Banking Taskforce

Appeals Process

Independent External Reviewer

Annual Report

2012/2013

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1. Executive Summary

I opened the Executive Summary of my first annual report by saying that I was pleased to report that in my opinion the banks were open for business all be it in a different way than they were pre 2008. I also said that the challenging economic conditions were stopping many Small and Medium Enterprises (SMEs) from making investment decisions, and indeed that many were deleveraging and paying off as much of their debt as they could afford. Over the past year as I and my team of 8 auditors have gained more information from the banks and from SMEs that are part of the process we have become even more familiar with the way the banks lend and customers respond so therefore I have no reason to change either statement.

Indeed, I now feel that as much as it can be that banks are now lending in what I would call a 'normal' way but, like last year, I need to explain what that means as it will form a great part of what comes later in this report. SMEs are still cautious in terms of investing or borrowing more which reflects the still uncertain state of the economy, as perceived by them, even though the picture is becoming slightly brighter in certain areas.

Banks, and indeed all financial institutions who lend to business, use two basic criteria in making their decisions. Firstly, there is their own internal lending process which varies bank to bank but now has affordability at its heart for every lender. Secondly, there is the state of the economy not just in macro terms but also within the sector that the business, which is looking for credit, operates. While most banks will have a similar view on the macroeconomic environment, they may differ on their view of sectors for various reasons. Pre 2008 we had aggressive and sometimes reckless lending in terms of the banks' own internal criteria operating in a buoyant and growing economy. We have now returned to normality in terms of the banks' own internal lending processes, and the sectors and business areas with which each feel comfortable, but the economy, as is stated above, is still relatively flat. It is my belief now that it is the latter that is causing much of the anxiety that we still see amongst businesses in terms of their view of lending.

From all that we have seen over the last year both from the banks themselves and from their customers, who I now spend more time with, the issue is one of demand rather than supply in terms of lending that can be sanctioned. That is not to say that there are not businesses still looking for finance but the majority are those who already have financial challenges where affordability becomes an issue for the lender. Banks also have readjusted to both the large gap that was left when many banks withdrew from the UK at the time of the financial crisis, and also the readjustments that subsequent regulation has meant they have had to apply to their Balance Sheets in terms of keeping more cash set aside for possible future events. I do not think that the banks not having money to lend is an issue which it may have been just post 2008. The issue is as much about finding good projects to lend to or SMEs who want to increase their credit.

I think we have also forgotten that businesses and banks have never had a perfect relationship and from all my years in business there have always been complaints about specific businesses finding it difficult to find finance. It will never be perfect going forward either but the noise that was prevalent just post 2008 was caused by a shock that none of us had experienced before and that has now settled down. Therefore, I do not now see anything that is not the same that has been about for decades if not centuries between businesses and banks. The basic challenge remains one of expectation between banks and SMEs. Banks see themselves as debt not equity providers so therefore take less risk and demand assurance that the debt can be paid through their affordability processes. SMEs, especially small ones, still do not always see the difference between debt and equity so still ask banks at times for debt that is in effect equity and so beyond the risk boundary that debt would allow the banks to operate within.

Having said all the above I do think that the Appeals Process itself is having a real positive impact on lending to SMEs both in terms of the way banks are changing the way they do certain things and also identifying other issues that others need to rectify if there is to be a sensible lending environment between banks and business which meets the needs of each as much as it has ever been possible to do.

In terms of this year's Annual Report it follows very much the pattern of the first one[1], which I think is important for consistency, but also will address specifically each of the issues I raised last year in terms of where we have got to on each. We also have a much bigger data set to use now which allows us to delve deeper into the results which provide a richer and more comprehensive view on what is going on.

I am pleased to report in this second year that over its first two years the Appeals Process has generated almost 5500 appeals and a total value of overturned appeals, based on cases for which we have detailed data[2], of in excess of £28mn. While we cannot gross up from that number for various reasons, I am happy to say that the Appeals Process has returned over £30 million in lending into the economy in its first two years.

In Year 2 there were 3311 appeals as opposed to 2177 in year 1, which is at face value a 52% increase on last year.

[1] http://www.betterbusinessfinance.co.uk/images/uploads/Annual_Report_Master_2012.pdf

[2] Out of the total appeals of approximately 5500, we have captured detailed data from the banks of around 2700 cases, including a majority of those overturned in favour of the customer.

However before looking in summary at some of the other key numbers let me state quite clearly that Year 2 numbers cannot really be compared to Year 1 numbers because of a number of reasons, including the fact that process changes that the Appeals Process has brought about within specific banks have reduced the number of declines and therefore appeals.

The reasons for making comparison difficult include:

a) That it was not really until 6 months into Year 1 that all the banks involved in the process were up and running on the same basis.

b) Appeals on Credit Cards were one of the areas that took time in Year 1 to get up and running and since their overturn rates are higher than the norm last year's overturn rate was probably understated on a full year basis.

c) Some banks this year, based on analysis and input from us, in terms of how and when they make decisions have changed the way they operate which has both reduced declines and overturns.

d) Similarly some banks are now referring some initially declined lending decisions for further review rather than immediately declining them.

In terms of overturns in Year 2, the overturn rate was roughly the same as last year at 39.2%. However this hides a general trend over the last quarters of a decline in the overturn rate as the changes in processes that the banks are now putting in place start to impact on the numbers. In the first quarter of year 2 overturn rate rose to 53% reflecting the influence of credit card numbers, but by the last quarter of year 2 overturn rate had fallen to 37% reflecting the changes that lenders had initiated as a result of the Appeals Process.

This is primarily due to credit cards where this is the first year where we have a full year's data available and if you exclude credit cards from the data the overturn rate on other forms of lending is at 29.5% as opposed to 32.6% last year.

The detailed analysis of the appeal numbers is set out in section 6 of this report but the key areas for me are the difference in the decline reasons the minute that lending increases above the £25k level. The top four decline reasons are shown below.

<u>Lending Below £25k</u>

Credit Scoring	58%
Affordability	19%
Account Conduct	12%
Appetite	8%

Lending Above £25k

Affordability	48%
Appetite	20%
Account Conduct	8%
Business Experience	8%

While some of that is due to credit cards being all below £25k it is not just them changing the decline reasons and credit scoring is still the main reason for decline for other lending products below £25k.

The reasons for this are explored in the report but are focussed on two themes:

i) The processes all lenders use for evaluating small amounts of lending

ii) The effect that the Consumer Credit Act can have on these decisions in terms of the additional strictures it may put on lending processes.

In terms of the priorities we highlighted in Year 1, section 4 sets out where we believe we have got to on each.

In terms of communication and awareness I believe that making the customer and Relationship Manager within the banks more aware of the Appeals Process itself, and importantly that it is working, continues to be a key factor. On both I believe progress has been made but much more remains to be done but it is pleasing to be able to report that lenders, Trade Bodies, and Government are all looking at how that awareness can be further expanded and we highlight some of that in this report including the new easy access appeals button on the internet.

In terms of credit scoring which was a main issue highlighted in my first report, I now have gathered more data to understand the issue better and progress has been made on a number of fronts, as is highlighted later in this report, but there is still much to do. I am pleased though that as a result of the appeals work and SME Finance Monitor findings the BBA is publishing a guide to credit scoring. I will explore further with the Financial Conduct Authority issues surrounding the Consumer Credit Act.

The final issue to highlight here is the critical one of encouraging a better dialogue between customers and lenders. Again, I believe that this has progressed but still has some way to go but to me this is the main key benefit of the Appeal Process as even if the appeal is not overturned, in general, there is a better conversation between the customer and lender that could lead to further lending in the future.

In terms of the Appeal Process itself, I am encouraged by the way that all the banks have listened to what I and my team have said to them and we have seen many process and other changes within the individual banks which I feel will lead to a better outcome for not just the customer but also the bank. We have moved to a wider view on how we audit and now involve the bank as much as ourselves in preparing the data on each case which gives us a wider data set to examine as well as being more precise in how we audit.

Going forward into year three there is still much work to be done on many fronts by all parties, including myself, to ensure that:

A. Customers are made more aware of the Appeals Process and that it is working for them, and that all those who communicate with SMEs helps in that process.

B. Banks ensure that all customer-facing staff are not only aware of the Appeals Process but are encouraged to use it.

C. Banks' internal processes and communications become simpler and more readily understandable by customers.

D. Banks continue to change their process where it adds value to themselves and their customers, including specifically how best practice is shared and used across them all.

E. Credit Scoring and its impact becomes better understood by customers, those within banks that use it, and those outside banks whose rules and guidance can influence that.

F. I produce a short quarterly summary of progress on Appeals and the changes that it is advocating to ensure that we are all focussed on them.

G. If all the above move forward as I hope, then next year I should to be writing about a further increase in appeals numbers, a decrease in overturn rates, and a better understanding between banks and their customers of the key issues that affect them both. If I can do that then I will feel that the journey we all embarked on two years ago will be having the real positive effect I had hoped it would be having and that we can then start to embed the Appeals Process into the natural process of lending going forward.

Professor Russel Griggs OBE
Independent External Reviewer

June 2013

2. Introduction

Year 2 of the Appeals Process has been a year of consolidation and further learning for all those involved in the process including myself.

As the Independent External Reviewer of the Appeals Process it is my role to ensure that the banks both promote and examine appeals in a way that is transparent and fair. In doing that I sit on neither side of the lending fence and try to, from the evidence I and my team gather, to create solutions to blockages in the lending process which benefit all parties. This can be from any direction and can fall on the lenders but also on customers, those who advise them, and on Government itself.

As I stated in my first Annual Report, when I agreed to take on this task I did so on the understanding that we would look on this as an educational process where all (lenders, businesses, and Government) could enhance their knowledge and understanding, and in doing so make any necessary changes to anything that stood in the way of us all moving to a situation where we all played our parts in the lending process as well as we can. I believe that much progress has been made this year but there is still work to be done on all sides to take it forward. This has and never will be perfect as businesses and lenders will always have differing views on specific parts of the process, or individual cases, but it is always thus between any business and customer in any environment and process.

I have personally spent as much time this year, and will continue to do so, being with and talking to front line bank Relationship Managers and individual customers as I have with their Appeals Teams as it is only when you relate that knowledge to what the data appears to be saying that you can paint a real picture of what is actually taking place.

This is also the second Annual Report and therefore it should pick up any challenges or objectives I set myself and others for this year to see what progress has been made on them. I believe strongly that Annual Reports on processes like this should be interlinked and part of a journey with objectives and milestones along the road which I as much as anyone else should achieve.

In terms of the background to the Appeals Process regarding where it came from, what it is, etc., this is set out in Annexes A and B so it is not the intention to cover any of that background within this report.

