PPI REMITTAL

RESPONSE TO THE ACCENT REPORT ON BEHALF OF THE COMPETITION COMMISSION: "CONSUMER ATTITUDES TO PAYMENT PROTECTION INSURANCE"

A REPORT FOR LLOYDS BANKING GROUP

AlixPartners Ltd

9 JULY 2010

CONTENTS

1 ADDENDUM

1.1.1 Further to submission of this Report on 9 July 2010, the CC has confirmed (email from Matthew Weighill to Marc Biffin of LBG on 29 September 2010) that the information relating to questions 32 and 33 of the Accent report appeared in the data room in the reverse order to that presented in Appendix C of the Accent report.

1.1.2 In light of this we confirm that the analysis contained in columns 2 and 3 of Table 6 no longer applies. In view of this, the following adjustments to the text can also be made:

1.1.2.1 The second and third sentence in paragraph 1.1.15 can be withdrawn.

1.1.2.2 The following text can be withdrawn from the first sentence in paragraph 1.1.28: *"and that the results are also sensitive to the way in which this is accounted for"*.

1.1.2.3 Paragraph 3.3.6 can be withdrawn.

2 EXECUTIVE SUMMARY

2.1.1 This report sets out our response to the Accent report "Consumer Attitudes to Payment Protection Insurance." Our work is based on limited access to the Accent analysis and underlying data through the data room process.

2.1.2 The Accent research has concluded that although the majority of respondents favour no delay in the PPI purchase process, a "vocal minority" favour delay to such an extent that the valuation they place on delay more than outweighs the negative valuation placed on delay by the majority.

2.1.3 These results have been relied upon by the CC, to the exclusion of all other potentially relevant research, to support its treatment of loss of convenience in its welfare calculations of the impact of the remedy. This implies that the CC considers the Accent research to have a very high degree of robustness. Based on our work to date we consider the faith that the CC places on this research to be severely misguided for the reasons set out below.

Our approach

2.1.4 In the time available we have focused our analysis on a number of discrete areas. We believe that the access we have had to Accent's work and underlying data was, for reasons already shared with the CC, unreasonably restricted. Given more time we would like to carry out additional analysis to pursue further the lines of inquiry we have developed, and to explore additional lines of inquiry we have not had time or the data to progress. Accordingly, in our report we set out any material limitations of the analysis we have carried out to date and identify the further work that could be done.

2.1.5 Our approach was to first replicate the Accent results using the same software (ALOGIT) that Accent used (this was a highly involved process). We then focused our analysis on the following four issues:

(a) *Biased choices* - we reviewed in detail the choices respondents were presented with and analysed these for potential sources of bias.

(b) *Incoherence/Inconsistency* - we examined in detail the responses individuals gave to different questions and examined these for consistency and coherence. This involved carrying out a substantial amount of analysis not presented or touched on in the Accent report.

(c) *Representativeness of the sample* - we examined in detail the representativeness of the sample that Accent used to the underlying population.

(d) *Rationale for preferences* - we reviewed Accent's analysis of responses to individual questions relating to the rationale for the preference of delay, and assess the implications for the welfare modelling.

2.1.6 To support our analysis we have consulted with Lloyds Banking Group (LBG) in relation to the accuracy of data and assumptions used by Accent. In particular,

(a) For our analysis of representativeness of the sample we have relied on a population of all LTSB PLPPI consumers provided by LBG (as the CC declined to respond to our request for summary statistics of the database from which the Accent sample was drawn).

(b) For our analysis of bias LBG advised us in relation to market prices for different package options.

2.1.7 In view of the very limited time allowed to carry out all of this analysis and produce a written report to meet the CC's deadline of July 9th, we reserve the right to amend and supplement this report.

Our Findings

2.1.8 Based on this approach our findings at this stage are as follows.

Biased choices

2.1.9 Despite the strong impression given in the Accent report that respondents were presented with randomly selected choices across the "full spectrum" of combinations, we found that in fact the choice sets were severely restricted. Out of a possible 6480 choice options available only 30 were used and 99% of options came from just 18 choice sets.

2.1.10 In light of this, we examined whether there is material bias in favour of delay options. This involved an assessment of the relative value for money of different product combinations.

2.1.11 Based on this assessment, we found that 4 of the 18 choice sets very strongly favour delay (defined as offering a superior product for the same or better price) compared to 2 that very strongly favour no-delay. We also found that 2 of the 18 choice sets strongly favour delay

(defined as offering ASU plus Life and CI instead of unemployment-only with only a minor disadvantage in terms of duration of cover or price) compared to 1 that strongly favours no-delay.

2.1.12 We also find that the Accent results are sensitive to evening up the apparent bias in the choice sets offered. For example,

(a) Evening up the choice sets that very strongly favour delay or no-delay reduces the size of the coefficient (and associated willingness to pay for delay) by up to 24%.

(b) Extending this to also remove choice sets that strongly favour either delay or no delay results in all delay coefficients becoming insignificant.

2.1.13 We believe that this raises significant concerns regarding the robustness of the Accent results. In our view, further work on the issue of choice bias should be carried out. Ideally, this would include constructing a precise value for money metric for each package respondents are offered. We note the CC would be best placed to do this using data from all market participants.

Incoherence/Inconsistency

2.1.14 We carried out two pieces of analysis to assess the coherence of responses given by respondents and we have assessed the robustness of Accent's results to the removal of certain incoherent responses.

2.1.15 First, we tested whether Accent's results are sensitive to the removal of respondents using the interviewer's own estimation of the degree to which respondents understood, considered sufficiently, or held concentration during the interview process. Our analysis shows that Accent's results are sensitive to these exclusions. In particular, the removal of individuals who were thought to have given little or no consideration to their choices makes the coefficients on delay statistically insignificant.

2.1.16 Secondly, building on our analysis of bias in choice sets we identified instances where respondents categorised as favouring delay actually responded to questions that strongly favour delay by inconsistently choosing the no-delay option. We considered that this was the best evidence of inconsistent or random answers given by respondents. We found a sizeable minority (between 6% and 25% depending on the choice set) of respondents fell

into this category. This raises further doubts regarding the coherence of the responses and the robustness of the Accent findings.

Representativeness of the sample

2.1.17 We analysed the extent to which Accent's sample of 800 respondents is properly representative of consumers who buy PPI. To do this we first tested whether the Accent results varied significantly by population characteristics in terms of age, income and sales channel. We did not have time or the information to check for representativeness of other potentially relevant parameters such as credit score. We found significant variation in valuations of delay according to age, income and sales channel.

