

ENDSLEIGH INSURANCE

RESPONSE TO COMPETITION COMMISSION ANNOTATED ISSUES STATEMENT, WORKING PAPERS AND HEARING TRANSCRIPTS

1. INTRODUCTION

1.1 Endsleigh welcomes the opportunity to comment on the evidence and conclusions set out in the Annotated Issues Statement, Working Papers and hearing transcript.

1.2 We propose to confine our comments to the issue that Endsleigh considers to be of the greatest significance: the competitive impact of PCWs, their practices and their contractual terms.

2. THE MARKET POWER ENJOYED BY THE FOUR MAJOR PCWs

2.1 The CC concludes in its WP that the four major PCWs “have some bargaining power against PMI providers”. This significantly understates the extent of their market power.

2.2 First, the four major PCWs are each individually a “must have” partner for the very many providers of PMI (including both underwriters and brokers). There is no comparable route to market for new business.

2.3 This can most clearly be seen in their share of new business, which we set out in respect of Endsleigh in the table below:

Year	Share of new business
2011	79%
2012	84%

2.4 We agree with the comments from AXA (a very large insurer) set out in the Working Paper: “providing quotes through the four large PCWs at least is a ‘must have’ in order to achieve sufficient market coverage”¹.

2.5 Furthermore, even if a PMI provider were to take the substantial risk of delisting on a single PCW (hoping that it could attract the ‘lost’ consumers elsewhere), this would reduce bargaining power vis-à-vis the three other major PCWs still further: they would be aware that delisting from a second PCW would do such damage to the PMI provider’s business that it would not be commercially realistic.

¹ Paragraph 72 of the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

2.6 Second, the CC underestimates the negotiation strength of the four major PCWs². The fact that it is in practice commercially impossible to delist from a major PCW means that they have an enormously strong negotiating position – even with the largest PMI providers, but most especially with small and medium-sized providers. We have noted the comments made by BGL at the brokers’ hearing where they alleged that a PMI provider who suggested that MFN clauses were the subject of “individual negotiation”³: this is highly disingenuous, and out of line with the observations of other brokers at that meeting. In practice, it is impossible for PMI providers to resist their demands for wide MFN clauses: PCWs are able to adopt a “take it or leave it” position.

2.7 This “take it or leave it” approach is commonplace. [✂].

2.8 Third, the profitability of PCWs is also a strong indicator of their market power. The levels of profitability they have achieved have been in spite of enormous advertising expenditure (due to the fact that competition is taking place on the wrong dimensions as we explain below). These levels have also been achieved at a time when the rest of the value chain has been under severe pressure from a profitability point of view. We note the CC’s conclusion that their levels of profitability “could be consistent with [] PCWs having some bargaining power against PMI providers”⁴ and we urge the CC to do further work in this respect.

2.9 Fourth, the CC’s analysis of their pricing fails to measure their ability to raise prices against the appropriate metric. It may be correct that CPA figures have risen only by a limited amount by comparison with inflation⁵. However, that masks the fact that they have grown enormously as a proportion of total costs in the insurance value chain. Since 2008, Endsleigh’s customer acquisition costs have risen as a share of its total costs from 38% to 55% in 2011 and 54% in 2012. This rise is attributable to PCW CPA fees. At a time when other parts of this chain are being squeezed by competition, PCWs have been immune from this.

2.10 Indeed, the fixed CPA costs imposed by PCWs have made it uneconomic to insure certain risks which have a low premium, which is a bad outcome for consumers – contrary to the suggestions of BGL at the brokers’ hearing that PCWs’ market strength did not have “any impact actually on the consumer”⁶; the implication being that the more diligent driver is being penalised.

2.11 Fifth, the CC is right to say that there is no meaningful competition from other PCWs outside the “Big Four” and no prospect of entry⁷. Indeed, the very fact that the

² Paragraph 11 of the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

³ Page 26 of the draft transcript.

⁴ Paragraph 9 of Appendix 2 to the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

⁵ Paragraph 14 of the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

⁶ Page 28 of the draft transcript.

⁷ Paragraph 15 of the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

likes of Google and Tesco have failed to make an impact in this market is the clearest sign of the collective market power of the four leading brands.

2.12 In conclusion, it is clear to Endsleigh that the “Big Four” PCWs possess individual and collective market power, the exercise of which is having an adverse effect on competition.

3. MFNs IN PCW CONTRACTS

3.1 The MFN provisions in PCW contracts are anticompetitive and cannot be justified. This is true of any formulation of which we (and the CC) are aware – including all of the “own website MFN”, “online sales MFN” and “all sales MFN” formulations identified by the CC⁸.

3.2 There are several reasons why they are anticompetitive:

- (a) First, they inhibit price reduction, as the CC correctly identifies⁹. This is as true of “narrow” MFNs as it is of “wider” MFNs. Endsleigh is currently unable to offer our student customers more competitive rates if they visit the Endsleigh website having seen our brand or campaign on their university campus. Students are unable to benefit from Endsleigh’s work representing them to insurers because all rates have to consider the PCW fee, and the cost incurred on cancelled or fraudulent business introduced by PCWs (and paid for by Endsleigh);
- (b) Second, they inhibit innovation¹⁰. Endsleigh has in fact actively encouraged PCWs to consider alternative models which reward and encourage the right behaviours in the value chain but none have been receptive to an alternative approach. They prevent the development of any more innovative pricing models. Most importantly, they mean that a PCW that invests in its systems (e.g. for fraud prevention), which should allow it to lower its rates, will gain no competitive advantage from doing so; and
- (c) Third, they add to barriers to entry¹¹. A PCW seeking to enter on a “low price” model has no ability to do so, since PMI providers are unable to enable it to quote a lower rate even if it charges a lower CPA fee. Moreover, given the prevalence of MFNs which prevent price competition, competition is nowadays taking place on advertising spend. This creates an enormous barrier to entry. We believe that it means that competition is taking place on the

⁸ Paragraph 8 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

⁹ Paragraph 28 and paragraph 50 *et seq* of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

¹⁰ Paragraph 67 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

¹¹ Paragraph 61 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

wrong metric: it is not to the benefit of consumers that competition should take place on this basis rather than price, quality or innovation.