Therefore with all the above in mind this year’s report is broken down into parts namely:

Current Economic and Financial Context

Priorities for Year 2 as set out in last year’s Annual Report as well as progress made by the banks against their Action Plans in Year 2 and areas of Best Practice emerging

Auditing Practices in Year 2

Key Numbers for Year 2

Key Priorities for Year 3

As always, I would like to take the opportunity at the outset to say thank you to everyone I have worked with on this throughout the year which is now a significant number and for all the honesty and openness that has been an integral and common part of the discussions and exchanges that have taken place. I hope that this process adds as much to the knowledge of who I and my team speak to, as they do to us. It is only with this openness and honesty that we can all make progress and I think we all can see the benefit of that now and going forward.

3. Current Economic and Financial Context

In the first Annual Report I set out a picture of what I felt the differences were between the lending environment (for all lenders not just banks) pre and post the 2008 crisis. In doing that I did state that initially perhaps the risk appetite post crisis by all lenders had swung too far to the adverse risk end of the spectrum. I think now that it has come back to a more sensible and normal place within the context that lenders make decisions. I think this is partially due to the financial sector now recovering from both the withdrawal of a significant number of banks from the UK at the time of the crisis and the impact of the subsequent toughened regulation on their Balance Sheets. I think banks now have a more stable picture of where they are now which is allowing them to return to this ‘normality’.

How all lenders make decisions is in very general terms split into two parts:

1. The lender’s own decision making process.
2. The state of the economy or the specific sector in which the business operates.

In terms of the first all the banks, and indeed other lenders, have their own way of making those decisions but all do so within a similar context.

Lending decision making is a very linear process with when you make the decision dependent on how much information you want to collect before making it. At one end you can make the decision very quickly based on only very minimal information but history and good sense says that this does not lead to good decisions in many cases. At the other you can wait until you have all the information you need to make a perfect decision but that would take too long for both parties and indeed would never be perfect as situations can change during that process. Therefore each lender makes its own decision on when it thinks it has enough information to fit within its lending risk appetite. This will vary but in general terms since 2008 all lenders will now ask for more information and take longer to make decisions than they did pre 2008. However for those of us that can recall the time before the buoyant period of the 90’s and early 2000’s then is it probably back to where it was before that.

However, we will highlight later in this report the positive impact that the Appeals Process is having on some lenders in terms of when and how they make their decisions.

Also there is a more general case that could be made that if a business provided more information at the outset of its relationship with any lender then it would make subsequent lending decisions easier. This would be at account opening and would take the KYC (Know your Customer) principle to a different place. However it is likely that this would bring resistance from businesses as it would be time consuming at the beginning.

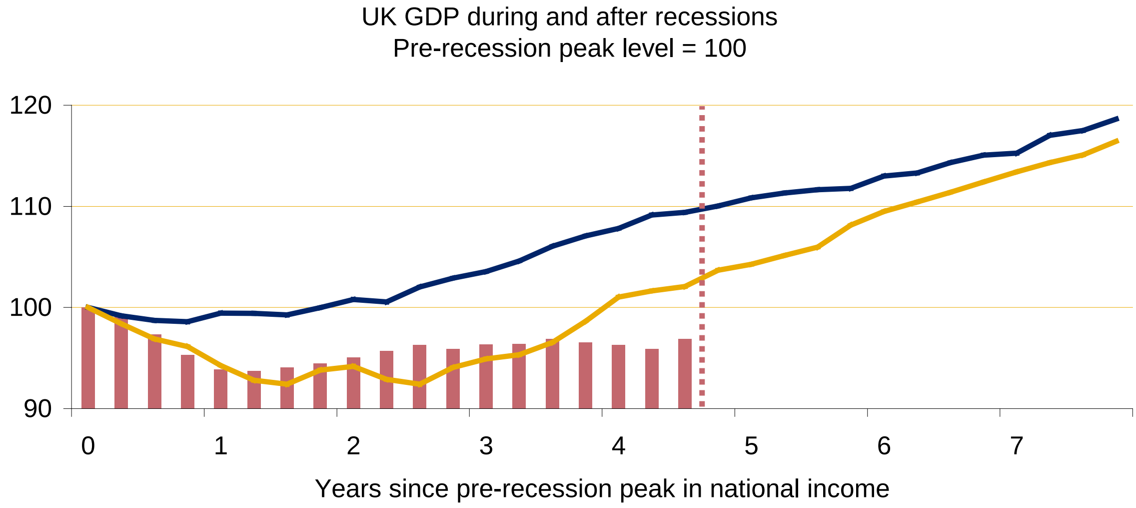
From the almost 5500 cases that have been through the Appeals Process, I believe that the way in which banks are now making decisions is back to what could be referred to as ‘normal’. However, post crisis the proper assessment of risk by the banks, including the customer’s ability to repay any lending, has become more visible and more regularly adhered to. The banks make decisions to ensure they live within the boundaries of the regulatory and financial restrictions that they have to operate within at that time. In the end there has to be a balance between having a good and sustainable financial sector and not letting it take too much risk and the banks are operating within that. Whether any of us believe that to be right or wrong is, in a sense, irrelevant as it is where we are and we have to adjust to operate within it.

The key criteria driving those decisions now are affordability of the lending being asked for at that time, the ability of the business to deliver its plans, and the security (if needed) that is available to support that lending if it all went wrong. In many ways these are the basic principles of lending that have always been in place with risk being the factor that differentiates different kinds of lending in different forms and price. However, as we will highlight later in this report, some external influences and factors at some parts of the lending process, especially to micro businesses or those wishing relatively small amounts of lending, can have a detrimental effect on the lending process which may not be helpful for business.

In terms of the second part of the lending process, namely the state of the economy as a whole or the specific sector that a business exists within, that is where there is still uncertainty which is the current main issue for both business and lenders.

The economy remains in essence flat with growth being slow. This is not making any political or economic point just, I believe, an accurate reflection of what I feel from talking to businesses and lenders. The challenge that all politicians, lenders and economists have is that we have never been where we are before in terms of a return from a recession.

Table 1



Source: Office of National Statistics/ Bank of England
Colour Codes – Blue line = Average of all recessions 1955 – 1990's
Yellow Line = Great Depression
Red Block = 2008 to Q3 2012

There have been many graphs and articles on this subject but the above chart, compiled from Bank of England and Office of National Statistics data, and used widely within at least one of the banks, shows the time it has taken the UK economy to recover in times of recession. As can be seen in all the recessions we have had over the last 100 years the economy has recovered by now to the level it was pre-recession. This is not the case in this recession so we are in new territory in terms of forecasting. This is causing uncertainty both to business and lenders, and indeed to economists, which is why lenders are still cautious in looking forward. Sentiment is a key driver of any economy and while it has improved since the year's immediately post 2008 it is still not back at a level which either encourages businesses to make some of the key decisions they need to make, or in terms of lenders for them not to, at times, discount some of the forecasts that business will put to them when looking for credit. The media has a part to play in sentiment as well and, without wishing to be drawn into, or be part of, a media debate it is clear that many SMEs still rely on the national media as a key source of data and advice on the economy. Its impact therefore does and can drive sentiment, as indeed does political rhetoric, so both need to be balanced and measured or they will add to the uncertainty that already exists.

Since affordability is now the key decision driver for lenders, it is based on the lenders' belief that the finance it will lend can be repaid. This may differ from the view of the business in that the lender may well discount the revenue or profit forecasts that a business may make in terms of the lender's view of the economy or sector which may give it a different affordability view compared to that of the business.

From the customers I have spoken to over the year, while confidence levels are getting better, sentiment and uncertainty are still making businesses think longer and harder about investment decisions, and then about any extra credit it would take for that which means that demand is still an issue and will remain so until certainty returns. Interestingly business in general can work round any certainty, including bad ones, but not knowing is the thing that makes business stop and pause. Also many businesses are still deleveraging and looking to repay existing debt quicker than they had planned which again all falls into many SMEs being cautious in their approach to growth and lending at present.

Finally in terms of this section, the other factor affecting lending overall is that lenders are returning to a business model of focussing on what they see as their key areas of expertise and in where they feel comfortable operating. In doing so they are operating no differently to any other business when conditions are challenging. That is not to say that lenders are turning anyone away but in terms of where they are targeting their interest they are becoming much more focussed. Pre 2008 they had all become generalists looking for business almost everywhere but now that the economy and lending conditions have changed so they have returned to what they know has brought them success in the past or to sectors in which they have greater experience of operating.

In summary therefore, the lending environment has and is returning to some sort of normality given that the situation that we were in pre 2008 was abnormal but the uncertainties within the world economy are still dampening both demand and lending in terms of what can be afforded by businesses and the tighter fiscal and regulatory regimes in which lenders now have to operate.

4. Priorities for Year 2

In my first Annual Report, I highlighted some issues that I felt we all needed either to address or do further work on, plus I set myself some areas of focus for Year 2.

In terms of my own focus these were on 5 areas, namely:

1. Find ways to get the message out to more SMEs that there is an Appeals Process and also that it is worth appealing.

2. Make sure that the banks continue to operate an effective appeals system by continued auditing at a level which gives me the assurance I need.

3. Make sure that the things the banks and others said they would do and would build into their appeals and other processes from Year 1 are completed. To ensure that we will put in place with each organisation involved a plan which sets out details and a timescale for delivery of each change.

4. Make sure we maintain and enhance the data source we have on the appeals. This will allow us to gain even greater understanding of the reasons and causes of decline.

5. Reveal any other issues that we have not discovered this year that will need to be resolved to get lending to the sensible place we all wish it to be.

As well as these I identified some other areas which had come out of Year 1 which we needed to pursue namely:

6. Ensure that retraining of bank staff continued

7. Ensure that businesses were educated into what the new lending environment meant for them.

8. Understand how credit scoring operated and what could be done to make its impact better or more understandable to businesses.

9. Continue to encourage more and better dialogue between a business and its bank.

10. Look at how the signposting to other forms of finance was progressing.

While 10 does not fall into the remit of the Appeals Process per se, it does now impact on it given that signposting to other forms of finance is a part of the obligation that banks have taken on and where and how the Appeals Process fits into that process is of interest to me.

The following sections of this report deals with each in turn.

4.1 Find ways to get the message out to more SMEs that there is an Appeals Process and also that it is worth appealing.

Communication of the Appeals Process has been a key area of discussions with all those involved in the process (banks, Trade Bodies, and Government) throughout the year. Also, it has become clear to me that one of the areas we did not highlight last year was that communication of the process within the bank itself is as critical as communication to the businesses.

At the end of Year 2, all I think I can exactly say is that we have made some progress but there is still a lot to do by all parties involved.

In the best practice section 4.3 below, we highlight the fact that where a bank has allocated a manager specifically to the process of promoting and managing the Appeals Process both within and outside the bank, real progress has been made in communicating the process both within and outside the bank. Some banks, we believe, will follow that model which is encouraging. I look forward to working with the banks over the coming months to see how this piece of best practice plus others stated elsewhere in this report can be taken on board by all lenders. That is not also to say that each bank does not have an individual allocated to the Appeals Process who are doing a good job but they do so within the confines and restrictions that their other responsibilities put on them and the experience shows that where the maximum time is allocated to the Appeals Process then maximum benefit derives from it.