2.1.18 To test representativeness of the sample, we carried out a comparison with data provided by LBG on 595,000 LTSB PLPPI customers. Our comments are subject to the caveat that this sample may vary from the total population but we would expect it to be much closer than the Accent sample of 800. The CC has declined our request to compare to the CC's database comprising data from all parties and we note that the CC may be best placed to refine this analysis using data from all parties.

2.1.19 We found that Accent's sample varies significantly from the LTSB population by having a much higher proportion of customers who purchased over the telephone. This biases the result substantially because telephony customers place a far higher valuation on delay than other customers. To illustrate we recalculated Accent's results using population weights from the LTSB database. This produced results that showed the coefficients on delay were statistically insignificant.

Rationale for preferences

2.1.20 We reviewed Accent's analysis of qualitative responses to questions exploring the reasons why certain respondents expressed a preference for delay. Analysis of these responses is subjective, and we came up with a different but similar categorisation of responses. Our analysis suggests that respondents fall roughly evenly into two groups. The first group essentially see delay as offering "time to reflect". The second group essentially see delay as offering an "opportunity to shop around" and search for a better product. The latter group accounted for 50% of MPPI and 42% of PLPPI respondents.

2.1.21 In our view this demonstrates that for almost half of the respondents the CC's use of the Accent results involves double counting with the additional welfare gains of price cuts. We

believe this also supports the view that for those seeking "time to reflect" the welfare implications should, so far as relevant, be modelled in the manner set out in paragraphs 2.3.19 - 2.3.24 of our June 4th report.

2.1.22 We have revisited our welfare modelling set out in that report and using the above splits recalculated welfare estimates. The results are shown below:

Table 1: Revised welfare estimates

£ millions	Original Scenario	Revised Scenario
CC Base Case	**170**	**33**
High	11	-88
Medium	-255	-312
Low	-475	-527

2.1.23 We note that these estimates take at face value the positive valuations put on delay by those respondents that expressed a preference for delay. However, we also believe this is an overestimate as it is likely to reflect a significant degree of "buyer's remorse".

2.1.24 It is unfortunate that Accent did not explore why the majority of respondents had a preference for no-delay. We consider that the negative valuations placed on delay are an underestimate because they derive from respondents that have already benefitted from the availability of PPI at the POS. As a result, these valuations are likely to exclude the welfare loss associated with customers being deprived of the opportunity to understand properly their needs, such that they do not purchase a product from which they would otherwise have benefitted.

2.1.25 Finally, we note that Accent's report derives very high valuations by consumers for the inclusion of Life and Critical Illness. We understand that in a secondary market providers are unlikely to offer this cover to the same extent as has been the case with an integrated sales process and the CC should take this further potential downside into account in its welfare modelling.

Our Conclusions

2.1.26 In view of these findings, and subject to the caveats set out in our report, our conclusions at this stage are as follows:

2.1.27 First, we believe the design of the stated preference survey suffers from fundamental bias in that delay options appear to have been significantly favoured by the inclusion of more attractive product combinations. Whilst the precise degree of bias can be quantified more accurately our initial analysis shows that Accent's results are sensitive to this.

2.1.28 Second, we conclude that respondents' answers in the Accent survey demonstrate a significant degree of incoherence and inconsistency and that the results are also sensitive to the way in which this is accounted for. In our view Accent has not done enough to analyse properly this issue or to address it in its presentation of estimates.

2.1.29 Third, we believe that Accent's sample is likely to be substantially unrepresentative of the population in areas that have a material influence on consumers' valuation of delay. As a result we believe that Accent's sample is biased and that the Accent results are likely to substantially overstate the overall valuation of delay by consumers.

2.1.30 Fourth, we believe that the Accent survey provides important but incomplete insights into the rationale for valuing delay that support our view that the way the Accent results are incorporated into the CC's welfare modelling is flawed and substantially overstates the positive impact on welfare of delay.

2.1.31 In view of this we conclude that the CC should revisit its decision to rely entirely on the Accent results, to the exclusion of other potentially relevant evidence, for the purposes of quantifying the impact on convenience in the welfare modelling. If the CC is going to rely in part on the Accent results a substantial amount of additional investigation into the precise robustness of the results is clearly merited in light of the above points.

3 SUMMARY OF ACCENT METHOD AND RESULTS

3.1 BACKGROUND

3.1.1 In April 2010, Accent (a market research firm) published its report "Consumer Attitudes to Payment Protection Insurance (PPI)." This report was commissioned by the CC with the goal of, *"understanding all the advantages and disadvantages to the consumer of separating the purchase of PPI from the purchase of the loan it is taken out to insure."*[1] Moreover, the CC was interested in focusing on the issue of loss of convenience stemming from the implementation of the POSP.

3.1.2 Accent undertook this study using an approach that combined both qualitative and quantitative methodologies. For the qualitative study, Accent conducted five focus group sessions across Glasgow, Manchester, and London as well as six face-to-face interviews that took place in Leeds. For the quantitative study, Accent created a pilot study of 50 interviews, consisting of 26 mortgages customers and 24 loans customers. This pilot study sought to calibrate and assess several factors, including the clarity of the questionnaire, the design of the stated preference study, and the survey hit rate. After the pilot study, Accent adjusted several factors in its study design and wording, and increased the range of costs used in the stated preference study.

3.1.3 After the pilot study, Accent began its main stage research and conducted 806 phone-post/email-phone interviews with people who had purchased PPI within the last year. Accent obtained contact details from a national database supplied by PPI providers at the request of the CC and respondents *"were randomly selected for interview from this database."*[2] The respondents in this round completed a stated preference survey and a follow up interview.

