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**FINAL NOTICE**

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**To: Capital One Bank (Europe) Plc**

**Of: 350 Euston Road**  
**London**  
**NW1 3JJ**

**Date: 15 February 2007**

**TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (“the FSA”) gives you final notice about a requirement to pay a financial penalty.**

**1. THE PENALTY**

- 1.1. The FSA gave Capital One Bank (Europe) Plc ("the Firm/Capital One") a Decision Notice on 12 February 2007 which notified Capital One that pursuant to section 206 of the Financial Services and Markets Act 2000 ("FSMA"), the FSA had decided to impose a financial penalty of £175,000 on the Firm in respect of a breaches of the FSA's Principles for Businesses ("the FSA Principles").
- 1.2. Capital One confirmed on 31 January 2007 that it will not be referring the matter to the Financial Services and Markets Tribunal.
- 1.3. Accordingly, for the reasons set out below and having agreed with the Firm the facts and matters relied on, the FSA imposes a financial penalty on Capital One in the amount of £175,000.

## **2. REASONS FOR THE PENALTY**

- 2.1. The penalty is imposed on Capital One in respect of breaches of the FSA Principles referred to in paragraphs 3.3 – 3.5. These occurred over various periods between 14 January 2005 and 5 April 2006, in relation to the sale by the Firm of payment protection insurance ("PPI") policies. The breaches relate to Capital One:
- (1) failing to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems (Principle 3); and
  - (2) failing to pay due regard to the interests of its customers and failing to treat them fairly (Principle 6).
- 2.2. Capital One breached Principles 3 and 6 by failing to have in place adequate systems and controls in relation to the sale of PPI to ensure that its customers were treated fairly.
- 2.3. As a result of the inadequate systems and controls:
- (1) the Firm failed to send a policy document to 98,000 of its 1.3 million PPI customers (of which 48,000 related to the period prior to FSA regulation<sup>1</sup>);
  - (2) two out of four script options used for all telephone sales did not ask the customer for consent explicitly to receive only limited information over the telephone;
  - (3) the form of disclosure used in scripts for customers who purchased PPI over the telephone did not ensure adequate disclosure, in an acceptable number of cases, of:
    - (a) policy features and benefits; and
    - (b) policy exclusions and limitations;
  - (4) the Firm failed to provide customers who purchased PPI other than by telephone with the policy document prior to the conclusion of the contract; and
  - (5) the Firm's compliance monitoring of telephone sales of PPI was not sufficiently effective.
- 2.4. These matters are viewed as serious by the FSA. In particular, the Firm's failure to provide more than 50,000 customers with a policy document (rather than just a policy summary which was provided in all cases) meant that affected customers did not have the opportunity to consider all aspects of the PPI policy, and whether it may have met their demands and needs, prior to purchase.

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<sup>1</sup> The FSA has regulated insurance mediation only since 14 January 2005.

2.5. There are several factors which the FSA has taken into account in mitigation. Most notably, Capital One proactively, and without prompting by the FSA, has engaged in a substantial remediation programme to ensure that all customers who did not receive a policy document, including those who purchased PPI prior to the commencement of FSA regulation, have the opportunity to be recompensed. The cost of this programme, including potential premium refunds, has been estimated to be in the region of £1.1 million in relation to sales made after FSA regulation and £1.9 million before FSA regulation was introduced. In addition, Capital One has:

- (1) agreed to review all declined claims relating to policies purchased since January 2005 and reconsider the claims in light of information provided or not provided to the customer at the time of sale;
- (2) agreed to establish a specialist complaints handling team to deal with any complaints from its customers in relation to PPI;
- (3) agreed to communicate to all customers acquired through the telephone channel during the period where scripted disclosure of policy features and benefits was not adequate to encourage customers to read the full terms and conditions of the PPI policy to ensure that the policy meets their demands and needs;
- (4) on its own initiative, implemented its own PPI Improvement Process and commissioned external consultants to review its PPI activities; and
- (5) has co-operated with the FSA's investigation, in some respects demonstrating best practice.