However the majority of banks only highlight the Appeals Process to those who have been declined which I feel falls short of where we need to be. I stated in my first Annual Report that knowing that there was an Appeals Process there, knowing that it is working properly, and that declines are being overturned could influence more businesses to consider lending as knowing a safety net is there always encourages human beings to do things beyond what they might.

Also we know from past research that people do not always read all of the content of letters sent to them especially if it is informing them of something they do not want to hear so even informing all customers who are declined by letter that there is an Appeals Process will not get that information to all those as well.

Over this year banks have tried in various ways to get the appeals message out to their wider customer base and we have seen short term increases in some banks' appeals numbers when that wider mailing of information on the Appeals Process or other event happens. However more has to be done including more selling and informing of the benefits of the process inside each bank to the Relationship Managers and Customer Service Centres who are the key front line interface with customers. Again the bank that has spent the time making each of its divisions aware of the Appeals Process and how it can add benefit to them has shown the most sustained increase in numbers. Also they have been able to show others within the bank that the loan book from overturns performs the same as their standard loan book which has reassured many and shown that they can add to their lending book safely by encouraging appeals. The reason I highlight this is that I am still not convinced that every Relationship Manager in every bank either knows about or is convinced that the Appeals Process is something they should recommend. All banks have made it clear that Relationship Managers will not be 'judged' by appeals overturned but there could still be some reticence in certain Relationship Managers. Also we need to further the message to SMEs who again feel that appealing would harm the relationship they have with their Relationship Manager, and show that it would not and indeed your Relationship Manager should be encouraging you to do so if you feel aggrieved.

However, it is not just the banks that can do more. The Trade Bodies themselves need to do more and it is good to see that after round table discussions at the turn of this year with all parties (banks, Government, and Trade Bodies) they are going themselves to more actively make their members aware of the process. Also the banks' own trade association the British Bankers' Association is working with all parties to put in place a simple online Appeals Button which will allow those that wish to appeal to do it simply and access it from multiple sources (see Annexe J 8.10).

Government also could do more and it was encouraging in the meetings that I have had this year with Ministers that they see the need for that as well and are embarked on a process of looking at ways of getting more information out through their channels including providing every MP with a supply of Appeals Process leaflets (see the accompanying Poster in Annexe K 8.11) for their constituency offices. The devolved administrations should also do the same as economic and business development is devolved to the different administrations. Indeed, in a review done by the Economic Advisory Group for the Minister of Enterprise, Trade and Investment in Northern Ireland recommendation 3 states.

"We recommend that banks should work with the Independent Reviewer for the UK Banking Appeals Taskforce to strengthen and publicise the credit appeals process in Northern Ireland. Business organisations should also play a role in publicising the process."[3]

The results of the Finance Monitor report for Q1 2013 are encouraging and show overall appeals awareness, amongst those customers interviewed, has improved to 13% (10% in Q4 2012). However, we know that getting the message out to SMEs is never going to be a simple process as those that have tried to market others things to this audience have found over the years, but that does not mean that we should not

[3] http://www.eagni.com/fs/doc/publications/eag-review-of-access-to-finance-for-ni-businesses-final-report.PDF

do more. Also at any one time there are probably only 11% of SMEs looking for finance (new and renewal applications) so the constituency to reach will be even smaller.

However, there is more that all Trade Bodies, through using their forums and conferences to get the message out to business, and others can do including the use of the Trade Journals across a wide area and I have stated many times this year that I am happy to go and speak or be interviewed by anyone and anywhere if that helps get the message about the Appeals Process out there and that it is working. I therefore would be disappointed if I was not invited to more this year.

4.2 Make sure that the banks continue to operate an effective appeals system by continued auditing at a level which gives me the assurance I need.

Section 5 of this report (below) sets out the changes we have made to the methodology and frequency of auditing this year to augment the standard processes we already have in place which are set on in Annexes C-F.

Maintaining a good and solid data set based on a significant sample of the overall appeals is now also critical to us as it allows us to do the type of deeper analysis which we have done this year and is set out in section 6 of this report (below).

4.3 Make sure that the things the banks and others said they would do and would build into their appeals and other processes from Year 1 are completed. To ensure that we will put in place with each organisation involved a plan which sets out details and a timescale for delivery of each change.

At the end of Year 1 we put in place with each bank an action plan with milestones that each had to deliver to satisfy issues we had raised with them.

Banks have each prepared a Suggested Improvements plan which fully encompasses the issues we raised with them. These are tailored for each bank but, as summarised below:

- All banks, in communicating with their SME customers will highlight the better business finance and taskforce initiatives and inter alia the Appeals Process that forms part of that.
- Where practicable, banks will make a written or audio record of the decline conversation that the Relationship Managers and other front line staff of the bank has with the customer. That conversation, from evidence from Year 1, we believe in many cases is a key part of the declines process.
- Written lending decline letters are being enhanced providing additional signposting to:
    - the new businessfinanceforyou.co.uk website enabling businesses to review the range of alternate finance providers

- the option for the business to be referred to a relevant Community Development Financial Institutions (CDFIs) for the finance application to be reviewed and assessed by the CDFIs for suitability of the CDFIs to extend the finance requested. The pilot in this area is now complete and the model is now being rolled out nationally with one bank already operating it across the country. I will be following the progress with interest
- the offer of a bank mentor to support the business in considering next steps plus also through the other initiatives around the better business finance website regional events, (businessfinanceforyou.co.uk) etc. which are all part of the ways that banks are trying to help businesses with support and impartial guidance

- Continued bank on-boarding/awareness training for customer facing bank officers.
- Bank review of their lending application processes to address opportunities where borderline "automated" decline decisions are manually reviewed before the decline decision is communicated to the customer.
- In some cases, banks are enhancing their IT systems to deliver process improvements.

It should be noted that even small changes, e.g. to decline letter content, require changes to IT systems. Like any large corporate, such changes to systems will need to be fully tested and then scheduled for release within the constraints of other releases and priorities so may take some time to complete.

Progress on all the plans generally has been good.

There has been good progress specifically in the areas listed below:

a) In the two critical areas of decline letters and recording of the RM conversation with the customer when the appeal decision is related to them.

b) In terms of letters many have been shortened and simplified and made less legalistic, and a number of banks are looking at how they can restructure them to make sure that reference to the Appeals Process appears earlier in the letter, as currently it has tended to be towards the end of it.

c) The most pleasing development to us is how two of the banks have examined where and how they make their decisions in the automated part of their lending process and have moved the decision point backwards which allows for the gathering of more information before a decision is made. We have already seen a fall in overall declines, appeals, and overturns in those banks which mean that both the customer and the bank are achieving a better outcome without having to resort to further analysis. I think this shows that the banks are seeing the Appeals Process as meaningful and adding value to what they do and also listening to the advice that we give from the analysis that we can do. Also, once each of these banks determined that these were issues they needed to resolve, they applied appropriate senior resource to make sure it happened and delivered a good solution.

d) While all banks have individuals overseeing the Appeals Process, in most cases this role tends to be part of wider responsibilities. I have already mentioned above how having a person within the bank whose sole job is about promoting and managing the Appeals Process adds greater value. Being able to devote significant time to Appeals has shown benefit where the focussed person is and we know that at least one other bank is moving in the same direction and hope others may look and learn from what benefit this has given that bank not just in terms of the Appeals Process but in its wider relationships with its customers.

In terms of CDFIs referral etc. it is still too early to make a general judgement as the process has only recently started in its totality.

During this year as we have come across issues so we have put in place supplementary plans with each bank to take those issues forward.

We will discuss and agree revised action plans with each bank for the coming year.

As well as the above, we are now beginning to see examples of other best practice in the banks which are worth highlighting for other banks to examine and look at to see if they would enhance their systems and processes as they have for others. We will work with all lenders to see how the best practice listed below and others highlighted elsewhere in this report can be put in place by all lenders as appropriate.

Best Practice

1. Promoting greater customer awareness of the Appeals Process through direct mailing campaigns and bank statement mailshots.
2. Bank Appeals awareness training.
3. Decline letters which clearly state in “plain English” the decline reason/s.
4. “Searchable” bank websites which give customers detailed and helpful information on making an application for lending and available sources of finance.
5. Online Appeals.
6. Appeal Acknowledgement letter sent by banks appeals control point.
7. Bank Appeal Reviewers empowered to interface directly with the customer.
8. Appeal outcome letters which deliver a timely response to the customer notifying that an appeal has been overturned ahead of sending bank facility documentation. Where a decline has been upheld on appeal, the letter clearly states the reasons why the bank is unable to approve the lending request.
9. In the small business sector and small lending part of banks Relationship Managers have a choice if a customer is initially declined that before going back to them to tell of that decision they can refer the decision to someone else to look at. I am pleased to say that due to recommendations and actions

that we have suggested this is happening more often and indeed in some banks all the time where it is not an automatic response. This has reduced the number if initial declines plus again creates a better dialogue between bank and customer when either the decline or acceptance is concluded.

4.4 Make sure we maintain and enhance the data source we have on the appeals. This will allow us to gain even greater understanding of the reasons and causes of decline.

As is stated above the changes we have made to the auditing process as set out in section 5 below have allowed us to ensure that we have a good and solid data source going forward.

4.5 Reveal any other issues that we have not discovered this year that will need to be resolved to get lending to the sensible place we all wish it to be.

We did not identify any unrelated or unconnected issues from our work during the year. However, the additional data gathered and conversations held has helped to sharpen the focus for the discussions we have had with the banks. It is also helping to identify the priorities for the coming year.

4.6 Ensure that retraining of bank staff continued

All the institutions have continued and augmented the training they give to their customer facing staff, including the Relationship Managers, and it is clear now that lending decisions at specific levels can only be given by personnel who have been trained and accredited up to that level. This means now that there is a good progression route within each bank with added training to be had and confirmed before progressing up the lending ladder. That said it is an area the banks recognise is still work in progress.

4.7 Ensure that businesses were educated into what the new lending environment meant for them.

I have spent a lot of my time this year with the front line Relationship Managers of all the banks and a variety of customers in terms of size and sector.

I have discussed the issue of educating businesses with Relationship Managers and SME customers when I meet with them and there has been a mixed response to it.

The answers I get most frequently are:

a) There is still an issue.

   In section 4.1 of this report (above) I explored in some depth the need to get more information on the Appeals Process out to businesses and I will not repeat that here. However, the issue here is a wider and more general one. It is not clear, even if a business did know about the Appeals Process, how prepared or knowledgeable about the lending process they are and how that will help or hinder their approach and chances of success, and also whether they will come to lenders in the first place.

