 of CP 10/6), it is aware of modifying agreements currently being used by some firms.

Further, the OFT indicates that the rules on modifying agreements will become easier to comply with following implementation of the Consumer Credit Directive (CCD).[1] Where these new rules apply, a modifying agreement will still need to be signed by both parties, but broadly need only provide the information that is changing as a result of the modification (and indicate that all other information remains unchanged)

So, we remain of the view that, notwithstanding any operational difficulties, modifying agreements are a possible method (among others) for restructuring a credit agreement to remove the finance of the single premium PPI. This applies whether the firm takes the full return of premium approach to redress or approaches A, B and C to comparative redress. Approach D is intended solely for loan brokers that are unable to restructure a loan or deal with regular premium collection, so we do not expect modifying agreements to be used by firms applying Approach D.

As explained above, we believe there are alternative methods firms could consider using to restructure loans, when providing redress, including the following:

- Issue a new credit agreement replacing both the original principal agreement and the PPI agreement. This removes the need for the firm to enter into a modifying agreement and in effect refinances the original loan. The new credit agreement must adhere to the requirements under the CCA. The OFT advises it would be likely to consider it unfair if the firm did not waive any early settlement charges that might otherwise apply on the redemption of the original loans.

- As mentioned on page 55 of CP10/6, the firm may be able to simply refrain from enforcing relevant aspects of the original principal agreement and/or the PPI agreement as a unilateral concession, but the unilateral concession should be documented in some durable way, such as a letter acknowledging it to the customer.

- Alternatively, the firm may, under s.82(1) of the CCA, rely on a power contained in the original principal agreement and/or the PPI agreement to vary unilaterally the terms and conditions of the agreement.

- Another method available for loan brokers or intermediaries if adopting the comparative redress, is to apply Approach D as described on page 50 of CP10/6.

- If none of the above options were suitable, we would still expect a firm to be able to provide redress by applying DISP App 3.7.4E(1)(b).

We do not consider that the validity of these alternative methods would depend on whether or not the PPI credit agreement is treated as a multiple agreement in parts by virtue of section 18 of the CCA, although this may affect how any changes are documented.

[1] The regulations implementing the CCD are due to come into force on 1 February 2011, although it will be open to firms to comply earlier if they wish.

Affordability assessments

One industry response highlighted that restructuring of loans carried out in light of our provisions would result in affordability assessments having to be undertaken in accordance with the OFT's Irresponsible Lending Guidance (OFT Guidance).[2]

Our response: We contacted the OFT to better understand the implications of the OFT Guidance for firms. Our intention is not to provide detailed instructions on how firms should interpret or comply with the OFT Guidance. Any concerns or queries over a firm's responsibilities under the OFT Guidance should be addressed to the OFT directly.

Our understanding is that the OFT expects firms to monitor borrowers' repayment records and to consider affordability issues throughout the lifetime of a credit agreement (subject to proportionality considerations), not just prior to a credit agreement being made with the borrower or prior to the restructuring of an existing credit agreement.

On the above basis, our provisions should not give rise to a new obligation as such on firms to assess affordability (though we recognise that the restructuring of an existing credit agreement will act as a 'trigger' for affordability to be reconsidered and that, therefore, our proposals may increase the frequency of the process). The OFT confirms that the following considerations are relevant when firms consider a restructure of the loan due to a mis-sale of PPI:

- If the firm was already aware that a borrower was experiencing financial difficulty, prior to the restructuring, the OFT would expect it to have already reconsidered affordability issues and taken appropriate action. If not, the rescheduling provides an opportunity for the firm to reconsider affordability.
- In reconsidering affordability, a firm should take account of whether there has been any material change to the borrower's financial circumstances since the credit agreement was made (at which time the agreement should only have been made if it was appropriately assessed as being affordable) and whether the way the credit agreement is being restructured is likely, in itself, to have any adverse impact on the borrower's ability to continue to meet repayments in a sustainable manner or any other adverse impact on the borrower's financial circumstances.
- If a firm discovers at the point of restructure that the borrower appears as if he is experiencing financial difficulty, or likely to experience financial difficulty in the future (even with a reduction in the balance on the credit agreement and monthly payments), then it should take appropriate action in line with the OFT Guidance.