2.6. Having taken into account all the relevant circumstances of the case, the FSA considers that a financial penalty of £250,000 is appropriate in this case. Capital One has qualified for a 30% reduction in the financial penalty by agreeing to settle the matter at an early stage in the case, reducing the financial penalty to £175,000.<sup>2</sup>

### **3. RELEVANT STATUTORY PROVISIONS**

3.1. Section 206 of FSMA states:

*"If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate."*

3.2. The FSA Principles, as set out in the FSA's Handbook of Rules and Guidance ('the FSA Handbook') represent a general statement of the fundamental obligations of firms under the regulatory system.

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<sup>2</sup> Chapter 13.7 of the Enforcement Manual ("ENF") contains guidance on discounts for early settlement.

3.3. Principle 3 provides:

*"A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems."*

3.4. Principle 6 provides:

*"A firm must pay due regard to the interests of its customers and treat them fairly."*

3.5. The FSA has also had regard to ICOB 4.2 and ICOB 5 which contain detailed rules about the information that firms selling general insurance must provide to customers.

3.6. The FSA's Rules and Principles constitute requirements imposed on authorised persons under FSMA.

#### **4. FACTS AND MATTERS RELIED ON**

##### ***Background***

4.1. Capital One is a public limited company that was incorporated in the United Kingdom on 17 November 1999. It is part of a group of companies, owned by Capital One Financial Corporation, which offers financial services to nearly 50 million account holders in the United States of America, Canada and the United Kingdom.

4.2. In the UK Capital One carries on business offering credit cards, loans, and savings accounts with its operations centre in Nottingham, East Midlands. It also acts as an insurance intermediary, selling PPI to its credit card and loan customers.

4.3. Capital One sells PPI to its credit card customers through a number of sales channels:

- (1) during telephone calls from customers during both the credit card application and activation processes;
- (2) during telephone calls to customers (up to September 2005 only); and
- (3) during the credit card application process to customers who apply over the internet, or in response to direct mail or press insert marketing.

4.4. Capital One has been selling insurance in relation to its credit cards for a number of years. It employs approximately 250 full-time sales associates to sell PPI over the telephone and has over 1.3 million PPI customers. In 2005, following the commencement of FSA regulation, Capital One sold approximately 335,000 UK card PPI policies.

- 4.5. Capital One has been regulated by the FSA since 1 December 2001, but in relation to its insurance mediation activities, only since 14 January 2005.<sup>3</sup> It is an authorised person under FSMA with permissions to carry out a range of regulated activities.
- 4.6. The penalty imposed by the FSA relates only to the sale of PPI to its credit card customers, which is only one part of Capital One's regulated business.
- 4.7. FSA supervision visited the Firm on 28 July 2005, as part of a thematic project into the sale of PPI with credit arrangements. The Supervisors identified some concerns relating to Capital One's sale of PPI, which primarily focused on the risk that customers were not receiving sufficient information during the sales process.

#### ***Breaches of the FSA Principles***

- 4.8. As set out above, the FSA has imposed a financial penalty on Capital One in respect of breaches of the following FSA Principles in relation to the sale by the Firm of PPI:
  - (1) failing to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems (Principle 3); and
  - (2) failing to pay due regard to the interests of its customers and failing to treat them fairly (Principle 6).
- 4.9. Capital One breached Principles 3 and 6 by failing to have in place adequate systems and controls in relation to the sale of PPI to ensure that its customers were treated fairly. Each of the breaches set out below contravened both Principles 3 and 6, apart from the failure to adequately monitor compliance of the telephone sales channel, which was only in breach of Principle 3.

#### ***Failure to provide the policy document to customers***

- 4.10. In the period from 14 January 2005 until 5 April 2006 Capital One failed to provide the policy document to 50,428 customers who had purchased PPI. This arose as a result of a defect in the Firm's automated system which meant that PPI customers who opted not to receive marketing mailshots from the Firm also did not receive their PPI policy document.
- 4.11. Customers were provided with the policy summary, including price, key benefits and significant exclusions; however the policy document contains the full terms and conditions of the PPI policy and would have provided information to these customers which was not included in any other document. All of the Firm's PPI sales are made on a non-advised basis, which means that the Firm does not make a personal recommendation to each customer, but provides information to enable the customer to make an informed decision about whether the particular insurance is suitable for their needs. It is also important when customers come to make a claim. The FSA

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<sup>3</sup> The FSA has regulated insurance mediation only since 14 January 2005.

acknowledges that the policy summary is a key document in the sale of PPI and that Capital One provided this to customers before the conclusion of a contract. However, the provision of full policy information is important as PPI is a complex product which consumers need to fully understand in order to make the decision that it is suitable for their needs. As a result of the Firm's failure to provide a policy document, affected customers were not given full information to form a judgment as to whether the policy was suitable for their demands and needs. The FSA considers this to be a serious and significant failing.