This latter point tends to come from Relationship Managers who believe that the message from the media and from elsewhere that banks are not lending, is still harming demand and stopping businesses looking for credit approaching them. I have heard this also from smaller customers where this tends to be more prevalent as larger SME businesses have better and more informed networks that they can use to keep abreast on the reality of what is going on in the economy and lending. In the micro business (0-9 employees) and small lending space (10-49 employees) there are at any time only about 7% who are thinking about looking for extra lending (new applications) to grow their business, and since many other pieces of research have shown that sentiment in the micro business area is a key driver of lending decisions then more has to be done to change the story getting to them.

Therefore encouraging more SMEs to appeal and showing that decisions can be changed is also a key part of raising business knowledge in its widest sense as well as increasing awareness of the availability of the Appeals Process.

b) There is nowhere now to go for help.

This is an issue that I highlighted last year and has been highlighted again in England by customers especially those from small businesses. In general the larger the company or the larger amount of credit that is being sought the more sophisticated the company applying is or has the resources, either internally or bought in, to understand the dialogue and process that is needed with the lender. Small businesses are different in that many only think about applying for lending infrequently and therefore have not built up knowledge of the changing lending environment and process. Also the smaller the company or amount to be borrowed the less sophisticated the Relationship Manager in the lending institution tends to be and will, in general, have a larger company portfolio to deal with than those Relationship Managers dealing with larger businesses.

With the demise of Regional Development Agencies and Business Link (both face to face and in its web presence) the places to go for help for small business in England has reduced significantly. While the Local Economic Partnership network and the Chambers of Commerce are trying to fill the gap to some extent it is very patchy and inconsistent. There is a gap in financial readiness assistance at the small end of the business and lending spectrum in England which needs to be addressed. It is interesting to see that in the Chancellor’s latest budget it was said that this would be part of the new

Business Bank's offering but this still appears to be some way off so the gap continues to exist for the present.

However as is stated above the banks themselves have initiated a variety of schemes that are highlighted in 4.3 above.

c) Customers still do not seem to want to consider alternative forms of finance

Into this as well I will include issue 10 namely '*Look at how the signposting to other forms of finance was progressing*' as they are inexorably linked.

Much has been done this year to ensure that companies are pointed at other forms of finance and while it does not fall directly into my own remit on appeals I have been following its progress to see how it fits in with the Appeals Process. The reason for my interest is that we have seen declineswhere had the SME applied for the credit in a different form or accepted a different product from the bank then a resolution could have been found.

Following discussions between BBA, Government and banks, SME businesses who meet the criteria (which may vary by region), are signposted to CDFIs which might provide another option for lending. This will be through the decline letter or by dialogue with their Relationship Manager or both. This does not preclude the business from appealing their original decline with the bank but gives them another option. It will be interesting to see how this develops over the coming year as CDFIs by their nature will be as robust in assessing a lending proposition as a bank, all be it with different criteria. These alternative lenders should not be seen as easier than the traditional banks but just different.

What type of lending that businesses are using to fund their business has also been a specific topic at the majority of meetings I have had with Relationship Managers and businesses. The reason for this, as is stated above, is that the form of the lending that a business asks for may be the reason for the decline and changing that form may allow the bank to approve it.

Traditionally the overdraft has been the form of product that most small businesses have gone for in terms of funding day to day working capital in their businesses. It is simple and not very expensive in terms of interest and charges but is not secure and not flexible which are the two downsides. As lenders have reshaped their own businesses after 2008 both in terms of those businesses they want to focus their attention and selling on, and in terms of the products they offer, lenders will now try in many cases to move businesses to invoice discounting in its many forms as an alternative to overdraft.

Historically, many small businesses have had issues with invoice discounting due to its cost but primarily I think that their view was that lenders only offer it to 'companies in trouble' so it will taint them. However on the plus side, it is certain and flexible and can grow with the business in many cases.

I have spoken to many businesses about their reasons for using it or not and I think the best reply came from:

a) a largish business who said that since moving to invoice discounting (which all their blue chip customers are aware of) they have been able to grow their business in a better and more certain environment. This specific company bids for large logistics contracts with large corporates and invoice discounting allows them to price tenders more effectively as they know exactly when they will receive cash into their account from invoices sent so can price the 'cost of finance' element in the tender precisely which would not be possible in terms of overdraft.

b) a family business of many decades who wanted to increase their credit to underpin growing sales but decided that at their time of life personal or property guarantees were not something they wished to do so were happy to pay the little extra that invoice discounting cost to replace their overdraft which had conditions that did not suit them. Now some years on from that decision they are content they made the correct decision and it has just become a normal part of their business.

Many other customers' views on invoice discounting have changed and they now see it as a legitimate form of financing for any business, not just ones in trouble, and, while its cost still remains higher than overdraft, generally it is easier to operate and the encumbrances attached to it may not be as exacting as those attached to an overdraft.

However it continues to get bad press sometimes due to the wide number of operators involved in it and the misdemeanours of some of them. That may be the explanation whilst the total numbers of businesses using invoice discounting is still incredibly small at around the mid 40,000 which in terms of all businesses receiving credit is very small[4].

I am not advocating one over the other as circumstances will dictate what is best but am advocating that more businesses consider other lending products perhaps more than they do and that banks make their use and benefit clearer to customers.

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[4] http://www.abfa.org.uk/statistics/ABFA%20Quarter%204%202012%20Statistics.pdf

4.8 Understand how credit scoring operated and what could be done to make its impact better or more understandable to businesses.

This was a key issue that I raised in last year's annual report as failed credit scoring was, and still remains, the main reason for businesses being declined so if we could resolve or help this issue then declines should reduce.

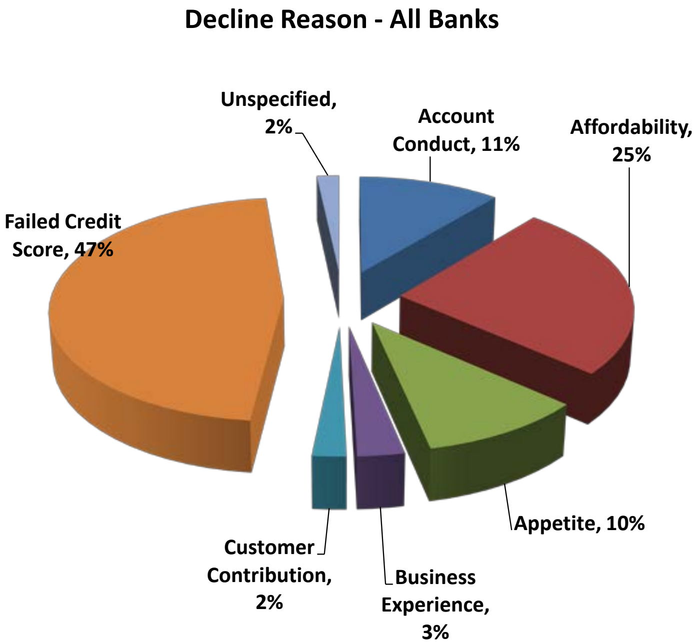
Let me say though at the outset of this section that performance and credit scoring of business customers has been used for more than 20 years in the UK. Lenders have always worked on the premise that the personal and business finances can be intrinsically interlinked. Therefore I don't see it necessarily as unfair that personal creditworthiness can affect the decision to lend to an unincorporated business. However, it would certainly be helpful for both bankers and customers to have a better understanding of Credit Reference Agencies (CRA) and to communicate lending decisions better where credit scoring is used.

Having spent a lot of this year pursuing this, it is not as simple an issue as it would appear and is many facetted but I am pleased to say that we appear to be making progress on all parts of this so I will try and take them one by one.

Firstly and key this year is the amount of data we have collected has grown so we have been able to dissect the data better and look at sections of it more closely.

Below is the overall chart that shows the reason for decline

<u>Table 2</u>



Failed Credit Score at 47% is by far the biggest category, and if you split further by start-ups (*54%)* and those switching banks *(53%)* it is even starker.

When you split that by size of lending at £25,000 in any form, below which is where unsecured credit, and also the Consumer Credit Act, which has its own strictures, applies then a different picture emerges.

Table 3

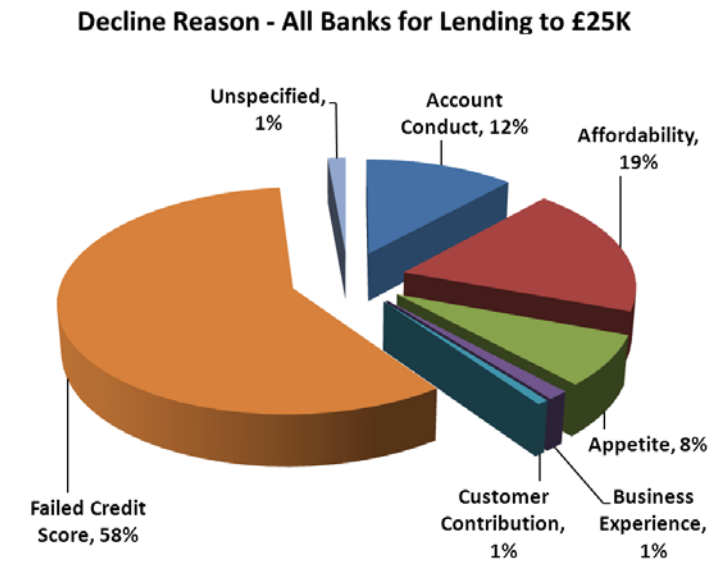
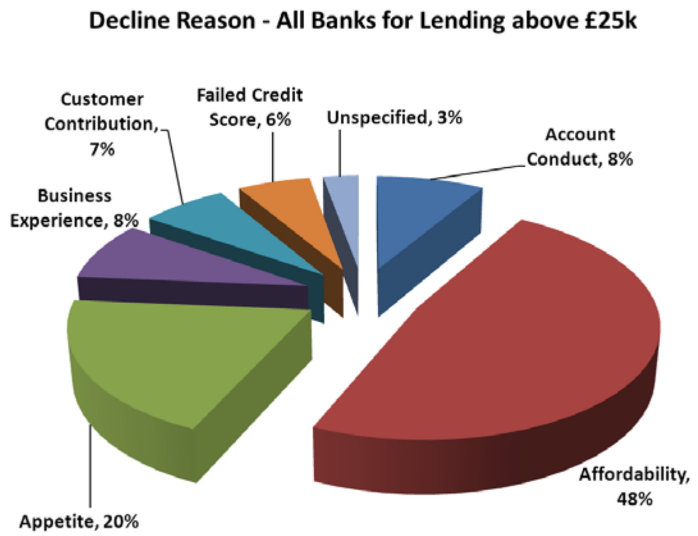


Table 4[5]



What can clearly be seen is that once lending gets above £25,000 failed credit scoring is not the prime reason for decline and it moves to the more specific areas of affordability where a better and different conversation can be had with customers.

[5] NB: All Credit Card applications are below £25k and are therefore excluded from this table.

