

Lloyds Banking Group Plc

PPI Remittal - Response to Provisional Decision

This paper comprises the response of Lloyds Banking Group ("LBG") to the Provisional Decision of the Competition Commission ("CC") following the remittal of the CC's proposed Point of Sale Prohibition remedy ("POSP") by the Competition Appeal Tribunal.

In this response, we refer to submissions and evidence which we have previously provided to the CC. Please note that, where we cross-refer to such submissions or evidence, those references are not to be taken as a waiver of confidentiality in the underlying submissions or evidence.

LBG persists in its submission that the CC has not made out a good case for adopting the POSP in respect of PLPPI, MPPI, SMPPI and CCPPI and continues to rely on the evidence and submissions provided to the CC during the CC's present investigation. LBG continues to take issue with the CC's assessment of evidence submitted by LBG. In particular, LBG persists in its submission that LBG's experiment to test the effects of the POSP strongly suggests that there is a real risk that the POSP will cause a large body of consumers not to buy PPI even though they would have benefited from doing so, and would have done so had the POSP not applied.

To the extent that this paper comments on issues relating to the implementation of the POSP, those comments should not be interpreted as implying that LBG accepts the CC's provisional decision that it should adopt the POSP or abandons its previous submissions and evidence.

1. Introduction and Overview

- 1.1 We are disappointed that the CC has provisionally concluded that it should require the introduction of the remedy package set out in the 2009 report, including the POSP, for PLPPI, MPPI, CCPPI and SMPPI.
- 1.2 We are concerned that the CC's decision rests on evidence which is fundamentally unreliable. Most notably, LBG submits that there are deficiencies in the research carried out by Accent into Consumer Attitudes to Payment Protection Insurance. To the extent that the CC relies on the outputs of the Accent research to inform its welfare modelling, that modelling is also necessarily flawed. But the welfare modelling also embodies additional errors arising independently of its reliance on the Accent research.
- 1.3 Whilst LBG acknowledges that its proposed "opt-in" annual renewal remedy does not wholly address the point-of-sale advantage, we remain of the view that the opt-in annual renewal would have the effect of substantially diminishing the point of sale advantage, whilst retaining many of the benefits to consumers of allowing the sale of PPI at the point of sale of the credit product. LBG considers that the opt-in annual renewal remedy, with

appropriate informational remedies, is most likely to create a sustainable and competitive market for the supply of PPI. The CC should therefore give this alternative remedy further consideration.

- 1.4 The remainder of this paper is structured as follows:-
- (i) We identify and discuss certain obvious deficiencies in the Accent research report in Appendix 1 to this paper. However, for the reasons set out in section 2 below, we are presently unable to provide a full critique of the Accent report, and we reserve the right to make fuller submissions on Accent's work, once we are in a position to do so.
 - (ii) We identify and discuss the key deficiencies in the CC's welfare modelling in Appendix 2 to this paper, which comprises a report produced by AlixPartners, economists instructed by LBG.
- 1.5 In light of these submissions, we would urge the CC to reconsider its provisional conclusions. We have however noted the CC's intention (if its provisional conclusions are confirmed) of proceeding quickly to adopt the package of remedies set out in the 2009 report. Accordingly, we also comment in this response on various issues relating to the implementation of the CC's proposed package of remedies (including the POSP) which we have identified in planning for implementation of the remedies, or in devising and conducting experiments to test the likely effect of the remedies. We consider that, unless these issues are addressed in the definition and implementation of the CC's remedies, the remedies will be unfair, unworkable and ineffective. The resulting regulatory uncertainty may well deter firms from participating in the market. It is therefore important that these issues should be addressed by the CC at this stage in its proceedings.

2. Accent research

- 2.1 LBG has reviewed the Accent research report published on the CC's website, and has requested further data from the CC to assist it and its advisers in reviewing and checking the results and conclusions recorded in the report.
- 2.2 The CC has refused to provide all the additional data requested by LBG, relying (among other matters) on its established policy of refusing to provide the data underlying such surveys. The CC has referred, in particular, to concerns as to the potential disclosure of information about individual respondents who might be identifiable from the data and as to whether such disclosure would be compliant with the CC's duties under the Enterprise Act and Data Protection Act.
- 2.3 LBG has given further consideration to these matters. It continues to believe that, unless it has access to the underlying data, it will be unable to conduct a sufficient critique of the Accent research report. We have outlined in Appendix 1 why further data is needed, and the way in which LBG and its advisers would wish to use it.