The OFT further confirms that the primary purpose of the OFT Guidance is to provide clarity on the types of business practices that the OFT may regard as constituting irresponsible lending practices for the purposes of section 25(2B) of the CCA. It is not intended to discourage an appropriate restructure following a mis-sale.

[2] See: http://www.oft.gov.uk/shared_oft/business_leaflets/general/oft1107.pdf

Open letter, listing common PPI sales failings, with a mapping to our Handbook provisions

Direct line: 020 7066 1100
Local fax: 020 7066 1101
Email: Christina.sinclair@fsa.gov.uk

Stephen Haddrill, ABI
Chris Cummings, AIFA
Paul Smee, UK Payments Administration
Angela Knight, BBA
Eric Galbraith, BIBA
Adrian Coles, BSA
Michael J Coogan, CML
Stephen Sklaroff, FLA

COMMON POINT OF SALE FAILINGS FOR PPI SALES

Today the FSA has published guidance for the proper handling of PPI complaints. In consultation with stakeholders on these proposals and from our on-going supervisory work with firms and other intelligence, we have become concerned that one reason many firms are not handling PPI complaints correctly is because they are not applying the appropriate standards for the sale of this product. This is despite our having repeatedly reminded firms of these standards in numerous speeches, thematic reports and other publications over recent years. In order to remind your members of the appropriate standards, we have set out, in the appendix to this letter, common failings at the point of sale which result in poor outcomes for consumers. These failings have come to our attention, through thematic work, mystery shopping, and enforcement actions. They are not intended to be exhaustive.

As I am sure you will agree, there is no excuse for these failings and we will continue to take robust action – including disciplinary and other formal action as appropriate – when we identify them.

The FSMA regulatory framework covering the sale of general insurance commenced on 14 January 2005, so our Principles for Business and conduct of business rules have applied to PPI sales made on or after that date. In the FSA's view, the general principles of fair conduct by firms when selling PPI before 14 January 2005 have much in common with our standards after this date (see, for example, relevant extracts from GISC and ABI codes set out in the appendix). Firms should have regard to the list of failings when considering their point of sale obligations for earlier sales, including in the context of assessing complaints about such sales.

Yours sincerely

Christina Sinclair
Head of Department
Retail Policy and Conduct Risk Division

COMMON TYPES OF FAILINGS IN PPI SALES

General failings in the conduct of the sale

1. The firm:

- pressured the customer into taking a payment protection policy; or
- assumed the customer would want the payment protection policy from the outset (e.g. by automatically including it in a loan quotation); or
- led the consumer to believe that the payment protection policy had to be taken in order to obtain the loan (or other goods or services) or would improve his prospects of doing so; or
- made the sale without the customer's explicit agreement to purchase the payment protection policy; or
- did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, that:
    - the payment protection policy was optional; or
    - the purchase of the payment protection policy involved the purchase of an insurance policy.

2. The firm did not disclose to the customer, in a way that was clear, fair and not misleading, the duration of the cooling-off period or that the customer could cancel the policy within the cooling-off period in good time before the conclusion of the sale (and under ICOBS did not also disclose that cancellation during the cooling-off period is without penalty).

3. The firm did not explain whether it was selling on an advised or non-advised basis.

4. The firm did not provide the written documents required under the FSA's rules (such as, for example, a policy summary, statement of price, or statement of demands and needs) and, where relevant, did not stress to the customer the importance of reading the material.

5. The firm provided misleading or inaccurate information about the policy.

Failings around eligibility, exclusions and limitations

6. The firm did not take reasonable steps to ensure the customer only bought a policy for which he was eligible to claim benefits.

7. While arranging the policy, the firm was aware (or ought reasonably to have been aware) that parts of the cover did not apply but did not so disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading.