*Failure to gain consent of telephone customers to receive limited information*

- 4.12. Firms must provide detailed information about the insurance product to customers prior to the conclusion of a non-investment insurance contract unless, in the case of telephone sales, firms obtain the explicit consent of customers to receive only limited information.
- 4.13. Capital One's sales associates had the option of using one of four scripted questions when seeking to obtain customers' explicit consent to proceed on the basis of limited information. Two of these questions fell short of obtaining the explicit consent required as it was not adequately clear that customers were being asked to consent to receiving less than full information. Consequently, in a significant number of cases sampled by the FSA, Capital One failed to obtain the explicit consent of customers purchasing PPI over the telephone to receive only limited information.

*Failure to provide adequate disclosure to customers in sales by telephone*

- 4.14. The form of disclosure used in scripts for customers who purchased PPI over the telephone did not always ensure adequate disclosure, in an acceptable number of cases, of:
  - (1) significant features and benefits of the policy; and
  - (2) significant and unusual exclusions and limitations of the policy.
- 4.15. The mandatory wording of the Firm's telephone sales script was not by itself adequate to ensure that customers were fully advised of all of the significant features and benefits of the policy during the telephone call. Sales associates were provided with guidance in presenting PPI to customers. However, in some cases some of the significant features and benefits of the policy were omitted or described in an incomplete or inaccurate manner. As a result, some customers purchased PPI without receiving adequate disclosure of the features and benefits of the policy.
- 4.16. In particular, the script, due to parts of it being guidance rather than mandatory wording, was not designed to ensure that, in an acceptable number of cases, customers received accurate information about:
  - (1) the benefit that would be paid to successful claimants (either 10% of the outstanding balance from the customer's last monthly statement paid each month for accident, sickness or redundancy/business failure claims, or the full outstanding balance owing on the customer's credit card account as at the date

of diagnosis for critical illness claims or as at the date of death for claims for the life benefit); and

- (2) the length of time for which the monthly benefit would be paid (until the customer returned to work, up to a maximum of 12 months).
- 4.17. The FSA considers these issues to be significant and serious as approximately 41% of the PPI policies sold by Capital One during the period January to November 2005 were sold through the telephone sales channel.
  - 4.18. Capital One also failed to ensure that it provided customers purchasing PPI over the telephone with adequate disclosure of all of the policy's significant and unusual exclusions and limitations although this information was provided in the policy summary.
  - 4.19. From 14 January 2005 to September 2005 only four significant and unusual exclusions or limitations were disclosed to customers before a sale was concluded over the telephone. This compares to ten such exclusions or limitations disclosed over the telephone from October 2005, and up to 21 disclosed in the policy summary from January 2005. While the four exclusions and limitations disclosed by Capital One between January 2005 and September 2005 were intended to capture the broad categories of exclusions, this disclosure still fell below the number of exclusions included in the policy summary.
  - 4.20. As a result of these failures, some Capital One customers may have purchased a PPI policy over the telephone without receiving adequate information to enable them to make an informed decision about whether the policy was appropriate for them.

*Failure to provide adequate disclosure in sales other than by telephone*

- 4.21. In a non-telephone sale, an insurance intermediary must generally provide the full policy terms and conditions to a customer prior to the conclusion of the contract. This does not apply only where the customer has requested that the sale is concluded by a means which does not enable the provision of the policy document in a durable medium before the conclusion of the contract.
- 4.22. Capital One sold PPI through the following non-telephone channels:
  - (1) internet;
  - (2) direct mail; and
  - (3) press inserts.
- 4.23. To the extent that these contracts were concluded by post, the FSA considers that the means of communication did enable the provision of the full policy terms and conditions in a durable medium prior to the conclusion of the contract. Capital One did not provide the full policy terms and conditions prior to the conclusion of the contract. The full policy document was provided immediately after the conclusion of the contract as part of the pack which included delivery of the credit card.