- 2.4 We would point out that, since the CC places substantial reliance on the results and conclusions contained in the Accent research report, and since the conclusions provide key inputs into the CC's welfare modelling, it is clear that the CC's overall provisional conclusions are heavily dependent on Accent's work. It is therefore important that LBG should be given a fair and reasonable opportunity fully to review Accent's work.
- 2.5 We do not consider that the CC has provided any good reason for withholding the data which LBG has requested. Indeed, we consider that, if the CC wishes to rely on the Accent report (as it does in its provisional decision), then it is obliged to allow LBG and its advisers access to the underlying data:
- As the Court of Appeal recognised in R (on the application of Eisai Limited) v. National Institute for Health and Clinical Excellence [2008] EWCA Civ 438, an interested private party is entitled to have access to all the data it needs in order to review any modelling or other work on which a public body bases its decision. The public body is not generally entitled to withhold relevant materials on grounds of confidentiality, since the public interest in ensuring a fair procedure will, if necessary, justify the disclosure of confidential information.
 - Indeed, the CC's statutory duties under sections 237 ff. of the 2002 Act expressly contemplate that the CC may disclose confidential information for the purpose of facilitating the exercise of its functions.
 - LBG considers that it should be possible for the CC to provide the data in such a way as to avoid disclosing the identity of individual respondents, and LBG would be happy to discuss with the CC how this could best be done.
- 2.6 Accordingly, LBG now formally requests that the CC provides to it and its advisers the data underlying the Accent research report, and then allows LBG a fair and reasonable opportunity to analyse such data and comment more fully on the Accent research report. We have described in Appendix 1 the information which is required, and how it may be presented so as to avoid disclosure of the identities of individual respondents.
- 2.7 LBG will be happy to discuss further with the CC the precise format in which such data should be provided, so as to avoid the unnecessary disclosure of individual respondents' identities.

3. Implementation of remedies

- 3.1 Since the CC intends to proceed quickly to adopt the package of remedies set out in its 2009 report, we comment below on a number of key issues relating to the definition and implementation of the proposed remedies. If the POSP is to be adopted, LBG will be unable to evaluate future market opportunities and to decide to what extent it will wish to participate in PPI markets in the future until the difficulties and uncertainties arising from the CC's present draft Order are resolved.

- 3.2 These comments are made without prejudice to the fuller comments made in response to the CC's consultation on its draft Order in August 2009. We reserve the right to make further submissions in relation to these matters if the CC formally decides to proceed with these remedies.

Definitions of Credit Sale and Prohibition Period and related provisions

- 3.3 It is clear that, if the POSP is to work fairly and effectively, there must be complete clarity as to definition of the period during which Credit Arrangers and their Associates are prohibited from selling PPI.

- 3.4 It appears that the CC's intention is (in simple terms) that:

- The prohibition period should run for a period of 7 days from when the credit sale is completed;
- During that period, the only circumstance in which the credit arranger or its associates may complete the sale of a PPI policy to a credit customer is where the customer takes the initiative to contact the seller to complete the transaction and where such contact is made at least 24 hours after completion of the credit sale.

- 3.5 The CC appears to have chosen the periods of 7 days and 24 hours with the intention of striking what it judges to be the best balance between creating a sufficient period for the customer to reflect and shop around, and minimising the loss of convenience which might arise if the PPI sale/purchase were postponed for too long.

- 3.6 LBG submits that the CC's draft Order fails to give effect to its intentions in several important respects, because:

- In many common selling situations, it will be unclear, by reference to the wording of the draft Order, when the "Credit Sale" ends. In consequence, it will be unclear when the "Prohibition Period" will end, since the Prohibition Period is defined as running from the end of the Credit Sale. Likewise, it will be unclear when the relevant period of 24 hours ends, since the 24 hour period is also expressed to run from the end of the Credit Sale;
- In circumstances where a credit agreement is concluded on terms which provide for the availability of credit to be conditional on the fulfilment of various conditions precedent, the Prohibition Period will not start to run until the Credit Arranger has informed the customer that the credit has become unconditionally available. This could be some time after the signature of the credit agreement (or the making of a mortgage offer), and would appear to defer the possibility of the Credit Arranger's selling PPI for far too long.