8. The firm did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, the significant exclusions and limitations that would tend to affect the decisions of customers generally to buy the policy.

Failings specific to non-advised sales

9. Where seeking to sell on a non-advised basis, the firm:

- failed to make it clear it was only providing information on the policy; or
- gave advice to the customer regarding the policy (e.g. expressed an opinion on the merits of buying the policy).

Failings specific to advised sales

10. The firm advised on a policy without:

- taking reasonable steps to properly establish the customer's demands and needs; for example, not seeking information from the customer on:
  - existing means the customer already had of protecting the loan (including existing insurance, benefits from employer, and assets such as savings and investments); any pre-existing medical conditions which might be excluded under the policy; whether the policy would be affordable in light of the customer's income and outgoings; and whether the customer's circumstances were likely to change; or
  - (for single premium policies) whether there was a prospect that the customer would repay or refinance the loan before the end of the term of the policy; or
- taking reasonable care to ensure that the policy was suitable for the customer's demands and needs taking into account all relevant factors, including level of cover, cost, and relevant exclusions, excesses, limitations and conditions.

11. The firm advised on a policy without disclosing to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading:

- that any of the customer's demands and needs would not be met; or
- that a part of the cover did not meet a demand or need; or
- any exclusions and limitations which were particularly relevant to that individual customer.

Failings around price disclosure

12. The firm did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading:

- the total (not just monthly) cost of the policy separately from any other prices (or the basis for calculating it so that the customer could verify it) and, for sales of regular premium policies, this included providing the total cost of the premiums; or
- (for a policy of over one year with reviewable premiums) the period for which the quoted premium was valid, and the timing of premium reviews; or
- (for sales under ICOBS) price information calculated in a way to enable the customer to relate it to a regular budget.

Additional failings specific to single premium policy sales

13. The firm sold the customer a policy where the total cost of the policy (including any interest paid on the premium) would exceed the benefits payable under the policy (other than benefits payable under life cover).

14. The firm failed to disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading:

- that the premium would be added to the amount provided under the credit agreement, that interest would be payable on it and the amount of that interest; or
- that the term of the cover was shorter than the term of the credit agreement and the consequences of such mismatch.

15. The firm failed to disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, that the customer would not receive a pro-rata refund if the customer were to repay or refinance the loan or otherwise cancel the single premium policy after the cooling-off period.*

* This applies wherever the disclosure was likely to be relevant to the customer. We have made clear in the past "firms should consider whether they must draw the refund term to the customer's attention as a significant limitation of the policy in the policy summary". In our view, a firm properly considering the issue would have concluded that it must disclose whenever it was likely to be relevant to the customer, for example, because there was a prospect that the customer would repay or refinance the loan before the end of the term of the policy. When considering whether disclosure should have been provided, the firm should take into account both available information on the general behaviour of customers, and information of which the firm was aware (or ought reasonably to have been aware) about the particular customer.

Face-to-face and telephone sales – clear, fair and not misleading communication

The Principles require firms to pay due regard to a customer's information needs and communicate information to the customer in all situations in a way that is clear, fair and not misleading. In sales primarily conducted orally, it was not enough just to provide important information in writing. So, we have found it to be a failing where there was not a fair presentation of the information during the sales discussion, by, for example:

• giving an oral explanation; or

• specifically drawing the customer's attention to the information on a computer screen or in a document and giving the customer time to read and consider it.

In addition, the requirement to pay due regard to a customer's information needs and communicate information in a clear, fair and not misleading way required the firm to provide balanced information when making reference to a policy's main characteristics (whether orally or in writing). So, we have found it to be a failing if, where the firm described the benefits of the policy orally, it did not also provide an adequate description of the corresponding limitations and exclusions in a way that was clear, fair and not misleading, for example orally. Further, ICOBS requires that, if a firm provides information orally during a sales dialogue with a customer on a main characteristic of a policy, it must do so for all the policy's main characteristics.