There is also a marked difference when you look at product type and the chart below shows lending without credit cards.

Table 5

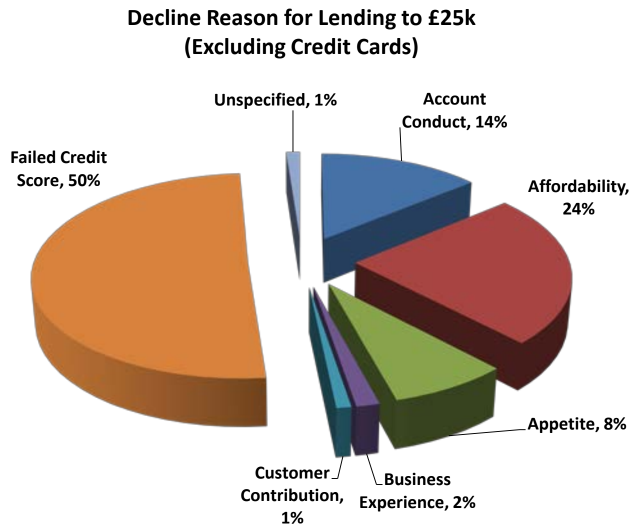


Table 4 highlights even more strongly the difference in decline reasons once you get above £25,000.

All the above has focussed my discussions and solutions around credit scoring at lending under £25,000 and on credit scoring that applies to all forms of lending under that but especially that through credit cards.

We know from all the research that has been done over the past decade from many sources that credit cards, either personal or business, remain the main source of working capital finance for micro businesses. While the research varies a little it would be safe to say that it is estimated that over 80% of funding for micro businesses comes from credit cards of some sort. My role only covers business credit cards so all that comes after this focusses on this but I have no reason to believe that it will be any different for personal credit cards which micro businesses use to fund their businesses as well.

Before coming through to credit cards specifically let me look at lending in general under £25,000 but specifically at that to non-registered business i.e. non Limited Companies. A vast number of businesses exist as sole traders, partnerships, or other forms of non-registered business where the lender in effect lends to the owners as there is no legal entity other than them to lend to.

They therefore fall within the bounds of the Consumer Credit Act and all that brings with it. The Consumer Credit Act which in part came from the UK but is also now guided and informed by The Consumer Credit (EU Directive) Regulations 2010 which was established to protect consumers from becoming bound to lending or credit that they either could not afford or on reflection did not want.

In broad terms, below are the basic boundaries within which it operates.

a) The Amount - It is currently fixed at £25,000 but the expectation is that this might be amended upwards in the future but timing is an unknown.

b) Products Covered – any borrowing on a specific account and covers loans, overdrafts, credit cards, and charge cards.

c) Those In scope – Individuals and since 6th April 2007 this includes sole traders, partnerships with three or fewer partners, trustees and unincorporated bodies such as clubs and societies.

d) Those Out of Scope – corporate bodies (limited companies and limited liability partnerships (LLPs)) and unincorporated partnerships where there are four or more partners.

It has grown in its scope and intensity over the years but below is how in essence it sees how consumers should be judged by lenders.

"*Creditors are required to assess the borrower's creditworthiness before granting credit or significantly increasing the amount of credit. The assessment must be based on sufficient information, obtained from the borrower where appropriate, and from a Credit Reference Agency where necessary.*"

Creditworthiness has always in essence meant the person's ability to repay the money borrowed in whatever form.

Post the 2008 crisis, it was enhanced with clauses on Irresponsible Lending and additional Guidance was issued.[6]

Annexe G highlights specific sections from that long guidance leaflet 'Irresponsible Lending – OFT guidance for creditors'[6] which show what lenders are now supposed to do to ensure that borrowers can afford to repay lending. Some lenders have turned these into affordability calculators which they use to satisfy the OFT guidance. This methodology also inevitably involves some form of personal credit scoring as it looks at the person and not the business in its widest form. While there are differences across the banks on how automated that process is, and whether it is a straight decline or refer, personal credit scoring is a key influencer in the decision.

It also means non-registered businesses are caught within the Consumer Credit Act and can be assessed the same as consumers and while many items that you would use to judge a consumer are the same for a business some are not. This does lead

[6] http://www.oft.gov.uk/shared_oft/business_leaflets/general/oft1107.pdf

sometimes to businesses being judged harshly or where they automatically get excluded before a proper exchange can be had. This is especially true for credit cards and other small lending methods which can be applied for on line with certain lenders.

This means that in many cases, and especially for start-ups who may only require small amounts of credit to assist in forming their business that it is the individual who is judged first and not the business. It follows that if the individual fails the credit check then the business may not even be considered.

A good example of this was a Sole Proprietor who was in the process of setting up a new business in the Accommodation and Food business sector. They had requested an overdraft facility of £20k and the Bank had declined the lending request due to a low credit score. It transpired that the reason for that was that the customer had purchased a new car some months prior which had been funded through a finance broker who had conducted numerous credit searches which adversely affected his credit rating. On review of the appeal the Bank agreed to provide financing but this shows the impact that events in your 'personal' life can have on your ability to gain credit for your business. This also was totally unknown to the person applying for the overdraft.

It is not just me that sees this issue as potentially unfair to small businesses but also some lenders themselves but, with even more focus on regulation and compliance now being a key part of what lenders have to do, it is difficult to see how this can be changed without a real shift in the way it operates. Also it occurs in the part of the stratified structure that all banks operate, in terms of Relationship Managers and differing size of businesses, where:

i) there are the lowest turnover or borrowing businesses

ii) the Relationship Managers have the most customers to deal with

iii) they could also be the least experienced in terms of lending

It makes it therefore even more difficult for Relationship Managers to be anything other than reactive with customers, other than in special circumstances, so the issue for the non-registered businesses is further compounded.

However let me be clear and say that I am not criticising the way that banks stratify their businesses and allocate customers to Relationship Managers depending on their size as there is no other way economically to do it, and in fact it only reflects the way that all business stratify their customer engagement in terms of how much a customer 'buys' from them.

This above situation with OFT and the Consumer Credit Act has been highlighted by both myself, other lenders, and indeed some of the Trade Associations that represent unregistered businesses and it is hoped that with the switch from the OFT to the new regulator for this area namely the Financial Conduct Authority (FCA) that changes can be made to guidance, or better still have a different set of guidance for unregistered businesses which split them from consumers generally in terms of lending.

It is my intention early in Year 3 to meet with the new Regulator to discuss these issues and see what can be done.

Turning now to credit cards specifically, they are the second biggest lending form within the Appeals Process. They account for approximately one third of all the appeals we receive but currently have 57% of those appeals overturned when appealed. However in terms of value of lending, credit cards account for only about £1.1mn (4%) of the total value of all appeals overturned showing the low amount of credit being asked for per case. They are also the most automated of all the lending forms in terms of application and approval and use credit scoring as an integral part of all approvals.

Credit cards we believe are also the product with the most targeted and heavy marketing by some lenders which has resulted in an increase of applications as a result.

Throughout the last year we have spent much time with the major commercial credit card providers discussing how their process works. From the high level of appeals and overturns we see the majority are overturned after the gaining of extra information which could have been gathered originally. Therefore I am pleased to say that we are now seeing changes in how the major credit card lenders operate in terms of:

a) Referring rather than declining some applications before formal decline which allows those extra bits of information to be collected earlier and in many cases then approve the lending.

b) In general change their decision systems to gather more information before they make any decision at all.

We have started to see already significant changes in the number of declines and appeals due to these changes and the overturn rate is dropping as well. Therefore while I always will expect to see appeals and overturns for credit cards being at the top of the list of lending forms, due to the mainly automated way that the system operates for what is in essence a volume product, I would expect to see the overturn rate decline which will bring the overall decline rate down as well.

If action is taken on the OFT issue and the major credit card providers tackle the issues discussed above then we will already have tackled some key issue in credit scoring.

However, it still leaves the basic concerns that I had when this issue become apparent last year, namely:

a) How much do people actually know about credit scoring in terms of how it is applied for business lending?

b) In terms of start-ups or unregistered businesses that are new to a specific lender do they understand that it is them as individuals as much as their business that is assessed?

As I have talked to businesses, Trade Associations, Government officials, and indeed Relationship Managers about this topic over the last year it is clear that all share the same concerns.

It is worth being clear what we mean by credit scoring in this context. All lenders use some form of credit scoring in assessing any lending and in general terms I have no issues at all in the way that the bank compiles their own scores themselves as they constantly monitor them. However, in some instances, concerns can arise where personal credit scores are combined with business credit scoring or used in isolation to make decisions on un-incorporated businesses without further screening or information being added.

The good thing about this last year is that everyone, including the Credit Reference Agencies themselves, agree that there is an issue here to resolve and we have made good progress in doing so, of which I hope to see the impact in the coming year.

The main area that we have all focussed on is education, mainly for customers, but also for Relationship Managers where it plays an important part in what they do. There are issues around consistency and accuracy of data but without education any solutions that were found to those would have only minor impact.

I highlighted above an example of a person being turned down for business credit due to numerous credit checks being done unbeknown to him by a third party in the purchase of a private car. There are many others I could give but also there is the basic lack of understanding about the relationship between them as people and them as their business.

I think the example that I most recall is the case of someone from Eastern Europe who had come to this country recently and wanted to borrow a small sum of money to help her finance her hairdressing business. The person could not understand how judging her as a person – which would always be negative at this time – had any bearing on her ability to be or run a good business.

All lenders do have leaflets and information that can now be provided to customers which say how banks make their decisions in terms of credit scoring but they tend to be long and legalistic and not ones that small business would readily understand.

Therefore working with the banks, the Credit Reference Agencies, the Trade Associations, and Government the banks have produced a new simple leaflet (Annexe H) which we hope will be given to all new businesses seeking to gain credit from a lender before they apply. In simple terms the leaflet will help to inform them that getting themselves credit worthy is as important as getting their business plan credit worthy. It will highlight some simple things that they can do to make that happen and importantly what is likely to make them 'fail'. The main purpose is to make new businesses coming to a bank think about what they need to say if they know that the bank will find things out about them as an individual when it conducts a credit reference search that might make the bank decline lending to them.

Raising awareness on this is to me the key factor, as from all the businesses I have talked to, not many of them had factored this in to their thoughts. From the declines we have looked at and the appeals from them it is clear that a significant reason for a new business not getting funded is a personal issue with the business owner and nothing to do with the business itself.

For instance, during Year 2 we reviewed over 1700 appeals and of these adverse CRA data was one of the component parts in the banks reasons for declining the application for lending in approximately 15% of the cases. Review of the appeals, where adverse data was a factor in the original decline, resulted in an overturn in favour of the customer for just over half of these cases (54%) which was due, in part, to the materiality of the adverse data. This helps to reinforce the fact that it is worth appealing and better still if the customer is already aware that such issues might potentially impact their application for lending that they discuss this with the bank at the outset.