3.1.4 The stated preference (SP) survey is central to Accent's analysis. Accent reports their method as a randomised statistical design in the following manner:

> *"[The] [s]tated preference survey allows respondents to express preferences between a range of alternatives so that it is possible to determine what is important to them in a very robust way. Respondents are offered different pairs of hypothetical options and asked to indicate which option they prefer from each pair… [T]he options presented to*

[1] "Consumer Attitudes to Payment Protection Insurance," by Accent, April 2010, p. 4.
[2] Accent report, p. 8.

respondents are randomised across a statistical design; this allows the full spectrum of options to be presented across the sample population."[3]

3.1.5 Accent designed its stated preference study across four different attributes. The table below summarises the options tested within across each product attribute:

Table 2: Product Attributes in Accent Study

	Option 1	Option 2	Option 3
Time of purchase	Immediately at point of sale without a delay	A delay of purchasing of 24 hours	A delay of purchasing of 7 days
Product type	Unemployment	Unemployment, accident and sickness	Unemployment, accident and sickness and life/critical illness
Duration of cover	Up to 6 months	Up to 12 months	Up to 24 months
Price	Greater than current premium by 15%/20%/25% (20% on average)	Same as current premium	Less than current premium by 15%/20%/25% (20% on average)

3.1.6 Respondents were presented with six choice sets, each comprising two options. For example, a respondent could be asked to choose between a product without a delay, only unemployment, 6 months of cover, and costing more than his/her current PPI premium versus a product available only after 24 hours of delay, including unemployment and accident and sickness, lasting up to 12 months, and costing the same as his/her current PPI premium.

3.2 THE RESULTS OF THE ACCENT STUDY

3.2.1 The results from the stated preference questions were analysed via an econometric model. The dependent variable is the choice the respondent made between choice 1 or choice 2.[4] The factors that determine the individual's choice are set out in table 2 above. The willingness to pay (WTP) is computed using the marginal utility from the change in delay, scope, or duration, calibrated from the marginal utility associated with a change in price.

3.2.2 The main findings of this study were the following:

(a) 60% of consumers have a negative valuation as a result of the delay imposed by the POSP equivalent to 23% of the cost of PLPPI policy (£7.30 on an average monthly premium of £32). These are referred to as Group 1 consumers.

[3] Ibid.
[4] Such a model is denoted a discrete choice in that it is estimated as a logit model, where the characteristics of the hypothetical PPI policies formed the independent variables for the model.

(b) 31% of consumers receive a positive benefit from the delay imposed by the POSP equivalent to 60% of the cost of the PLPPI policy. These are referred to as Group 2 consumers (£19 on an average monthly premium of £32).

(c) 8% of consumers are indifferent to the delay. These are referred to as Group 3 consumers.[5]

3.2.3 Accent interprets these valuations as willingness to pay (WTP) for delay or to avoid delay. For example, the 31% of respondents wishing to see a 7 day delay are willing to pay £25.20 per month for the feature,[6] whereas those who prefer to buy PPI at the credit point of sale would require compensation of £7.30 per month to make them indifferent to the remedy. The net figure for the 7 day extension is £3.70 per month.[7]

3.3 ADDITIONAL INFORMATION PROVIDED AND THE DATA ROOM

3.3.1 After the publication of the study, Accent and the CC provided AlixPartners with more details in response to a series of requests via email and phone calls.

3.3.2 In an email dated 27 May 2010, the CC provided information on the study itself. The CC disclosed that 12,489 people were contacted (i.e. someone in the household was spoken to), 1,813 people accepted taking part in the survey, 705 people dropped out of the survey after they had been recruited, and 806 people completed the survey. Consequently, out of over 12,000 contacted individuals, only 6.5% completed this survey.

3.3.3 More information was also provided from Accent via a phone call on 14 June 2010. The first call revealed that Accent had not undertaken any analysis of representativeness of the sample with the underlying population. The sample size of approximately 800 (a quota sample) was *"determined by the CC in conversations with Accent."*[8] Furthermore, there had been no comprehensive analysis of the representativeness of the sample with the 12,489 sample provided by the banks or the underlying population.

3.3.4 Subsequently, the CC agreed to provide access to the underlying Accent data via a data room with access granted for one week, between the hours of 9.00 and 17.00. The software

[5] Figure 16 of the Accent report. It is noted that these values do not sum to 100%.
[6] Page 42, table 11 of the Accent report.
[7] Table 9 of the Accent report.
[8] The estimation of the necessary sample size is usually undertaken after the results of the pilot sample are analysed. A required sample size is determined with reference to an appropriate margin of error for the variable(s) of interest, and from the required margin of error, a sample size can be computed. There is no mention in the Accent report of any analysis to determine that 800 was an appropriate sample size.

available was restricted to Microsoft applications, such as Excel, along with more specialized econometric software such as STATA. The software used by Accent for the estimation work contained in their report (ALOGIT) was not made available by the CC. In order to analyse and replicate Accent's work, we needed to purchase ALOGIT, a third party proprietary statistical program that is not as prominent in the market as traditional packages such as SAS or STATA.

3.3.5 On 24 June, Accent re-released its report as an updated and final version. This version included changes in the number of respondents for MPPI and PLPPI, modifications to survey classifications, and other changes.

3.3.6 From 28 June until 2 July 2010, AlixPartners and other bank advisors had access to the data room at the CC. This room contained individual response data that could not be disseminated due to data privacy concerns. AlixPartners attempted to replicate Accent's results in ALOGIT; however, there were technical difficulties in the set-up and running of the software.

3.3.7 A second conference call was organized on 29 June 2010 where Accent and the CC revealed further information about the design of the study. In this call, Accent stated that it had used a "D-optimal" design in establishing the stated preference choice sets offered to respondents. Hence the actual number of possible choices offered to respondents was not randomly selected across all possible sets of PPI product combinations, but in fact had been restricted to a specific set to increase the efficiency of results (i.e. lower standard errors) behind consumers choosing between alternative PPI characteristics.[9] Accent also disclosed that it had previously designed its stated preference study to include 8 different pair combinations, but trimmed this selection down to 6 after witnessing "fatigue issues" during the pilot study.

3.3.8 On Wednesday 30 June, the CC made available the underlying respondent data in an ALOGIT '.DAT' file format, enabling us to replicate the Accent results using the ALOGIT software.

3.3.9 Our approach was based on using the same model, estimated with the same software, in order to examine on a 'level playing field' how different sensitivity analyses affect the

[9] D-optimal design is a statistical technique that aims to achieve the lowest efficient number of choices in a survey design. The D in D-optimal stands for 'determinant' which is the part that computes the standard errors of the coefficients.

results. The results could then be judged on the basis of Accent's data, with differing exclusion restrictions, rather than suspecting that a different result was derived on the basis of different software.[10]

3.3.10 Hence this report is based on only 3 days work in the CC data room. There are a number of other possible avenues of inquiry that remain unexplored because of time limits imposed by the CC (as detailed above). The results set out below are therefore necessarily illustrative and are not intended as the end statement on the Accent report.