Common types of failings in PPI sales – Relevant FSA Handbook provisions[1]

	Failure	Principles	ICOB / ICOBS
1	The firm: • pressured the customer into taking a payment protection policy; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
	• assumed the customer would want the payment protection policy from the outset (e.g. by automatically including it in a loan quotation); or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
	• led the consumer to believe that the payment protection policy had to be taken in order to obtain the loan (or other goods or services) or would improve his prospects of doing so; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R and 5.5.14R (Statement of price) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.1.13R (Price disclosure: connected goods or services) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision)
	• made the sale without the customer's explicit agreement to purchase the payment protection policy; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) ICOBS:

[1] This table lists the most relevant FSA Principles, rules and guidance in relation to each common failing identified in the conduct of PPI sales. This is not an exhaustive list and other FSA Handbook provisions may be relevant depending on the facts and circumstances of a particular case.

This table does not list relevant aspects of the general law, which may also be applicable depending on the facts and circumstances of the case, such as the Consumer Protection from Unfair Trading Regulations 2008, the Misrepresentation Act 1967, and common law principles such as duty of care or statutory duty (for example, under section 150 of the Financial Services and Markets Act 2000).

	Failure	Principles	ICOB / ICOBS
			2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
	• did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, that: • the payment protection policy was optional; or	P.6, P.7	<u>ICOB:</u> 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R and 5.5.14R (Statement of price) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.1.13R (Price disclosure: connected goods or services) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision)
	• the purchase of the payment protection policy involved the purchase of an insurance policy.	P.6, P.7	<u>ICOB:</u> 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.2.2R and 4.2.8R (Status disclosure) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R, 5.5.1R and 5.5.5R (Policy summary) 5.3.1R(2) (Drawing orally to the customer's attention importance of reading policy summary) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 4.1.2R (Status disclosure) 4.1.6R (Scope of service) 4.2.2G and 4.2.3G (Ensuring customers can make an informed decision) 4.2.4R (Limits of service provided) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can

	Failure	Principles	ICOB / ICOBS
			make an informed decision) 6.4.4R and Annex 2R (Policy summary) 6.4.5R (Payment protection contracts: importance of reading documentation)
2	The firm did not disclose to the customer, in a way that was clear, fair and not misleading, the duration of the cooling-off period or that the customer could cancel the policy within the cooling-off period in good time before the conclusion of the sale (and under ICOBS did not also disclose that cancellation during the cooling off period was without penalty).	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R, 5.5.1R and 5.5.5R (Policy summary) 5.3.1R(2) (Draw to customer's attention importance of reading policy summary) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.2.5R (Disclosure of cancellation right) 6.4.4R and Annex 2R (Policy summary) 6.4.5R (Payment protection contracts: importance of reading documentation)
3	The firm did not explain whether it was selling on an advised or non-advised basis.	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.2.2R and 4.2.8R (Status disclosure) 4.4.1R (Statement of demands and needs) 4.4.2R (Exemptions) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 4.1.7R (Scope of service) 4.2.2G and 4.2.3G (Ensuring customers can make an informed decision) 4.2.4R (Disclosing the limits of the service provided) 4.2.5R (Status disclosure for insurers)
4	The firm did not provide the written documents required under the FSA's rules	P.6, P.7	ICOB:

	Failure	Principles	ICOB / ICOBS
	(such as, for example, a policy summary, statement of price, or statement of demands and needs) and, where relevant, did not stress to the customer the importance of reading the material.		2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.2.2R and 4.2.8R (Status disclosure) 4.4.1R (Statement of demands and needs) 5.3.1R(1) (Provision of information to retail customers before the conclusion of a contract which is not a distance contract) 5.3.1R(2) (Drawing orally to the customer's attention importance of reading policy summary) 5.3.4R (Provision of information to retail customers on conclusion of a contract which is not a distance contract) 5.3.6R (Provision of information to retail customers before the conclusion of a distance contract) 5.3.8R (Provision of information to retail customers on conclusion of a contract which is a distance contract) 5.3.15R, 5.3.16R, 5.3.18R and 5.3.21R (Provision of information to retail customers on renewal) 5.3.24R and 5.3.25R (Provision of information to retail customers on mid-term changes) <u>ICOBS</u>: 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 4.1.2R (Status disclosure) 4.1.6R and 4.1.7R (Scope of service) 4.1.9R (Means of communication to customers) 4.2.4R (Limits of service provided) 4.2.5R (Status disclosure for insurers) 4.3.1R (Fees disclosure) 5.2.2R and 5.2.3R (Statement of demands and needs) 6.2.2R to 6.2.5R (Non-life insurance directive disclosure requirements) 6.3.1R (Life insurance directive disclosure requirements) 6.3.3R (Mid-term changes) 6.4.4R (Policy summary) 6.4.5R (Payment protection contracts: importance of