It is the relevance of that adverse consumer data to the business credit decision that, in many cases, is critical and many of the overturns in this area have come as a result of a re-examination of that relevance and have been overturned.

However given that it is difficult to find meaningful information easily on unregistered businesses it is not a criticism of the way that banks operate. The person or business owner leading the business is the only item to follow or track in credit terms. With registered business there is a company number which can be tracked which can build up a much wider and better picture of the business which is not possible for unregistered businesses and having looked at this long and hard there is not an easy answer to find a similar thing to follow for unregistered businesses.

I do feel that if all the banks, Government, and Trade Bodies push and distribute this leaflet, and the reason for it, hard over the coming months then I hope it will have a significant impact on appeals to banks and also importantly on developing better on-going relationships between banks and their customers which leads neatly into the final issue identified in last year's report.

4.9 Continue to encourage more and better dialogue between a business and its bank.

Within the above short phrase lies the best outcome to all that we and others do in the Appeals Process can achieve.

If business and lenders can establish a better way of talking to each other, explaining what they need and why, then we will all move to a better place.

In my own view one of the greatest outcomes of the whole Appeals Process to date has been to increase this dialogue which has to happen when an appeal is made. This is not just in terms of those appeals that are overturned but also with those that are not, as in many cases that we have seen it has created a better understanding of the reasons why it was declined on both sides, which will lead to further lending in the future.

A simple example of this was an existing customer who had been the Bank's customer for 18 months, had asked for an overdraft facility of £10k. The Bank declined this request due, in part, to poor account conduct as the customer had been going overdrawn on their account without having an overdraft facility in place. However, from the Customer's perspective they had thought this was OK because their Relationship Manager had been approving the overdrafts each time so thought they were doing the right thing. Review of the appeal highlighted the fact that the company had recently taken on a new business contract and wanted to have a formal rather than the ad hoc overdraft facility in place as a safety valve under the new contract. On review of the appeal the original decline decision was overturned in favour of the customer. The Relationship Manager by not organizing and discussing the issue better and more formally through the times that they had gone overdrawn without permission had given the customer the wrong impression so a situation was created that could have been avoided.

We highlighted in last year's report that better dialogue is enhanced by the Relationship Manager themselves taking more corporate ownership of the decline decision and not relying on the 'computer' or 'credit committee' as an easy way to tell the customer why they were turned down. I am pleased to say that there is evidence that all the banks are in differing ways trying to make sure that happens and part of that has been our insistence that the Relationship Manager's actual conversation with the customer on decline or appeal, mainly as a written record of the key points discussed, is recorded so that others can see what is said. All the banks have embarked on this process and I believe this will have a big impact over time on the customer and bank dialogue.

Also, as I highlighted earlier in this report the majority of the banks are looking to make their decline letters simpler and more understandable so that again it encourages the customer to both read them and then also ask questions of the bank in terms of what they can do to make the reasons for decline not be in place the next time they come back for lending. Banks like all of us nowadays worry about what is in letters so they can be legalistic so we think that this move towards better and simpler letters by some is best practice that all should follow.

Finally, in this section there is one issue that does and will continue to get in the way of this better dialogue especially in the strata of Relationship Managers that deal with small businesses.

To have a better dialogue probably means that you have to devote more time to having that dialogue with the customer. No one disagrees with that, but acting against this is the increased compliance that we have noted that increased regulation on the banks is causing to Relationship Managers.

We are all aware that banks have been more heavily regulated post 2008 both on prudential and conduct matters. This means that to be seen to comply with regulatory requirements banks now keep more complete and detailed records of all transactions, conversations, etc. that go on between them and their customers. This means that their records have to be up to date and precise so the amount of their time Relationship Managers have to give to compliance has increased. Since 2008 the amount of time Relationship Managers spend on compliance is estimated to be at least 50% above what it was pre 2008. This is not to say that banks and Relationship Managers should not do this, but is to point out that the increase in compliance does mean that the time for dialogue between Relationship Managers and customers will have declined. This makes it even more important that we get that time used to its maximum advantage for both parties.

5. Auditing Practices in Year 2

In setting out how we have audited the Appeals Process which the individual banks put into place, it is worth remembering that no one had ever done this before in the way that was being proposed. I had also to make sure that I was delivering a robust and sound process that would be beneficial for the SME and for the banks.

As I mentioned in last year's report, there is not one single process that can be applied to all banks. Each bank enables its customers to access business finance in several different ways, including: telephone; on-line; through local Relationship Managers; and specialist lending units. The size and type of the lending product being sought also creates differences in approach to which the standard principles of the Appeals Process have been applied.

The review team, which currently comprises eight members of staff, has established a robust and methodical approach to its work over the last two years. The team has a broad base of experience in various parts of financial services with an emphasis on business lending, customer file reviews and banking regulation. They have demonstrated independence throughout their review work, including the ability to challenge the banks on matters relating to specific case files as well as wider issues relating to process and approach. As last year, the review team has continued to discuss various aspects of the Appeals Process with the TFBs and made recommendations, after each visit, to the individual banks about areas which may benefit from process changes and improvements as well as discussing key points on specific cases including appeal outcomes. The banks have responded positively to suggestions for improvements and in some cases, this has involved substantial investment in business and IT process change.

The experience gained from reviewing over 900 individual loan files in Year 1, enabled the independent review team to confirm the effectiveness of their approach and to make refinements where appropriate. For Year 2, I concluded it would be appropriate to allow the banks themselves to fill in the Appeal forms on a monthly basis and allow my review team to visit the banks on a quarterly basis and audit a sample of the forms received against the original lending files to confirm accuracy. In addition, where the number of appeal cases was high, the review team visited the relevant bank on a more frequent basis. This has generated a detailed dataset on just under 54% of the total number of Appeals received by the banks during the year. My review team audited and reviewed, through a continuation of the on-site visits, just over 1000 appeal case files during the year.

As last year, the review team have continued to make recommendations, at each visit, to the individual banks about broad areas which may benefit from process changes and improvements as well as points on specific cases. The banks have responded to suggestions for improvements and in some cases, this has involved substantial investment in business and IT process change.

The standard of form completion by the banks as verified by our auditing of over 57% of cases received (and including some additional data from case files reviewed and completed by my audit team) was sufficient to rule out the need to undertake additional on-site visits. The on-site visits also provided the review team with the opportunity of holding face-to-face discussions with the staff at each bank handling the appeals cases, together with their management. Feedback to each bank is given at the end of each site visit and, with the benefit of more case data, it has been possible to draw clearer conclusions about key areas on which focus is needed.

The approach to sampling of cases continues to focus predominantly on those cases where the bank has overturned its original declined decision. For each bank, we receive detailed data on between 25 and 30 appeal cases each month throughout the year. In instances where a bank may receive less than 25 cases per month, we receive data on 100% of those cases. The on-site reviews every quarter will allow us typically to audit between 35% and 40% of the forms received over the three month period for most of the banks. The charts and tables shown elsewhere in this report demonstrate how the large volume of data we now have provides for a strong picture on important issues such as the reasons for decline.

I also have tried to look at other similar Appeals Processes elsewhere and see how we could learn from them. I now meet regularly with John Trethowan who has a similar role to my own within the Appeals Process in Eire. While there are differences between the roles and processes to suit the business and political environment they operate within many of the issues we are discovering are the same. One of the differences between my own role and his is that he publishes a short quarterly report on progress. I have been reflecting on this and given the large amount of actions that will emanate from my report this year and the need to look at how certain issues for example around credit scoring, and awareness are going I have decided for at least this year and next to produce a short quarterly report to update on how things are going. Given that this report is just being reported now and contains much of what has happened in the first quarter anyway my intention would be to publish my first short report in late October and then three monthly thereafter.

6. Key Numbers for Year 2

Before going into the detail of the Year 2 numbers it is worth repeating what I have stated earlier in this report is Year 2 numbers cannot really be compared to Year 1 numbers because of a number of reasons. These include:

a) That it was not really until 6 months into Year 1 that all the banks involved in the process were up and running on the same basis, as while all banks offered appeals from the first day that the Appeals Process started we had to work with each to ensure that the process fitted into the independent auditing process that we required for assurance.

b) Appeals on credit cards were one of the areas that took time in Year 1 to get up and running and since their overturn rates are higher than the norm last year's overturn rate was probably understated on a full year basis.

c) Some banks this year based on analysis and input from us in terms of how and when they make decisions have changed the way they operate which has both reduced declines and overturns.

d) Some banks are now referring more initial declines for further review before making a decision.

Therefore, with that large health warning, total appeals for Year 2 were 3311 with an overturn rate of 39.2%. However, as is stated in the Executive Summary of this report this yearly average masks a decline in recent quarters from 53% at the end of the first quarter of year 2 to 37% at the end of the final quarter of year 2 as the changes of processes that banks have now put into effect begin to operate. I expect to see that decline continue over time.

Also, since, as I have explained many times in both this year's and last year's report, banks operate differently trying to compare market share figures of lending which some banks publish to appeals or declines numbers is not worthwhile as they do not correlate in any substantive way.

Over the two years this now gives us total appeals of almost 5500 and a total value of overturned appeals, based on cases for which we have detailed data[7], of in excess of £28mn. While we cannot just gross up this number pro rata as the cases we have full data on are not necessarily evenly taken from across all customer types or lending levels I can safely say that at the end of year two of the Appeals Process it has put more than £30 million back into the UK economy in terms of business

[7] Out of the total appeals of approximately 5500, we have captured detailed data from the banks of around 2700 cases, including a majority of those overturned in favour of the customer.

finance for SMEs that would not have been there had the Appeals Process not existed.

Given the large number of data sets we now have we can start to look at the data more exactly and in more detail. At the high level this means now that we can split the data into appeals including credit cards and appeals without it.

Before we get to that we need also to reiterate the more general bank numbers we used in year one.

The independent SME Finance Monitor undertakes 5,000 interviews of SMEs each quarter. Results for 2012 found that, in the twelve months leading up to SMEs being interviewed:

a) Some 7% of SMEs had applied formally for new overdraft facilities and 11% had their existing facility automatically renewed and, across those combined categories, 90% of SMEs ended up with the overdraft they needed. Of those applying for new facilities (some 316,000), 75,000 had applications declined.

b) Some 4% of SMEs had applied formally for a loan. 57% ended up with a loan and 9% took alternative funding, but of those applying (some 162,000), 55,000 had their application declined.

Data collected directly by the BBA from the Better Business Finance banks show that in the year to end-Mar 2013, 735,000 applications were received for credit products (loans, overdrafts, credit cards, asset-based finance, etc.) which were eligible for appeal, should they be declined. This applications total was 11% down on the previous review year, but the approval rate (86%) and decline rate (14%) were unchanged. Of those applications declined, approximately 3% were taken to appeal.