- 3.7 The CC's draft Order also contains anti-avoidance provisions, to prevent Credit Arrangers from selling PPI before a relevant credit sale, in a way which might circumvent the proposed POSP. The anti-avoidance provisions require Credit Arrangers to identify when a customer is likely to apply for credit, such as to lead to a possible credit sale.
- 3.8 However, LBG submits that the CC's attempt to define when a credit sale is sufficiently likely/imminent to trigger the application of the additional prohibition is unworkable.

Provisions dealing with stand alone sales of PPI

- 3.9 The CC's draft order apparently envisages that a Credit Arranger or its Associate may provide the customer with a personal PPI quote either during the credit sale process or at some later stage. In the latter case, a question arises as to whether the offer of PPI has sufficient nexus at all with the prior credit sale to justify its being subject to the Prohibition Period at all. The CC has apparently decided that the Credit Arranger's offer of PPI should be subject to the Prohibition Period if the offer or sale occurs within 6 months after the credit sale.
- 3.10 LBG submits that this is too long a period, and will place undue burdens on Credit Arrangers and their Associates. The CC's proposed approach is particularly onerous insofar as it applies to short term income protection products.

Wide application of Articles 8 and 9

- 3.11 The provisions of Article 9 of the draft Order implementing the POSP appear to prohibit a Credit Arranger from selling to a consumer any form of PPI during a relevant Prohibition Period. A relevant Prohibition Period will be triggered by a Credit Sale by the Credit Arranger in favour of the consumer of any relevant credit product. Thus, it is possible to envisage a situation where a consumer buys a credit card product from the Credit Arranger in month 1, and then applies to the Credit Arranger to buy CCPPI in month 7. The Credit Arranger will be free to sell CCPPI to the consumer without observing the Prohibition Period, since there has been a sufficient lapse of time to render the Prohibition Period inapplicable. But if the same consumer had purchased a personal loan from the Credit Arranger in month 5, then the Credit Arranger would appear to be subject to the Prohibition Period in selling CCPPI, since Article 9 of the draft Order does not limit the application of the Prohibition Period to cases where the Credit Arranger is selling PPI relating to the more recent Credit Sale. In order to comply with Article 9, it would be necessary for an organisation such as LBG group to be able to track whether a consumer approaching, say, the credit card business unit to buy CCPPI had bought credit from, say, the personal loan business unit, before being able to proceed with the sale of PPI.
- 3.12 The same problem would arise in respect of Article 8: for example, adapting the illustration outlined in paragraph 3.10 above, it might well not be open to

the Credit Arranger to sell CCPPI to the consumer immediately on his application in month 7 if, towards the end of month 6, the consumer had been discussing with another business unit of the Credit Arranger the possibility of taking out a personal loan, and was planning to do so shortly.

3.13 *[Excised – business secrets]*

3.14 LBG therefore requests that the draft order should be amended so as to excuse a Credit Arranger from the application of Articles 8 and 9 where it offers to sell or sells PPI in circumstances where, having made reasonable enquiries of the consumer, it has no reasonable grounds to believe that the consumer had taken out, or discussed taking out, a credit product in circumstances which would otherwise trigger the application of the POSP provisions of the draft Order.

Other issues

3.15 We have also identified various other difficulties with the working of the POSP provisions of the draft Order, relating to the sale of PPI via a combination of different media (face to face, followed by internet/telephone) and to the making of amendments to consumer credit agreements.

3.16 We discuss all these issues, and our proposed solutions to them, in more detail in the following paragraphs.

Detailed discussion

Definitions of Credit Sale and Prohibition Period and related provisions

Definition of Credit Sale

3.17 The draft Order provides that Credit Sale "means the process commencing when a Consumer makes an application for Credit and concluding when the Consumer receives confirmation in a Durable Medium that the Credit Provider is bound unconditionally to provide the Credit." The Prohibition Period commences "at the conclusion of the Credit Sale".

3.18 The CC said, in its comments on LBG's proposed POSP test, and in relation to the telephony channel (CC's letter to LBG dated 30 December 2009) that it was "unclear to us (a) [...] (b) why the prohibition period is assumed to start with confirmation of receipt of the signed consumer credit agreement, rather than with the provision of the consumer credit agreement for the customer to sign." The CC implied that this approach extended the prohibition period unduly and could affect take-up rates in the POSP test.

3.19 We explained to the CC (in our letter dated 18 January 2010) that LBG plans to treat the Prohibition Period as starting when it has received the signed credit agreement from the customer and has confirmed to the customer in writing that the credit is now unconditionally available. This reflects the terms of the current draft Order, since LBG will not be in a position to know that the

customer has signed the agreement, so as to render it binding on both parties, until it receives the signed agreement from the customer.