[10] We tried to replicate the results as presented by Accent in their report Technical Appendix (utility equation for loans only) using STATA but were unable to do so. The results were close, but not close enough to rule out differences in the operation of the software. A first order requirement of scientific inquiry is that results can be replicated, and once the parameters for replication are known, adjustments can be undertaken while holding the other known factors constant. Neither the CC, nor Accent, demonstrated that the results obtained with the ALOGIT software could be obtained in identical fashion with the STATA software. Simply providing STATA as the software for use did not guarantee that the results would be free from the possibility that a difference in results might be due to the algorithm contained in the statistical software.

4 OUR ANALYSIS OF THE ACCENT METHOD AND RESULTS

4.1 OVERVIEW

4.1.1 We examined the following four areas:

(a) *Biased choices* - we reviewed in detail the choices respondents were presented with and analysed these for potential sources of bias.

(b) *Coherence/consistency* - we examined in detail the responses individuals gave to different questions and examined these for consistency and coherence. This involved carrying out a substantial amount of analysis not presented or touched on in the Accent report.

(c) *Representativeness of the sample* - we examined in great detail the representativeness of the sample that Accent used to the underlying population.

(d) *Rationale for preferences* - we reviewed Accent's analysis of responses to individual questions relating to the rationale for the preference of delay, and assessed the implications for the welfare modelling.

4.2 BIASED CHOICES

4.2.1 To evaluate the preferences in the stated preference survey, a respondent needed to decide between two different choices, each containing different characteristics and prices for a PPI product. The respondent was shown a total of 12 cards, in 6 ordered pairs, and had to choose option 1 or option 2 across 6 rounds. Each option product pair had 4 different attributes with three different potential values for each attribute.

4.2.2 Given four product attributes and the three alternative values available for each attribute, there are 81 different combinations of product available. Between the two choice sets available (choice 1 or choice 2), there are 6480 possible combinations.[11]

4.2.3 If the choices offered to respondents by Accent had been truly randomised so as to allow *"the full spectrum of options to be presented across the sample population"* (as stated in the Accent report), the grid of choice sets for the stated preference would have cells with one or two observations, with some cells empty. The Accent study produced a sample data set of

[11] 6480 is derived from 81 product combinations for option 1 (3 alternative values for each of 4 attributes, or 3x3x3x3) multiplied by the 81combinations for option 2, less the 81 identical options.

4836 observations. With a possible 6480 cells from 81 different choice combinations for option 1 and option 2, some cells would be empty (there are more cells than observations), some cells would be populated with one observation, and by chance some cells might have more than one.

4.2.4 Table 3 below shows that in fact the full spectrum of options was not used. Instead only 30 choice sets are used, comprising six sets containing 278 observations, six sets containing 264 observations, six sets containing 253 observations, six sets containing 8 observations, and six sets containing 3 observations. Hence over 99% of choice sets offered come from 18 of the 6480 possible combinations. This resulted from Accent's "D-optimal" design discussed in paragraph 2.3.7.

Table 3: Number of responses per choice set[12]

	Option 2																												
Option 1	1122	1123	1132	1211	1232	1233	1313	1321	1333	2112	2113	2122	2131	2211	2213	2231	2321	2322	3112	3123	3132	3213	3231	3232	3313	3321	3323	3332
1112																		264						253				
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4.2.5 With such a limited choice of options offered to respondents, the composition of the choice sets becomes important to ensure that there is no bias in the way respondents are being asked to state their preference.

[12] The full spectrum would have 81 rows and 81 columns. Here we report only the rows or columns containing a choice set used by Accent.

4.2.6 In particular we understand that the range of product scope alternatives is likely to dominate the value for money associated with different options. Specifically, an accident/sickness/unemployment plus life and critical illness (ASU+CI) package could cost between 100% and 200% more than an unemployment-only product. In comparison, variations in duration of cover have a much smaller impact on value for money, similar to the variation in prices of ±15% - 25% Accent employed for the cost metric. There is a general concern regarding whether such dramatic variations in product would dominate and potentially "over-mask" the respondent's attitudes to delay.[13] However, of critical importance is to assess whether in addition there is a fundamental bias in the choices offered.

4.2.7 To explore this, we have divided up the 18 choice sets (that account for 99% of the observations) into the following categories:

(a) *Category 1*: Those that very strongly favour delay or no-delay as they involve a clearly superior product for the same or more attractive price.

(b) *Category 2*: Those that strongly favour delay or no-delay as they involve a much better product (i.e. ASU plus Life and CI instead of unemployment only) with only a modest reduction in duration or increase in price.

(c) *Category 3*: Those where the mix is ambiguous or there is no trade-off in terms of delay.

4.2.8 Category 1 choice sets[14] are the following:

(C) 3211 vs. 1233: No-delay (option 2) has longer duration and 33% lower price. **Very strongly favours no-delay**.

(I) 1333 vs. 2211: No-delay (option 1) has better product, much better duration and a 33% lower price. **Very strongly favours no-delay.**

[13] This issue of over-masking was discussed in the hearing (See hearing transcript of 15 June 2010, pp 10-13).
[14] Each choice set is denoted with a unique letter. The numbers relate to the three different options for the four product attributes as follows. 1111 is a product with no delay, unemployment coverage only, up to 6 months of coverage, at a price more expensive than a respondent's current PPI premium. 2222 is a product with 24 hour delay; unemployment, accident and sickness coverage; up to 12 months of coverage; at a price equal to a respondent's current premium. 3333 is a product with 7 days of delay; unemployment, accident, sickness, life and critical illness coverage; up to 24 months of coverage; at a price less than the respondent's current premium.

(L) 1112 vs. 2322: Delay (option 2) has much better product and better duration for the same price. **Very strongly favours delay.**

(J) 3233 vs. 2211: 7 day delay (option 1) has same product with much better duration and a 33% lower price. **Very strongly favours further delay.**

(P) 1112 vs. 3232: Delay (option 2) has better product and much better duration, for the same price. **Very strongly favours delay.**

(R) 1212 vs. 3332: Delay (option 2) has better product, much better duration, for the same price. **Very strongly favours delay.**

4.2.9 Category 2 choices are the following:

(B) 3322 vs. 1132: Delay (option 1) has much better product scope, for less duration, for the same price. **Strongly favours delay.**

(M) 1331 vs. 3112: No-delay (option 1) has much better product and duration for a 20% higher price. **Strongly favours no-delay.**

(Q) 2121 vs. 3313: Delay (option 2) has much better product, less duration and a 33% lower price. **Strongly favours further delay.**

4.2.10 Category 3 choices are the following:

(A) 3321 vs. 1123: Delay (option 1) has much better product scope, for same duration, but is 50% more expensive. *Ambiguous*.