	Failure	Principles	ICOB / ICOBS
			reading documentation) 6.4.6R, 6.4.7G and 6.4.8G (Price information: general) 6.4.9R (Price information: premiums paid using a non-revolving credit agreement) 6.4.11R (Mid-term changes)
5	The firm provided misleading or inaccurate information about the policy.	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
6	The firm did not take reasonable steps to ensure the customer only bought a policy for which he was eligible to claim benefits.	P.6 and for advised sales also P.9	ICOB: 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.4G (Demands and needs statement for non-advised sales) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of demands and needs) ICOBS: 5.1.2R and 5.1.3G (Eligibility to claim benefits: payment protection contracts) 5.1.4G (Disclosure of material facts) 5.2.2R (statement of demands and needs) 5.2.4G (Statement of demands and needs: non-advised sales) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
7	While arranging the policy, the firm was aware (or ought reasonably to have been aware) that parts of the cover did not apply but did not so disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading.	P.6, P.7 and for advised sales also P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs)

	Failure	Principles	ICOB / ICOBS
			4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.4G (Demands and needs statement for non-advised sales) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of demands and needs) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 5.1.2R (Eligibility to claim benefits: payment protection contracts) 5.1.4G (Disclosure of material facts) 5.2.2R (Statement of demands and needs) 5.2.4G (Statement of demands and needs: non-advised sales) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
8	The firm did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, the significant exclusions and limitations that would tend to affect the decisions of customers generally to buy the policy.	P.6, P.7 and for advised sales also P.9	<u>ICOB:</u> 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R, 5.5.1R and 5.5.5R (Policy summary) 5.3.1R(2) (Drawing orally to the customer's attention importance of reading policy summary) 5.5.6G and 5.5.8G to 5.5.10G (Guidance on significant or unusual exclusions or limitations) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision)

	Failure	Principles	ICOB / ICOBS
			6.4.4R and Annex 2R (Policy summary) 6.4.5R (Payment protection contracts: importance of reading documentation)
9	Where seeking to sell on a non-advised basis, the firm: • failed to make it clear it was only providing information on the policy; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.2.2R and 4.2.8R (Status disclosure) 4.4.1R (Statement of demands and needs) 4.4.2R (Exemptions) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 4.1.7R (Scope of service) 4.2.2G and 4.2.3G (Ensuring customers can make an informed decision) 4.2.4R (Disclosing the limits of the service provided) 4.2.5R (Status disclosure for insurers)
	• gave advice to the customer regarding the policy (e.g. expressed an opinion on the merits of buying the policy).	P.6, P.7, P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.2.2R and 4.2.8R (Status disclosure) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R (Statement of demands and needs) 4.4.2R (Exemptions) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 4.1.7R (Scope of service) 4.2.2G and 4.2.3G (Ensuring customers can make an informed decision) 4.2.4R (Disclosing the limits of the service provided) 4.2.5R (Status disclosure for insurers) 5.2.2R (Statement of demands and needs) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) • Also see: PERG 5.8.8G to 5.8.11G