- 3.20 Once LBG has received the signed consumer credit agreement, it will also have to provide the customer with the requisite confirmation (in a Durable Medium) that it is bound unconditionally to provide the credit, in order to satisfy the terms of the draft Order.
- 3.21 However, as the CC (rightly) implied in its comments on LBG's POSP test, where the Credit Sale does not take place in-branch, this will inevitably lead to some delay. In some cases, it could give rise to a considerable delay before the end of the prohibition period (resulting in detriment to consumers). This applies in relation to sales of both PLPPI and CCPPI (where the Credit Sale does not take place in-branch or, if the Credit Sale starts in-branch, it is not concluded immediately).

Credit to be unconditionally available

- 3.22 The definition of Credit Sale in the draft Order has the effect of imposing potentially even greater delay in relation to any possible sale of MPPI and SMPPI (regardless of the channel through which the sale is made). This is because the Credit Provider does not generally conclude a formal credit agreement until very late in the overall process, and becomes bound to provide credit only on fulfilment of the various conditions precedent to drawdown (e.g. receipt of a satisfactory report on title, valuation/survey etc.) Generally, the Credit Provider provides only a mortgage offer at the outset, with the formal credit agreement being signed much later.
- 3.23 As the CC's draft definition of Credit Sale presently stands, there could therefore be an extended delay between the date on which the mortgage offer is made (and the personal PPI quote provided) and the conclusion of the Credit Sale. LBG submits that this cannot have been the CC's intention (as this goes beyond what would be necessary to encourage consumers to shop around for MPPI).
- 3.24 LBG submits that the CC should amend the definition of Credit Sale, so that the credit sale will conclude when the Consumer receives confirmation in a Durable Medium that the Credit Provider is offering to provide the Credit, subject only to the fulfilment of such conditions or formalities as are specified by the Credit Provider, not being matters within the subjective discretion of the Credit Provider to fulfil. This would mean that the Credit Sale would potentially be completed when a relevant mortgage offer is provided to the consumer in a Durable Medium, and the Prohibition Period would start at that point.
- 3.25 However, there will be numerous cases where a mortgage offer is made subject to conditions within the discretion of the Credit Provider, and, in such cases, the POSP would continue to prevent the sale of PPI until a long time after the making of the mortgage offer. We would invite the CC to consider whether the draft Order should be further amended to allow the earlier sale of

PPI in such cases. If no amendment is made, there is a real risk that Credit Providers will not find it practically possible to offer MPPI at all.

Definition of Prohibition Period and 24 hour period

3.26 We previously proposed drafting changes to the draft Order with a view to bringing greater clarity to the definition of the Prohibition Period. Having now given further consideration to the changes that would be required to LBG's IT systems to implement and ensure compliance with the remedies, and the need for certainty as to how the Prohibition Period will operate more generally, we have identified a need for further clarification of the definition of "Prohibition Period" and/or Articles 7 to 9 of the draft Order.

3.27 We would ask the CC to consider (in particular) the following matters:

- (i) The draft Order does not currently make express provision as to the time of day at which the Credit Sale comes to an end, taking into account that the Credit Sale may end with the delivery of a relevant document to the Customer in person, or by e-mail, courier or normal post. (Article 7.4 makes only partial provision, dealing with electronic communication of personal PPI quotes.) This omission is particularly problematic in connection with the application of the "exception" provided for in Article 9.2 of the draft Order, which allows the sale of PPI products in cases where the Customer initiates the transaction (via the Internet or by telephone) when more than 24 hours have passed after the end of the Credit Sale;
- (ii) Where the full seven-day Prohibition Period applies, the Order does not currently make sufficient provision as to the time at which the Prohibition Period will end on the seventh consecutive day. LBG submits that, for ease of implementation, this should be 0.01 a.m. on the seventh day.

Anti-avoidance provisions

3.28 There have been significant changes in the regulation of credit business since the CC's consultation on the draft Order. In particular, the implementation of the Consumer Credit Directive and the OFT's Responsible Lending Guidance mean that banks and other credit providers are subject to additional duties designed to ensure that consumers understand the terms of any credit product they may consider.