3.3 PCWs have attempted to justify their MFNs, but none of the justifications hold good:

- (a) First, it is not correct that MFNs prevent free-riding either by other PCWs or by PMI providers, as appears to have been suggested to the CC¹²:
 - (i) There is no evidence that another PCW is able to free ride on the investments made by a PCW: we fail to see any mechanism by which it could do so. Even if a customer switches from PCW1 to PCW2 and makes his or her purchase on PCW2, that is unrelated to any investment made by PCW1;
 - (ii) There is no evidence that PMI providers are able to free ride on PCWs' investment. The number of customers who switch from a PCW to make their purchase direct from the PMI provider is very small. And they can be (and are) tracked via cookies. This is a much less restrictive means of addressing this issue than via an MFN clause; and
 - (iii) It is also fair to observe that PCWs also free ride on the investment of PMI providers in their brands and their systems; and
- (b) Second, there is no evidence that MFNs improve consumers' experience¹³. In particular, there is no evidence that they reduce search costs for consumers. Consumers are not aware of the existence of MFNs (and are unlikely, in practice, to take note of legal issues such as MFNs/price parity guarantees even if they were given better information by PCWs themselves). The CC's evidence shows that they consult multiple sites notwithstanding the existence of MFNs.

3.4 We note that some PCWs appear to have argued that PCWs are in a special position and that MFNs are "a core part of a PCW's proposition"¹⁴. This special pleading has no basis: there is no reason to consider that PCWs should not compete on the same basis as companies operating in other channels (e.g. brokers) who compete on the appropriate metrics of price, quality and innovation, to the benefit of customers, and who do not seek or obtain the protection of MFN clauses.

3.5 For these reasons, we believe that MFNs – in any formulation – are anticompetitive and cannot be justified. We believe that they breach Chapter 1 of the Competition Act 1998 and that the CC should act to ban them in this market.

¹² See paragraph 82 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

¹³ Paragraph 76 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*.

¹⁴ See paragraph 81 of the Working Paper, *Theory of harm 5: impact of MFN clauses in contracts between PCWs and PMI providers*. The same view was also expressed by BGL at the brokers' hearing: see page 32 of the draft transcript.

4. THE PLACE OF PCWS IN THE MARKET

4.1 The role of PCWs is widely misunderstood:

- (a) They are not “free” (as the CC suggests in one of its Working Papers¹⁵): in fact, their costs are a major, and increasing, component of the premiums paid by customers.
- (b) They are not independent. As the CC is aware:
 - (i) Comparethemarket is a subsidiary of BGL Group (which is a major insurance broker);
 - (ii) Confused.com is a subsidiary of Admiral (which is a major insurer); and
 - (iii) Gocompare is a subsidiary of esure (which is a major insurer).

Only Moneysupermarket.com can be said to be independent of PMI providers; and

- (c) They are not a “public service”; rather, they are mechanism to monetise consumer search for insurance products, and a very effective one at that.

4.2 In playing this role, they have succeeded in evading some of the responsibilities that have historically been undertaken by other channels for the sale of PMI: in particular, they have avoided any prospect of recourse where the business generated by them is fraudulent or otherwise not as presented. Most importantly for consumers there is no recourse should the product not be suitable for their needs i.e. not able to claim against.

4.3 PCWs have been enormously successful in the past several years, achieving enviable growth in the context of a market that has otherwise been under enormous financial pressure. We note the CC’s conclusion that the levels of profitability that they have achieved may indicate some degree of market power (and we address this further below).

4.4 Part of their success is attributable to their ability to “free ride” on the investment of brokers and underwriters in their brands and systems. We believe that brokers have and will continue to have an important role in this market, sourcing high quality business for underwriters, and ensuring that consumers choose the PMI provider which is best suited to their individual circumstances. We have adapted effectively to changes in the market – including the advent of PCWs – and we will continue to invest in our systems and in our brand. It is a matter of some frustration that PCWs continue to be able to “free ride” on those investments.

¹⁵ Paragraph 2 of the Working Paper, *Theory of harm 3: horizontal concentration in PCWs*.

5. CONCLUSION

5.1 Endsleigh believes that, notwithstanding the increased price competition that PCWs have created, their competitive impact, their practices and their contractual terms together give rise to an adverse effect on competition and hence to poorer outcomes for consumers. The four major PCWs have secured a market position, which they now seek to protect through contractual means and their commercial behaviour, that allows them to avoid innovation and generate profits above the competitive level, to the detriment of consumers.

5.2 We urge the CC to investigate more thoroughly their individual and collective market power – evident through their negotiation tactics, profitability and terms. We also urge the CC to ban MFN clauses in agreements with PCWs, given that they are demonstrably anticompetitive and generate no benefits for customers.