### *Failure to adequately monitor compliance of telephone sales channel*

- 4.24. In relation to the monitoring of its telephone sales channel, Capital One failed to control its affairs effectively and failed to maintain systems and controls appropriate to its business. While Capital One had systems and controls in place to ensure that call monitoring was carried out, the quality of call monitoring was inadequate.
- 4.25. Capital One provided the FSA with a sample of 100 PPI telephone sales occurring during June and July 2005 which had been reviewed by Capital One's Quality Assurance ('QA') function. A significant number of telephone calls passed as compliant by QA were found not to be compliant by the FSA's reviewers. The main area where the FSA found sales calls were non-compliant was in the presentation of the significant features and benefits of the PPI policy product, where the script was not itself adequate (as described in paragraphs 4.14 – 4.16 above). There were also a small number of sales to ineligible customers.

## **5. ANALYSIS OF PENALTY**

- 5.1. As a result of the above conduct, the FSA considers that Capital One breached Principle 3 and Principle 6 of the FSA Principles.
- 5.2. The FSA's policy in relation to the imposition of financial penalties is set out in Chapter 13 of the Enforcement Manual (ENF) which forms part of the FSA Handbook. The principal purpose of financial penalties is to promote high standards of regulatory conduct by deterring authorised and approved persons who have breached regulatory requirements from committing further contraventions, by helping to deter other firms from committing contraventions, and demonstrating generally to firms the benefits of compliant behaviour.
- 5.3. The severity of the penalty should reflect the degree of wrongdoing in each case and be proportionate to the breach in question. The following analysis of the appropriate level of penalty was undertaken before applying the 30% reduction in penalty for early settlement (ENF 13.7.3).
- 5.4. In determining whether a financial penalty is appropriate and its level, the FSA is required to consider all the relevant circumstances of the case (ENF 13.3.3).
- 5.5. The FSA has imposed a financial penalty of £250,000 on Capital One, in respect of the breaches of Principles 3 and 6 of the FSA Principles. In imposing this financial penalty the FSA has taken into account the following factors which it considers to be particularly relevant in this case.

### ***The seriousness of the misconduct or contravention***

- 5.6. The FSA has had regard to the seriousness of the contraventions, including the nature of the requirements breached. In assessing the seriousness of Capital One's conduct the FSA has also had regard to the nature of the insurance being sold and the potential impact on the affected consumers.
- 5.7. The FSA acknowledges that the potential consumer detriment for this type of insurance product is not as significant as with some other types of insurance. For

many consumers, PPI on a credit card will not be as significant a transaction as some other types of insurance such as motor vehicle, buildings and contents, personal injury insurance or single premium loan PPI.

- 5.8. In relation to the Firm's failure to provide the policy document to customers, the FSA acknowledges that in each case customers were provided with a policy summary, which mitigates the seriousness of this breach.
- 5.9. However, for the reasons set out below, the FSA considers that the breaches identified in this case are of a serious nature:
- (1) weakness in the systems and controls over the compliance of the telephone sales channel is particularly serious because, in the case of large firms such as Capital One, the failure to have adequate monitoring had the potential to expose a large number of customers to an unacceptable level of risk; and
  - (2) the disclosure failings identified above<sup>4</sup> arose from defects in Capital One's systems and controls. The omission of important information could have resulted in customers paying for insurance which did not meet their demands and needs or which may have been inappropriate for their circumstances, resulting in declined claims.

***The duration and frequency of the misconduct***

- 5.10. The breaches occurred over periods ranging from approximately eight months to more than fourteen months.

***The extent to which the misconduct was deliberate or reckless***

- 5.11. The FSA has not found any of the breaches to have resulted from deliberate or reckless conduct.

***The size, financial resources, and other circumstances of the Firm***

- 5.12. The FSA has taken into account Capital One's financial resources. It has no concerns about Capital One's ability to pay the penalty imposed.

***Conduct following the contravention***

- 5.13. Capital One has conducted its own PPI Improvement Process, which has resulted in a number of changes to its systems in relation to the sale of PPI. Following feedback from the FSA about shortcomings in its PPI sales process, Capital One also engaged an independent external consultant to review its PPI compliance arrangements and systems, provided the independent compliance report to the FSA and has adopted specific recommendations designed to remedy inadequacies.