(D) 3131 vs. 1313: No-delay (option 2) has much better product scope, but much less duration, and 33% lower price. *Ambiguous*.

(E) 2123 vs. 1321: No-delay (option 2) has much better product scope, same duration, but a 50% higher price. *Ambiguous*.

(F) 3123 vs. 1321: No-delay (option 2) has much better product scope, same duration, but a 50% higher price. *Ambiguous*.

(G) 2332 vs. 2113: Option 1 has much better scope, much better duration, but a 25% higher price, with the same delay. *Ambiguous.*

(H) 2312 vs. 2122: Option 1 has much better product, but less duration for the same price and same delay. *Ambiguous.*

(K) 2213 vs. 2231: Option 2 has much better duration, but for a 50% higher price. *Ambiguous.*

(N) 1231 vs. 3123: Option 1 has better product and duration for a 50% higher price. *Ambiguous.*

(O) 2223 vs. 3231: Option 2 has the same product for longer duration but a 50% higher price. *Ambiguous.*

4.2.11 Hence, there are two more choice sets very strongly favouring delay and one more that strongly favours it. To test if this impacts Accent's results, we have removed choice sets to attempt to "even up" the choice sets in terms of the extents to which they favour delay.

4.2.12 We carried out two sets of tests. First, we attempted to even up category 1 by removing two choice sets that favour delay (we varied which two we removed and ran 6 tests in all). Second, we also additionally removed category 2 altogether.

4.2.13 The results are set out in tables 4 and 5. These show the 7-day delay coefficient for PLPPI and the t-statistics for each coefficient. Where the t-statistic is below 1.96, results are not statistically significant at the 95% confidence interval.

Table 4: Regression results from removing bias from choice combinations (test 1)

Choice set removed	Accent Estimate	L, P	L, R	L, J	J, P	J, R	P, R
7-day delay	0.17	0.20	0.15	0.16	0.16	0.13	0.17
t-stat	2.10	2.90	1.88	2.29	2.05	1.81	2.19

Table 5: Regression results from removing bias from choice combinations (test 2)

Choice set removed	Accent Estimate	L, P, B, M, Q	L, R, B, M, Q	L, J, B, M, Q	J, P, B, M, Q	J, R, B, M, Q	P, R, B, M, Q
7-day delay	0.17	0.14	0.08	0.05	0.00	0.03	0.10
t-stat	2.10	1.40	0.90	0.50	0.00	0.30	1.10

4.2.14 Hence, this shows that reviewing a small number of biased choice sets can affect the significance of the Accent results, with reductions of up to 24%. Removing category 2 choice sets renders the delay coefficient insignificant in all permutations.

4.3 INCOHERENCE AND INCONSISTENCY

4.3.1 A known result in the survey literature is that the longer duration and more complex in scope a questionnaire, the more likely a respondent is to tire in giving answers, and the more likely the respondent will provide incoherent answers.[15] In a survey that involves a stated preference question set, the respondent may not fully understand the options, nor give the choices sufficient consideration, or lose concentration with the number of options and questions being given. To explore this, we examined for evidence of incoherence and inconsistency.

Incoherence

4.3.2 We examined whether results were sensitive to Accent's recognition of respondents that did not appear to understand or engage. We also examined whether respondents' answers were internally consistent and coherent.

4.3.3 As part of the Accent data, the interviewers were asked at the end of the survey to respond to three questions concerning the degree to which the respondent understood the questions, the amount of consideration the respondent gave to the questions, and the degree of fatigue over the course of the survey response.[16]

4.3.4 To test if the interview diagnostics made a difference to the utility model, the data was divided by preference towards delay, and then observations were removed if the respondent either:

(a) Did not to understand very much and/or not understand at all.

(b) Gave no consideration to the questions.

(c) Lost concentration in the later stages.

4.3.5 Table 6 provides the detailed results of the Accent model once the observations according to each of the criteria have been removed. The results given are for the coefficients on delay,

[15] For example see: Krosnick, J. A., & Presser, S. (forthcoming). Questionnaire design. In J. D. Wright & P. V. Marsden (Eds.), Handbook of Survey Research (Second Edition).

[16] See Section 4: Diagnostics in the Accent questionnaire. The exact questions were: "Q31: Irrespective of whether or not the respondent answered all of the stated preference questions, in your judgement did the respondent understand what he/she was being asked to do in the questions?" "Q32: Which of the following best describes the amount of thought the respondent put into making their choices?" "Q33: Which of the following best describes the degree of fatigue shown by the respondent?"

and only for the individuals who answered that they preferred delay (as part of question 19 in the Accent questionnaire).

Table 6: Regression results for individuals who stated they preferred delay

Coefficient	1	2	3	4
24 hour	0.42	-0.41	0.43	0.48
	1.91	-0.78	2.54	2.40
7 day	0.77	0.36	0.78	0.73
	6.06	1.04	4.79	4.40

1: When removing individuals who did not understand at all/much
2: When removing individuals who gave little or no consideration
3: When removing individuals who lost concentration or who lad lessened concentration
4: Results from Accent data for the whole sample

4.3.6 The results show sensitivity to exclusion restrictions on the degree of consideration shown by respondents. Where respondents that gave little or no consideration in making their choices are removed, the coefficients on delay were negative (for 24 hours) and insignificant (for 7 days). Hence, the positive coefficients from the whole Accent data (where individuals preferred delay) appear to derive from individuals who gave little or no consideration to the choices being offered as part of the questionnaire.

Inconsistency

4.3.7 The Accent report reveals 31% of survey respondents (Group 2) expressed a preference for delay. This percentage and the value associated with it were relied upon exclusively by the CC in its welfare analysis. Yet, the data shows that those who expressed an interest in delay often selected product combinations in the stated preference study that went against this preference.