	Failure	Principles	ICOB / ICOBS
10	The firm advised on a policy without: • taking reasonable care to properly establish the customer's demands and needs; for example, not seeking information from the customer on: o existing means the customer already had of protecting the loan (including existing insurance, benefits from employer, and assets such as savings and investments); any pre-existing medical conditions which might be excluded under the policy; whether the policy would be affordable in light of the customer's income and outgoings; and whether the customer's circumstances were likely to change; or	P.6, P.9	ICOB: 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) ICOBS: 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
	o (for single premium policies) whether there was a prospect that the customer would repay or refinance the loan before the end of the term of the policy; or	P.6, P.9	ICOB: 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) ICOBS: 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
	• taking reasonable care to ensure that the policy was suitable for the customer's demands and needs taking into account all relevant factors, including level of cover, cost, and relevant exclusions, excesses, limitations and conditions.	P.6, P.9	ICOB: 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) ICOBS: 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
11	The firm advised on a policy without disclosing to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading: • that any of the customer's demands and needs would not be met; or	P.6, P.7, P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of

	Failure	Principles	ICOB / ICOBS
			demands and needs) ICOBS:, 2.2.2R (Clear, fair and not misleading rule) 5.2.2R (Statement of demands and needs) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
	• that any part of the cover did not meet a demand or need; or	P.6, P.7, P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of demands and needs) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 5.2.2R (Statement of demands and needs) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
	• any exclusions and limitations which were particularly relevant to that individual customer.	P.6, P.7, P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of

	Failure	Princip les	ICOB / ICOBS
			demands and needs) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 5.2.2R (Statement of demands and needs) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision)
12	The firm did not disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading: • the total (not just monthly) cost of the policy separately from any other prices (or the basis for calculating it so that the customer could verify it) and, for sales of regular premium policies, this included providing the total cost of the premiums; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R and 5.5.14R to 5.5.15AG (Statement of price) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.1.13R (Price disclosure: connected goods or services) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.7G and 6.4.8G (Price information: general) 6.4.9R (Price information: premiums paid using a non-revolving credit agreement)
	• (for a policy of over one year with reviewable premiums) the period for which the quoted premium was valid, and the timing of premium reviews; or	P.6, P.7	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R and 5.5.14R (Statement of price) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules)

	Failure	Principles	ICOB / ICOBS
			3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.7G and 6.4.8G (Price information: general)
	• (for sales under ICOBS) price information calculated in a way to enable the customer to relate it to a regular budget.	P.6, P.7	ICOBS: 2.2.2R (Clear, fair and not misleading rule) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.6R (Price information: general)
13	The firm sold the customer a policy where the total cost of the policy (including any interest paid on the premium) would exceed the benefits payable under the policy (other than benefits payable under life cover).	P.6 and for advised sales also P.9	ICOB: 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) ICOBS: 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies)
14	The firm failed to disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading: • that the premium would be added to the amount provided under the credit agreement, that interest would be payable on it and the amount of that interest; or	P.6, P.7 and for advised sales also P.9	ICOB: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R and 5.5.14R (Statement of price) ICOBS: 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can

	Failure	Principles	ICOB / ICOBS
			make an informed decision) 6.4.9R (Price information: premiums paid using a non-revolving credit agreement)
	• that the term of the cover was shorter than the term of the credit agreement and the consequences of such mismatch.	P.6, P.7 and for advised sales also P.9	<u>ICOB:</u> 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs) 4.4.4G (Demands and needs statement for non-advised sales) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of demands and needs) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 5.2.2R (Statement of demands and needs) 5.2.4G (Statement of demands and needs: non-advised sales) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.9R (Price information: premiums paid using a non-revolving credit agreement)
15	The firm failed to disclose to the customer, in good time before the sale was concluded, and in a way that was clear, fair and not misleading, that the customer would not receive a pro-rata refund if the customer were to repay or refinance the loan or otherwise cancel the single premium policy after the cooling-off period.* * This applies wherever the disclosure was likely to be relevant to the customer. We have made clear in the past "firms	P.6, P.7 and for advised sales also P.9	<u>ICOB</u>: 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.3.1R (Requirement for suitability) 4.3.2R to 4.3.5R (Information about the customer's demands and needs) 4.3.6R and 4.3.7G (Assessing the suitability of a contract against the customer's demands and needs) 4.4.1R and 4.4.3G (Statement of demands and needs)