3.29 As a result, LBG envisages that it will become more common for banks to initiate discussions with customers about their potential need for credit than has been the case hitherto, and this may well give rise to uncertainty as to whether, in a particular case, a Credit Arranger should be regarded as having "reasonable grounds to believe that the Consumer will make an application for Credit within seven days of the discussion", so as to be precluded from selling PPI to the Consumer under Article 8 of the draft Order.

- 3.30 We would therefore ask the CC to reconsider the terms of Article 8.2 before any Order is adopted, so as to redefine the circumstances in which a Credit Arranger is to be regarded as having reasonable grounds to believe that the Consumer will make an application for Credit. At present, Credit Arrangers are still considering what changes to their sales practices may be required to comply with the new rules and guidance, and it is premature to attempt, at this stage, to decide how best to define the circumstances in which a Credit Arranger should be precluded from selling PPI, because an application for Credit is imminent.

Provisions dealing with stand alone sales of PPI

- 3.31 We noted above that the draft Order presently proceeds on the assumption that there is a sufficient nexus between a Credit Sale and a subsequent offer of PPI, for the subsequent offer of PPI to be subject to the POSP if it is made within 6 months of the Credit Sale. Sales of short term income protection insurance are subjected to the same provisions.
- 3.32 LBG submits that this approach imposes unnecessary and disproportionate burdens on Credit Arrangers and PPI Providers. It will require them to keep accessible data on all sales of credit made within the last 6 months, to enable them to identify cases where a PPI offer (or an offer of short term income protection insurance) is to be made to a consumer who has bought a relevant credit product. It appears most unlikely that the consumer would, in his/her own mind, link the two events/sales even after a much shorter period. The period of 6 months appears to be particularly disproportionate in respect of short term income protection insurance, where the product is not, by its terms, linked to any particular credit product, and the consumer is particularly unlikely to regard the two as linked.
- 3.33 We would therefore suggest that the POSP should apply only to offers of PPI and/or short term income protection insurance made within one month of the end of a Credit Sale in favour of the relevant Consumer or, if earlier, when the Consumer makes its first payment of interest/principal under the credit agreement. The first payment is likely, in the consumer's mind, to signify that the credit agreement is "up and running", so that any subsequent offer of insurance would be regarded as a new and unrelated sale.

Wide application of Articles 8 and 9

- 3.34 We noted in paragraphs 3.10 to 3.13 above the difficulties which arise for LBG (and other multi-product Credit Arrangers) by virtue of its business model, whereby it offers multiple credit products, via different business units, [*excised – business secrets*] We would invite the CC to adopt the suggestions made in paragraph 3.13 above to address this concern. The concerns which we have identified under this heading are particularly acute, when taken together with the points raised in paragraphs 3.27 ff and 3.30 ff.

Other issues

Application of Prohibition Period – completing sales in branch

- 3.35 LBG's POSP test confirmed that many customers have a strong preference for transacting business in-branch (and may be unlikely or unwilling to buy PPI over the internet or by telephone).
- 3.36 With this in mind, we would ask the CC to reconsider the terms of the exception provided for in Article 9.2 of the draft Order, which allows consumers to buy PPI from the Credit Arranger or its Associate within the 7 day Prohibition Period only if the customer initiates the transaction by telephone or over the Internet. LBG suggests that the draft Order should be amended to make clear that the parties should be entitled to take advantage of this exception if the customer contacts the Credit Arranger or its Associate by telephone or Internet, and then makes an appointment or requests permission to return to the branch premises to complete the purchase of the PPI product.

Amendments to existing Credit Agreements

- 3.37 It has come to our attention that there may be many more circumstances which will potentially fall outside the provisions of Article 9.4 of the CC's draft Order, in which minor amendments are made to credit agreements, and which should not be deemed to trigger a new Credit Sale.
- 3.38 We would therefore ask the CC to consider amending or expanding this provision, so as to make it clear that a new Credit Sale does not occur when there is a variation to an existing Credit Agreement between a Credit Provider and a Consumer which does not affect the overall character of the Credit Agreement, including, without limitation, cases where the maximum amount of Credit that a Consumer may borrow is varied during the term of the Credit Agreement, where the interest rate is varied, where a Credit Card is replaced, where a Consumer requests or draws down Credit under a facility available under an existing Credit Agreement, or where corrections are made to errors in respect of matters such as the name or address of the customer, or details of any security to be offered in support of the credit.

**Lloyds Banking Group
4 June 2010.**

APPENDIX 1

APPENDIX 2