4.3.8 Table 7 below identifies the number and different combinations of product choices Group 2 respondents faced in the stated preference survey. The shaded choices represent choice sets that strongly favour options with delay (based on the bias analysis set out in 3.2 above):

Table 7: Option matrix for group 2 respondents - number of decisions made for each choice set

	Option 2																										
Option 1	1122	1123	1132	1211	1232	1233	1313	1321	1333	2112	2113	2122	2131	2211	2213	2231	2321	2322	3112	3123	3132	3213	3231	3232	3313	3321	3323	3332
1112																		92						74				
1212																												92
1222																											3	
1231																				95		6						
1312																					3							
1331																			74									
1332										6																		
1333														92														
2121																									95			
2123								95									3									6		
2213													6			74												
2223																							92					
2231															3													
2312												95																
2332											92																	
3111					3				6																			
3123								95																				
3131							74																					
3211						74																						
3233														74														
3321		92																										
3322	6		95																									
3333				3																								

4.3.9 Given that Group 2 respondents value delay as 60% of the PLPPI premium, one would expect them to always choose an option that strongly favours delay. However, as the following table shows, this logic is not always followed. Table 8 shows the percentage of Group 2 respondents who actually preferred no delay or less delay.

Table 8: Percentage of group 2 respondents choosing an option with less/no delay

	Option 2																										
Option 1	1122	1123	1132	1211	1232	1233	1313	1321	1333	2112	2113	2122	2131	2211	2213	2231	2321	2322	3112	3123	3132	3213	3231	3232	3313	3321	3323	3332
1112																		5						9				
1212																												10
1222																											33	
1231																				67		33						
1312																					100							
1331																			57									
1332										0																		
1333														63														
2121																									25			
2123								60									n/a									0		
2213													n/a			n/a												
2223																							38					
2231															n/a													
2312												n/a																
2332											n/a																	
3111					33				0																			
3123								58																				
3131							58																					
3211						59																						
3233														12														
3321		18																										
3322	33		16																									
3333				33																								

4.3.10 Hence, in some cases 25% of respondents who expressed a preference for delay actually chose no-delay/less delay when faced with a choice set that strongly favours delay. Such inconsistency raises further concerns regarding the robustness of the Accent results.

4.4 REPRESENTATIVENESS OF THE SAMPLE

4.4.1 To test representativeness the Accent data was compared to two different sets of anonymised data provided by LBG:

(a) The sample of data provided to the CC as part of their data request in late 2009; and,

(b) Aggregate data from LBG's database of LTSB PLPPI customers.

4.4.2 LBG also provided customer details such as age cohort, sales channel of purchase, net income, employment status, and loan score.[17] The Accent data was classified to match the same definitions as found in the LBG data, where possible. Despite receiving data from LBG on income, we cannot compare these data with that from the Accent report as LBG reported data on a net basis while Accent reported on a gross, household level.

4.4.3 The distribution of policies across these parameters was then compared for each of the three data sources. The table below lists the results with very significant differences highlighted:

Table 9: Distribution of policies across different categories

[EXCISED – CONFIDENTIAL]

4.4.4 With respect to employment, there appears to be little variation among the three data sources in their distribution. With respect to age, the Accent data appears skewed, containing a higher percentage of 45-64 people in comparison to the LTSB data and a lower percentage of younger (18-44) people. The skewed nature of the sample has a direct impact on the results of the Accent study as the data showed that the preference for delay increased with age.

4.4.5 The other major difference between the Accent sample data and the underlying population data is in the distribution of respondents across sales channels. While [EXCISED CONFIDENTIAL]% of LTSB customers acquire PPI via branch sales, the comparable

[17] From an email received 26 June 2010, the variables LBG provided are defined as follows: Age is at time of application, Credit scores are at time of application and are based on LBG's internal rankings.

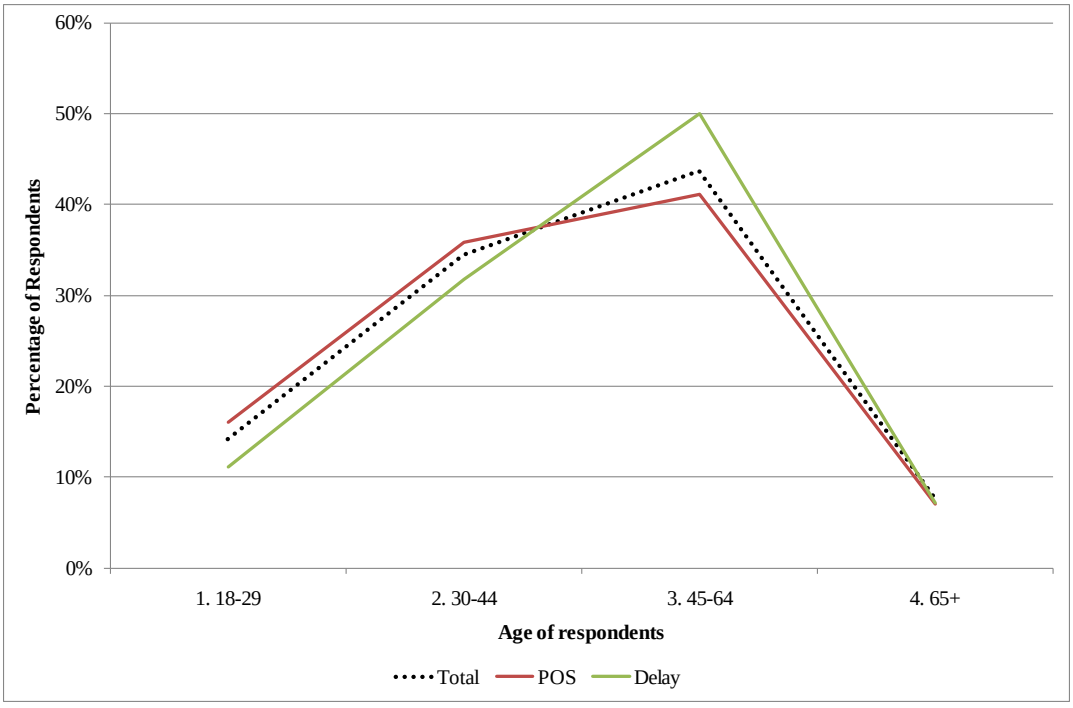
figure for Accent is 40% and nearly one-half of Accent respondents stated that they purchased PPI over the phone. Again, our analysis shows that individuals who have purchased PPI over the phone and through other "passive" channels tend to prefer a delay more so than respondents who purchased PPI via a more active sales channel.