	Failure	Principles	ICOB / ICOBS
	should consider whether they must draw the refund term to the customer's attention as a significant limitation of the policy in the policy summary". In our view, a firm properly considering the issue would have concluded that it must disclose whenever it was likely to be relevant to the customer, for example, because there was a prospect that the customer would repay or refinance the loan before the end of the term of the policy. When considering whether disclosure should have been provided, the firm should take into account both available information on the general behaviour of customers, and information of which the firm was aware (or ought reasonably to have been aware) about the particular customer.		4.4.4G (Demands and needs statement for non-advised sales) 4.4.5G (Demands and needs statement when a personal recommendation is made) 4.4.6G (Guidance on the contents of the statement of demands and needs) 5.2.13G (Provision of information to customers 'in good time') 5.3.1R, 5.3.6R, 5.5.1R and 5.5.5R (Policy summary) 5.3.1R(2) (Drawing orally to the customer's attention importance of reading policy summary) 5.5.6G and 5.5.8G to 5.5.10G (Guidance on significant or unusual exclusion or limitation) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 3.1.3R and Annex 2R (The distance marketing disclosure rules) 3.1.8R (Terms and conditions, and form) 3.1.14R and Annexes 2R and 3R (Exception: voice telephony communications) 5.2.2R (Statement of demands and needs) 5.2.4G (Statement of demands and needs: non-advised sales) 5.3.1R (Suitability) 5.3.2G (Suitability guidance for protection policies) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.2.5R (Disclosure of cancellation right) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.4R and Annex 2R (Policy summary) 6.4.5R (Payment protection contracts: importance of reading documentation)
	Face-to-face and telephone sales – clear, fair and not misleading communication The Principles require firms to pay due regard to a customer's information needs and communicate information to the customer in all situations in a way that is clear, fair and not misleading. In sales primarily conducted orally, it was not enough just to provide important information in writing. So, we have found	P6, P7	<u>ICOB</u>: 2.2.1G (Purpose) 2.2.3R to 2.2.7G (Clear, fair and not misleading communication) 4.1.6G and 4.1.7G (Purpose) 5.1.9G (Purpose) 5.2.13G (Provision of information to customers 'in

	Failure	Princip les	ICOB / ICOBS
	it to be a failing where there was not a fair presentation of the information during the sales discussion, by, for example: • giving an oral explanation; or • specifically drawing the customer's attention to the information on a computer screen or in a document and giving the customer time to read and consider it. In addition, the requirement to pay due regard to a customer's information needs and communicate information in a clear, fair and not misleading way required the firm to provide balanced information when making reference to a policy's main characteristics (whether orally or in writing). So, we have found it to be a failing if, where the firm described the benefits of the policy orally, it did not also provide an adequate description of the corresponding limitations and exclusions in a way that was clear, fair and not misleading, for example orally. Further, ICOBS requires that, if a firm provides information orally during a sales dialogue with a customer on a main characteristic of a policy, it must do so for all the policy's main characteristics.		good time') 5.3.1R(2) (Drawing orally to the customer's attention importance of reading policy summary) <u>ICOBS:</u> 2.2.2R (Clear, fair and not misleading rule) 4.2.2G and 4.2.3G (Ensuring customers can make an informed decision) 6.1.5R to 6.1.10G (Ensuring customers can make an informed decision) 6.4.2R and 6.4.3G (Oral sales: ensuring customers can make an informed decision) 6.4.5R (Payment protection contracts: importance of reading documentation)

PUB REF: 002346

The Financial Services Authority
25 The North Colonnade Canary Wharf London E14 5HS
Telephone: +44 (0)20 7066 1000 Fax: +44 (0)20 7066 1099
Website: http://www.fsa.gov.uk

Registered as a Limited Company in England and Wales No. 1920623. Registered Office as above.