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<sup>4</sup> See paragraphs 4.10 – 4.11 and 4.14 – 4.23 above.

- 5.14. In relation to the failure to provide the PPI policy document to customers who had opted not to receive marketing material from Capital One, it quickly established a team to identify the cause of the problem, resolve the problem and confirm any additional controls required in the PPI process.
- 5.15. In addition, on 19 May 2006 Capital One notified the FSA of the error and provided details of a remedial action plan which had been developed to ensure that all affected customers have the opportunity to be recompensed. Capital One has fully remediated the affected customers, to the satisfaction of the FSA. Capital One has estimated that the cost of premium refunds and retrospectively settled claims is likely to be in the region of £1.1 million in relation to sales made after FSA regulation and £1.9 million before FSA regulation was introduced. This remedial programme demonstrates a commitment by Capital One to treating its customers fairly.
- 5.16. Capital One commenced its PPI Improvement Process in 2005, which included a compliance-testing programme and the creation of a full-time PPI process owner responsible for end-to-end PPI fulfilment process. This represents industry best practice.
- 5.17. Capital One has also:
- (1) agreed to review all declined claims relating to policies purchased since January 2005 and reconsider the claims in light of information provided or not provided to the customer at the time of sale;
  - (2) agreed to establish a specialist complaints handling team to deal with any complaints (whether received in writing or otherwise) from its customers in relation to PPI and to report complaints data to the FSA on a monthly basis for six months;
  - (3) agreed to communicate to all customers acquired through the telephone channel during the period where scripted disclosure of policy features and benefits was not adequate (including those who purchased PPI prior to the commencement of FSA regulation), to encourage all customers to read an enclosed copy of the full terms and conditions of the PPI policy to ensure that the policy meets their demands and needs and contact Capital One to discuss any queries; and
  - (4) on its own initiative implemented its own PPI Improvement Process and commissioned external consultants to review its PPI activities.
- 5.18. Capital One has co-operated with the FSA's investigation, in some respects demonstrating best practice. During the investigation Capital One provided the FSA with a dedicated point of contact. Information requests were dealt with efficiently and thoroughly and the Firm was able clarify FSA queries quickly and effectively. In satisfying statutory information requests, Capital One provided full responses and often provided additional supporting material to further clarify its position and ensure that the FSA was provided with full and accurate information. Overall, Capital One's response to the investigation was a model for how firms should behave. This has been an important factor in determining the level of penalty.

- 5.19. The Firm has moved quickly to agree the facts of the case, ensuring efficient resolution of the matter. Without Capital One's commitment to redress, remedial action and early resolution of this matter the financial penalty would have been considerably higher.

***The disciplinary record and compliance history of the Firm***

- 5.20. Capital One has not previously been the subject of disciplinary action by the FSA.

***The previous action taken by the FSA in relation to similar findings***

- 5.21. The FSA seeks to ensure consistency when it determines the appropriate level of penalty. The FSA has in the past taken action against firms for similar failings and these have been taken into consideration in setting the level of the penalty against Capital One.

**6. DECISION MAKER**

- 6.1. The decision which gave rise to the obligation to give this Final Notice was made by the Executive Settlement Decision Makers on behalf of the FSA.

**7. IMPORTANT**

- 7.1. This Final Notice is given to the Firm in accordance with section 390 of FSMA.

**MANNER OF AND TIME FOR PAYMENT**

- 7.2. The financial penalty must be paid in full by Capital One to the FSA by no later than 1 March 2007, 14 days from the date of the Final Notice.

**IF THE FINANCIAL PENALTY IS NOT PAID**

- 7.3. If all or any of the financial penalty is outstanding on 2 March 2007, the FSA may recover the outstanding amount as a debt owed by the Firm and due to the FSA.

**PUBLICITY**

- 7.4. Sections 391(4), 391(6) and 391(7) of FSMA apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to you or prejudicial to the interests of consumers.
- 7.5. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

## **FSA CONTACTS**

- 7.6. For more information concerning this matter generally, you should contact Bill Sillett at the FSA (direct line: 020 7066 5880/fax: 020 7066 5881).

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**William Amos**  
**Head of Department**  
**FSA Enforcement Division**