Returning now to the split of the data between appeals with and without credit card data the chart below sets out the data for years 1 and 2 in that format.

Table 6[8]

Appeals - April 2011 to March 2013	Year One	Year Two	Total
Total No. of Appeals Received (ALL BANKS)	2177	3311	5488
Total No. of Appeals Overturned (ALL BANKS)	860	1298	2158
Overturn rate *(based on Appeals Received - ALL BANKS)*	39.5%	39.2%	39.3%
Total Value of Appeals Overturned *millions*	£10.0	£18.5	£28.5
Total No. of Appeals Received (Excluding Credit Cards)	1587	2146	3733
Total No. of Appeals Overturned (Excluding Credit Cards)	518	634	1152
Overturn rate *(based on Appeals Received - Excluding Credit Cards)*	32.6%	29.5%	30.9%
Total Value of Appeals Overturned (Excluding Credit Cards) *millions*	£9.7	£17.7	£27.4
Total No. of Cases Reviewed	946	1777	2723
Total No. of Cases Reviewed/Total No. of Appeals (as %)	43.5%	53.7%	49.6%
Total No. of OTurn Cases Reviewed/Total No. of Overturn Cases (as %)	49.5%	62.9%	57.6%

The above table does show that even given all the caveats about not comparing the data on a year on year basis I do feel that appeal numbers have increased in total and also that overturns are going down, as the quarterly figures for Year 2 reflect with a drop from 53% to 37% over the second year. This can be highlighted even more in overturns excluding credit cards where the overturn rate has fallen from 32.6% to 29.5% between the years. By next year's annual report I would expect to see further declines in both the total overturn rate and for that excluding credit cards.

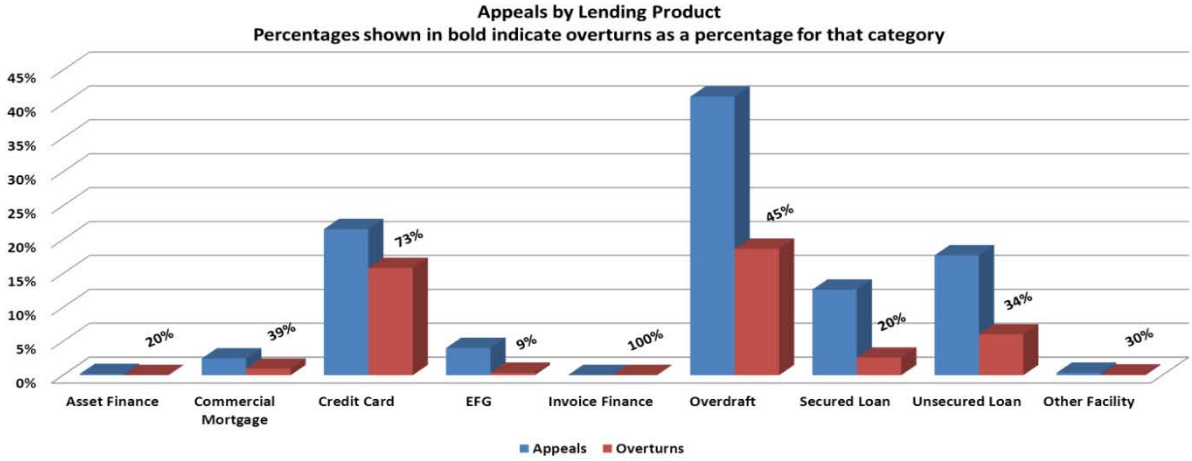
I have been asked many times what I think the overturn rate should be and answer the same way each time which is 'There is no one number and will depend on the type of lending product, the size of lending, and type of customer'. All I would say is that as the size of lending amount rises and the size of company gets bigger so we see a fall in the number of appeals. This is what would be expected given that in these areas we would expect the understanding and knowledge of the customer on lending practises to be greater, and also the interaction between the customer and the bank to be more regular. Also, as we say elsewhere in the report, it is also affected by how automated the process is. While I said in last year's report that all the banks involve a human being in most of their decisions (except those done on line for specific products) the impact of the human intervention varies considerably and often

[8] For Cases Reviewed we mean cases where detailed information regarding the actual appeal is known to us. Overturn means an outcome decision to lend to the customer.

it is reactive, e.g., to a lack of information or adverse credit score rather than being proactive also in seeking further information.

In terms of overturns the difference in overturn rate by product type is highlighted in the table below.

Table 7



As can be seen (with the exception of invoice financing) credit cards have the highest overturn rate followed some way behind by overdraft, and then loans. The percentage for other forms of lending, where the total number is small, is not as meaningful. This is further highlighted when you look at overturn rates by size of lending.

Table 8

Appeals by Size of Lending Request – (Apr 2011 – Mar 2013)

Size of Lending Requested	Total Appeals	Overturns
≤ £10k	62%	35%
£10k < x ≤ £25k	17%	6%
£25k < x ≤ £50k	5%	1%
£50k < x ≤ £100k	5%	1%
£100k < x ≤ £250k	6%	1%
£250k < x ≤ £1m	4%	1%
x > £1m	1%	0%
All Lending	**100%**	**45%**

The above table again highlights that the more the lending moves above the £25,000 level and away from the areas where lending is either all or partially judged on a credit scored basis then the overturn rates fall. If the overturn rates at the higher levels of lending were at the rate of the lower bands then I think I and everyone else would have a concern that there was a basic flaw in the way banks makes decisions on lending. However even at the higher amounts of lending it is not perfect, as it never has been, and it is good to see that both customers and banks in these higher lending areas both will appeal and in terms of the banks overturn decisions which I believe shows that the appeal is being judged independently within each bank.

The above is further highlighted when overturns by size of company is analysed.

Table 9

Appeals by Size of Customer Turnover – (Apr 2011 – Mar 2013)

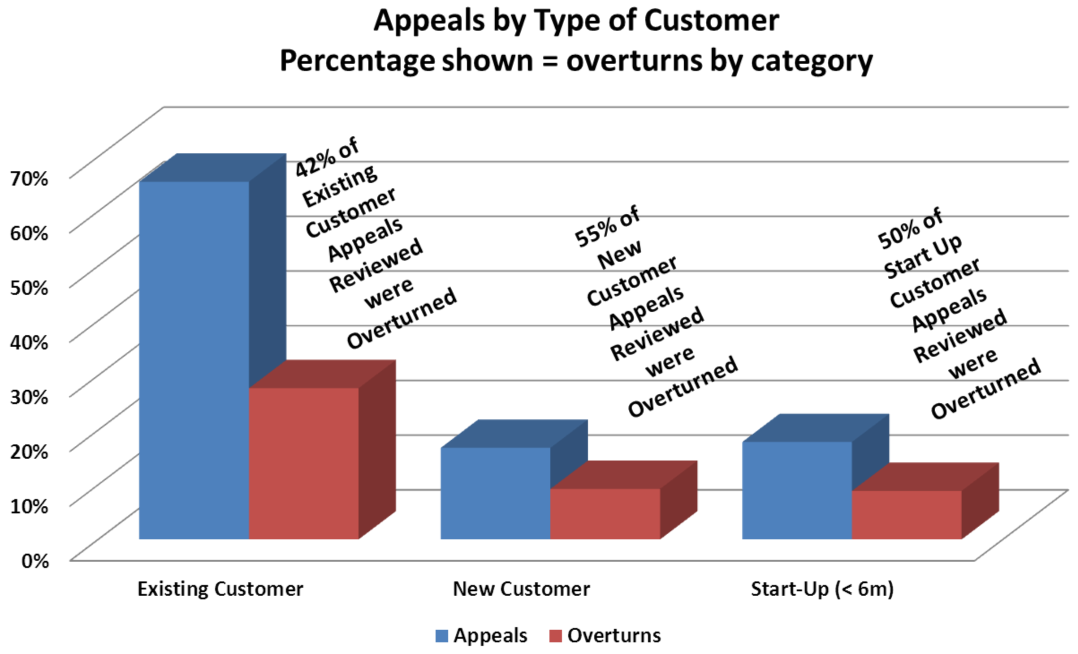
Customer Turnover	Total Appeals	Overturns
£0 < x ≤ £100k*	52%	24%
£100k < x ≤ £250k	23%	10%
£250k < x ≤ £1m	19%	9%
£1m < x ≤ £5m	5%	2%
x > £5m	1%	0%
All Lending	**100%**	**45%**

**Includes appeal cases where turnover is unknown*

Again this highlights the need for better dialogue between businesses and banks and the need for both parties to understand and make the time to do that. Given that both will always find that an economic challenge to do in terms of the time they would wish to devote to it, other ways of making that dialogue better must be found which is why simpler communications through decline letters and the credit scoring leaflet are needed to make the time that is available from both more effective.

In terms of customer types again the point made elsewhere in this report are highlighted.

Table 10



Since start-ups and new customers tend in general to be smaller customers or borrowers of small amounts the higher overturn rates by both of those again highlights the need for better understanding of the issues highlighted elsewhere in this report.

In section 4.8 on credit scoring the differences in decline reasons are highlighted.

Table 11

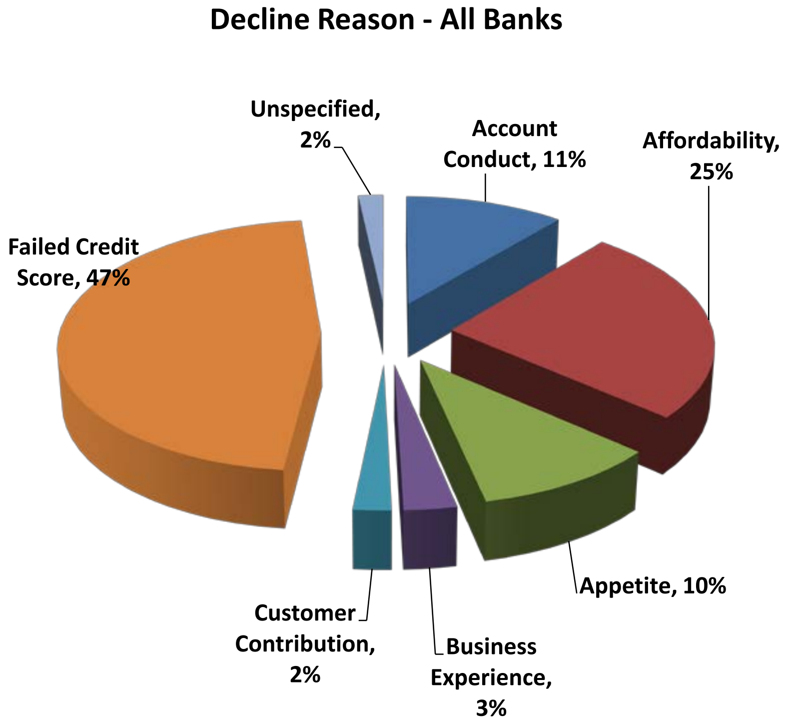
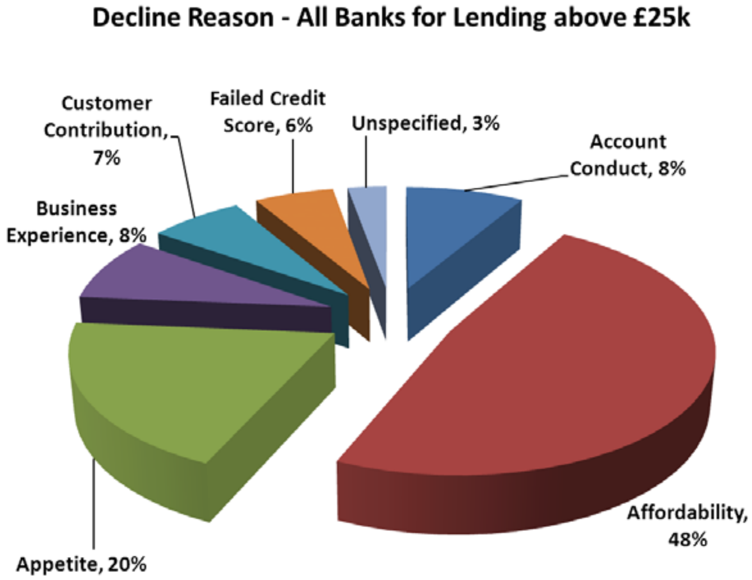