4.4.6 The difference between the sample used by Accent and the overall population impacts directly on whether the results from the Accent report can be deemed to be representative of the population from which the sample was drawn, or representative of the PPI purchasing population in the future.

4.4.7 Our analysis of the Accent utility model that is presented in the Technical Appendix to the report shows the estimated coefficients vary significantly according to age, income and sales channel. This is summarised in the following diagrams.

4.4.8 The figure below illustrates the percentage breakdown across age shows that the older cohort (45 - 64) is disproportionally higher in the group that prefers delay:

Figure 1: Distribution of age according to delay preferences (question 19)



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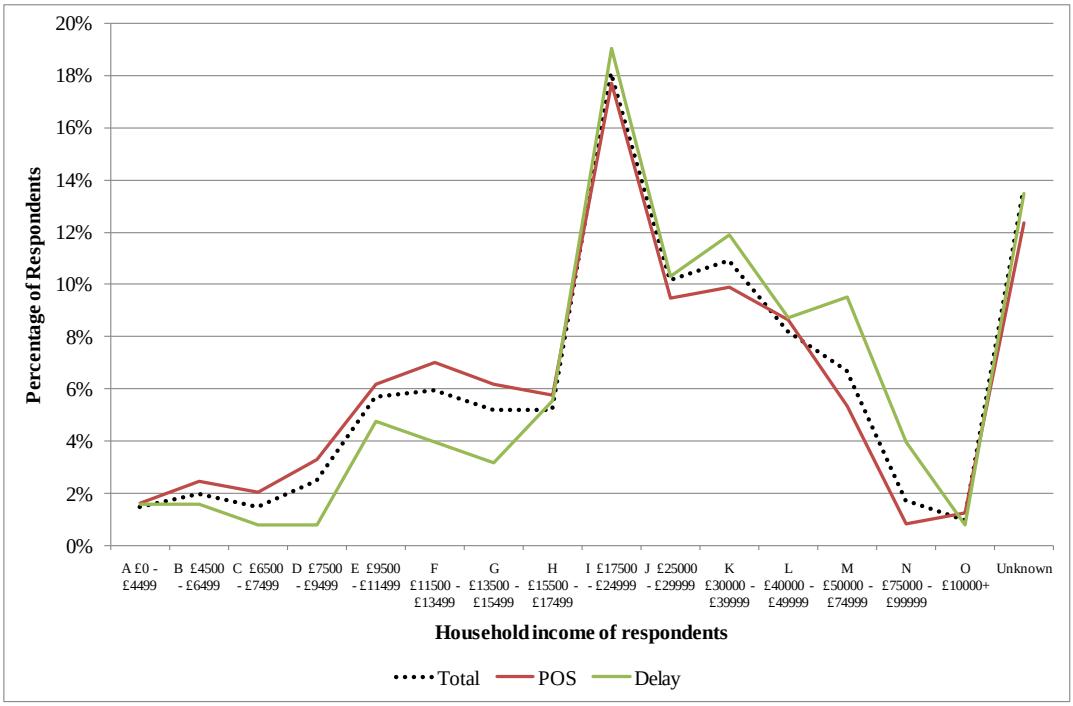
4.4.9 Similarly, figure 2 shows that Group 2 respondents are under-represented in lower income brackets and over-represented in higher income brackets within the Accent data. [18]

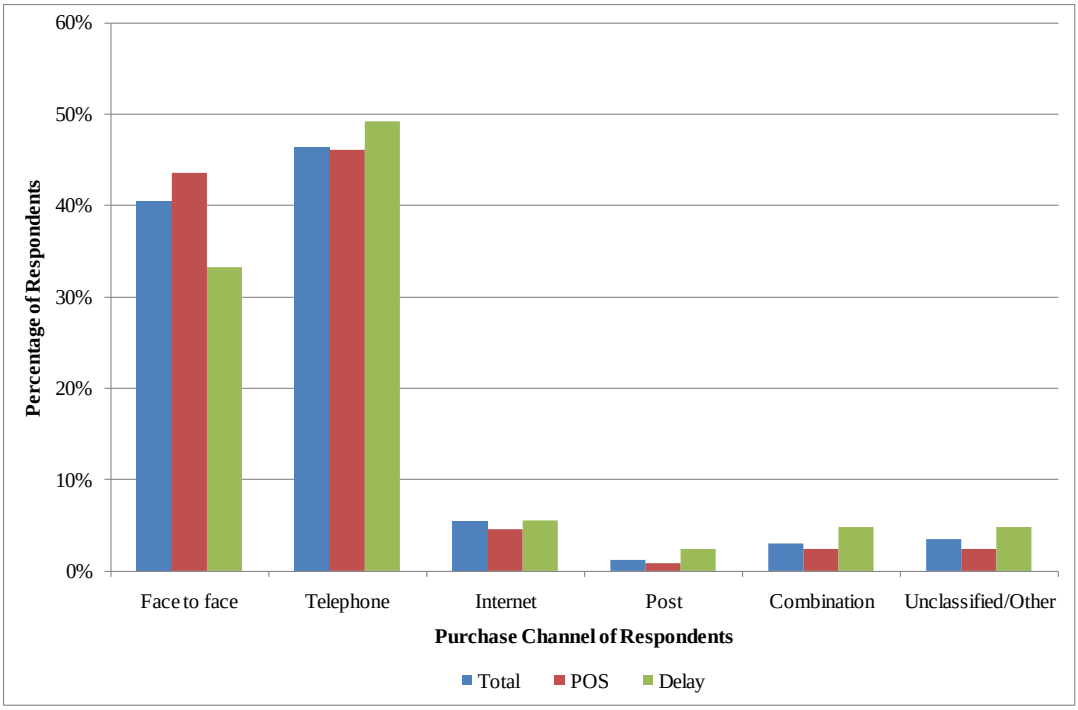
Figure 2: Distribution of income according to delay preferences (question 19)



4.4.10 Finally, figure 3 shows that Group 2 respondents are under-represented in face to face sales channels and over-represented in telephone sales channels within the Accent data.

[18] In question 30 of the Accent report, respondents are asked to best describe their total annual household income, before tax and other deductions. Although other demographic data is asked for, it is not possible to determine how many wages this number represents.

Figure 3: Distribution of sales channels according to delay preferences (question 19)



4.4.11 To illustrate the degree of bias in the Accent model, we took the results from the individual sub-sample regressions on age and sales channel and reweighted them into an overall regression for the whole sample for loans. The results for the delay coefficients only are given in Table 10 below.

Table 10: Reweighted coefficient results by sales channel and age

	Population weighting		Original
Variable	**Sales channel**	**Age**	
24 hours	-0.17	0.07	0.06
	-0.56	0.41	0.30
7 days	0.00	0.15	0.17
	0.03	1.57	2.10

4.4.12 What is apparent is that the results on delay change substantially once they are corrected for the unrepresentative Accent sample. Using the population weights, the coefficients on delay are no longer significant, have a different sign for the 24 hour delay period, and have a smaller insignificant coefficient for the 7 day delay period.

4.4.13 While the results are not definitive, because of time constraints, they show that the regression results from the Accent report are extremely sensitive to the possibility of an unrepresentative sample that was potentially the result of imposing a size limit of 800. Our

analysis indicates the Accent sample is not representative and that the Accent results are sensitive to sample bias.[19]

4.5 RATIONALE FOR PREFERRING DELAY

4.5.1 We have reviewed and extended Accent's analysis of the questionnaire that dealt with the motivations behind individuals who stated they wanted a delay when purchasing PPI. Question 21 of the Accent questionnaire asked Group 2 respondents why they would prefer to take out PPI later.

4.5.2 Analysing the individual responses to this question strongly suggests that respondents fall into two camps: those preferring delay to seek "time to reflect" on the purchasing process and those preferring delay in order to seek out other PPI offers. Accordingly, we have classified the responses as follows: those claiming that they wanted the chance to seek a better deal from another PPI provider or to compare prices or products, and those claiming that they wanted a chance to think about their potential purchase. The table below shows the number of people falling into these categories for both PLPPI (personal loan PPI) and MPPI (mortgage PPI).[20]

Table 11: Classification of comments regarding question 21

	Mortgages	Loans
Total Respondents	**403**	**403**
Respondents wanting delay	**136**	**118**
Seeking time to reflect	*69*	*66*
Seeking opportunity	*66*	*50*
Other	*1*	*2*

4.5.3 Hence for MPPI, the motivations behind those preferring delay were split evenly between those seeking time to reflect and those seeking opportunity. For PLPPI, more respondents preferring delay seemed to want a chance to reflect on their potential purchase. These responses are different but similar to the analysis that Accent sets out in figure 18 of its report.

[19] We note that our analysis could suffer from the fact that the LTSB population data is unrepresentative of the population as a whole. In view of this the CC should analyse Accent's results using the full database it has compiled, carrying out additional work to ensure that the database adequately reflects the population as a whole.
[20] The categorisation of responses was performed by reviewing each response individually and is subjective in nature.

4.5.4 These responses were disaggregated further by employment status and age. The table below shows the results by employment status for PLPPI respondents.

Table 12: Classification of comments regarding question 21, by employment status

	Total	**Want delay**	*Seeking time to reflect*	*Seeking opportunity*	*Other*
Self Employed	**18**	**9**	*6*	*3*	*0*
Employed Full-time	**279**	**77**	*38*	*38*	*1*
Employed Part-time	**42**	**10**	*7*	*3*	*0*
Student	**2**	**1**	*0*	*1*	*0*
Unemployed- Seeking work	**7**	**4**	*2*	*2*	*0*
Unemployed – Other	**3**	**2**	*0*	*1*	*1*
Looking after home/children	**6**	**2**	*1*	*1*	*0*
Retired	**35**	**13**	*12*	*1*	*0*
Unable to work due to sickness	**8**	**0**	*0*	*0*	*0*
Other	**3**	**0**	*0*	*0*	*0*
Total	**403**	**118**	*66*	*50*	*2*

4.5.5 The results illustrates that those employed full-time are split in their desire for delay, while retired respondents overwhelming prefer delay to give them more time to reflect on purchasing PLPPI.

4.5.6 When analysing the results by age, it appears that as the respondents increased in age, he/she preferred delay to seek time to reflect and evaluate the potential PLPPI purchase.

Table 13: Classification of comments regarding question 21, by age

	Total	**Want delay**	*Seeking time to reflect*	*Seeking opportunity*	*Other*
18 – 29	**57**	**11**	*5*	*6*	*0*
30 – 44	**139**	**38**	*20*	*18*	*0*
45 – 64	**176**	**60**	*32*	*26*	*2*
65+	**31**	**9**	*9*	*0*	*0*
Total	**403**	**118**	*66*	*50*	*2*

4.5.7 Given the concerns raised regarding the representativeness of the Accent sample the CC should view these categorisations with additional caution.

Implications for the welfare analysis

4.5.8 In our view these responses demonstrate that for almost half of the respondents the CC's use of the Accent results involves double counting with the additional welfare gains of price cuts as explained in paragraph 2.3.20 of our June 4th report. We believe this also supports the view that for the seeking "time to reflect" respondents the welfare implications should be modelled in the manner set out in paragraph 2.3.22 of our June 4th report.

4.5.9 We have revisited our welfare modelling set out in that report and using the above splits recalculated welfare estimates. The results are shown below:

Table 14: Revised welfare estimates

£ millions	Original Scenario	Revised Scenario
CC Base Case	**170**	**33**
High	11	-88
Medium	-255	-312
Low	-475	-527

4.5.10 In the CC's base case, welfare benefits drop from £170m (assuming all group 2 respondents will benefit) to £33m, if one assumes that 42% of group 2 respondents are effectively double counting the benefit from delay with the benefit they may receive from price cuts and the benefit from delay for the remaining 58% is modelled correctly. These adjustments result in estimates of even greater negative impact in the AlixPartners high/medium/low scenarios.

4.5.11 This analysis takes all other findings at face value. In particular, we note the following:

(a) The negative valuations are likely to be understated as welfare losses are likely to represent substantially more than just shopping around costs[21].

(b) Positive valuations may suffer from buyer's remorse.[22]

4.5.12 We also note that Accent results imply very significant valuation placed on life and critical illness (£5.20 compared with the net willingness to pay for delay of £3.70),[23] which may well not be provided in a standalone market.

[21] See June 4th 2010 report at paragraphs 2.3.5 – 2.3.13.
[22] See Annex 1 of LBG Response to the Provisional Decision.
[23] Table 7 of the Accent report.