Table 12



The above two tables highlight the differences that exist across the levels of lending with the first chart showing that for all the appeals the top four decline reasons are:

For Table 11 - All Lending:

Credit Scoring	47%
Affordability	25%
Account Conduct	11%
Appetite	10%

When those looking for credit below £25,000 are excluded, the picture total changes and the top four are

For Table 12 - Lending above £25k:

Affordability	48%
Appetite	20%
Account Conduct	8%
Business Experience	8%

The above two charts highlight better than any other the difference in the way lending is assessed for small and other businesses where affordability has to be judged, partially due to the regulations governing the Consumer Credit Act, in a different and more automatic way which uses data that in part will come from outside the bank.

I am not concluding that this is wrong or that there is a better way in the economic and regulatory model that banks have to operate within today, but it does focus where a lot of my work in Year 3 will be directed. However I would repeat that the economic model that a bank uses in dealing with its customers is very similar to any manufacturing or other business in the UK or indeed anywhere else in the world.

7. Key Priorities for Year 3

In terms of priorities for Year 3 the majority will be continuing to progress many that we have already identified but where the on-going focus remains important and these are listed below:

a) Getting the message on the Appeals Process and that it is working out to more SMEs and within the banks to more Relationship Managers both in terms of knowledge and understanding. This will involve everyone involved in the process - banks, other lenders, Trade Bodies of all types, Governments generally but also departments and bodies funded by them who contact businesses. I do think that a continuance of communication methods already used but across a wider range of bodies will assist greatly. I will also be looking for wider usage of other communication vehicles not currently used e.g. Trade Journals, Conferences etc. It also means looking at how all parties involved beyond the banks (Trade Associations and Government in its widest sense) can use their networks to increase the flow of businesses appealing

b) Work with Governments in all parts of the UK, with the BBA and banks, to ensure that SMEs have access to the type of support that they need to help them understand what lenders require from them in this new environment.

c) Spreading of best practice across the banks. While I accept that banks do operate differently there is learning and ways of working that can be used generically and where it has proved to work for one I will be pushing, for that to be replicated elsewhere where appropriate.

d) Progressing the work on credit scoring across various avenues.

   i) I will meet with the Financial Conduct Authority[9] (the new regulator for Consumer Credit) to see what can be done to make the difference between business and consumers more exact and allow lenders to make decisions on both appropriately. To be clear I am not suggesting new legislation but perhaps better or more exact guidance to highlight the different decisions lenders may make to a consumer and an unregistered business.

   ii) Get the new educational credit scoring leaflet out to as many start-ups and others seeking small amounts of business lending so that they are better prepared when approaching lenders.

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[9] www.fca.org.uk

iii) Continue to work with the credit card lenders and others where credit scoring is the major factor in deciding credit to ensure that their processes allow for the collection of sufficient information before a lending decision is made.

iv) To work with Companies House and HMRC to see how that can become part of this overall dissemination of information process.

e) Continue to meet with as many Relationship Managers and customers as I can sensibly, to allow me to judge the impact all the changes above and below are having on 'the front line'.

f) Work with all the lenders involved in the Appeals Process to make sure that the Appeals Process becomes an embedded part of their day to day process and will continue as an integral and positive part of their business operations into the future.

g) Ensure that we have, as far as is possible, a uniform system in terms of what customers can appeal on across all banks. While this has moved closer over the last year not all banks are exactly the same for various reasons and we need to even that out further over the coming year.

h) Ensure that the banks achieve all the actions that I set out for them in their action plans for Year 3.

i) Begin in late October 2013 to produce short summary reports on the Appeals Process to highlight progress.

8. Appendices

8.1 Annexe A – Bank commitments

The Taskforce banks committed to 17 actions across three broad areas. To improve customer relationships we will:

1. **Support a network of business mentors** by working with the business groups to deliver this free service to small businesses across the UK
2. **Improve service levels to micro enterprises** (businesses with fewer than 10 employees and turnover or a balance sheet under €2m) by setting out in a new Lending Code the levels of service banks will provide and outlining additional sources of help and advice
3. **Publish lending principles** which clearly set out the minimum standards medium-sized and larger businesses can expect when asking banks for loans and other services
4. **Establish transparent Appeals Processes** for when loan applications are declined, with processes independently monitored by a senior Independent Reviewer, who will publish the results of their review, to ensure each bank has a fair and equitable Appeals Process
5. **Initiate a pre re-financing dialogue 12 months' ahead of any term loan coming to an end**, which will include a timely review of business and re-financing needs and an assessment of what needs to be in place ahead of loan expiry to maximize the prospect of successful re-financing.

To ensure better access to finance we will:

6. **Establish and invest in a new £1.5 billion Business Growth Fund** (built over a number of years) to fill a crucial gap in the market and provide capital for viable businesses which want to invest and grow
7. **Support the Enterprise Finance Guarantee Scheme**, seeking continued Government backing through to 2012, and accommodating any changes made by Government
8. **Help mid-sized businesses access syndicated debt markets** by raising customer awareness, training customer-facing staff and engaging more actively with business groups and customers
9. **Improve access to trade finance** through targeted SME awareness-raising campaigns and exploring possible regulatory adjustments with the FSA. Seek to open with Government access to trade finance products for businesses that qualify for the Enterprise Finance Guarantee Scheme
10. **Signpost alternative sources of finance**, giving customers helpful information and advice if a loan is declined and raising awareness about the financial solutions they should consider

11. **Help improve the supply of credit to the wider economy**, working with the authorities to ensure that wholesale markets can support the necessary lending capacity as the economy recovers.

To provide better information and promote understanding we will:

12. **Fund and publish a regular independent survey**, commencing in early 2011, to a methodology agreed with Government and business groups, so there is an agreed and authoritative set of data on business finance demand and lending supply

13. **Enhance the cross-industry lending dataset** by broadening the statistics on lending available for wider bands of business activity; on lending to deprived areas; and on national and regional data on the provision of bank support to business start-ups

14. **Hold regional outreach events** throughout 2011 with business groups to enable business customers and business groups to meet with key staff from the banks to answer questions and explain what services are available

15. **Improve customer information** including a review of literature and other materials, so customers can more easily understand what products will best meet their needs

16. **Host a dedicated website** through the BBA to draw together and link useful sources of information to help customers access the most appropriate information. This will also connect mentoring networks

17. **Establish a Business Finance Round Table** where senior representatives from the banks and business groups meet regularly to discuss and review trends, identify emerging areas of concern, ensure problems are addressed and facilitate the implementation of the Taskforce initiatives.

8.2 Annexe B – Monitoring & Appeals Process

Principles & Definitions

Background

In July 2010, HMT and SIS published a Green Paper- 'Financing a private sector recovery' which asked for proposals on how the UK can improve the banking sector environment to ensure businesses (in particular SMEs) are supported as the economy moves out of the recession.

The CEOs of "the Task Force banks" and the BBA took up the initiative, issuing a Business Finance Task Force report on 13th October 2010.

As part of the range of initiatives, the Task Force has agreed to institute an Appeals Process for business customers. The process is to be created within a standard industry framework appropriate to each Bank's structure and strategy. The objective of the initiative is to provide a credible Appeals Process that allows a Business customer to dispute a bank's actions if they believe them to be in breach of the Lending Code or Lending Principles. This can include having a finance application reviewed.

The Appeals Process is a voluntary code with external oversight rather than formal regulation – i.e. the role is not that of a formal statutory regulator.

The Process is to be implemented by the end of Q1 2011. It will also be embedded in a revised Lending Code and Lending Principles which are to be issued at the same time.

The Principles of the Appeals Process

At a high level, the Process will be:

- Transparent (i.e. promoted, communicated individually and disclosed as part of an annual report on total outcomes)
- Available to all business customers with a Group Turnover below £25m
- Carried out fairly and promptly
- Subject to an external review of the process- i.e. the External Reviewer
- All lending products to businesses are in scope

Customers will get the result of an appeal with an explanation of the findings, in writing.

The 5 UK Retail Banks of the Task Force- LBG, Barclays, HSBC, RBS and Santander- will be involved in the Appeals Process initially and it is likely that other Banks will then take up the Process over time. These standards will be published by the BBA through the BBA website, media briefings, etc. as part of the overall communications approach of the Task Force as well as by individual Banks.

The Appeals Process is to be launched at the end of 01 2011 and will be linked to the launch of Recommendation 2: Better Service Standards for Micro Enterprises and Recommendation 3: Lending Principles for Larger Businesses.

The Coverage of the Appeals Process

- **Customers in Scope:** Most banks operate separate support and recovery departments to provide intensive management support to help businesses who are struggling to avoid failure and to prevent recourse to the legal recovery process. These are structured in different ways at each bank and on that basis we propose that the Appeals Process is out of scope for businesses that are managed within a 'special support' or 'recoveries' unit.

  Any customer where the formal recovery process has commenced; i.e. formal demand for repayment has been made, will be out of scope for appeals because they will be ineligible for further lending and so the lending Appeals Process will not be value adding.. When things don't work out as planned, it can quickly result in the need to appoint administrators or, in extreme cases, liquidators. Speed is often of the essence here to protect the creditors and the employees of the company.

  Applications declined due to breach of regulations/Government/AML factors/Sanctions will not be a part of the Appeals Process.

- **Products in Scope:** All lending products to businesses.

The Definitions of the Appeals Process

1) External Review

A review team independent of Banks and the BBA Task Force has been formed to meet the Principle of the Process being "Subject to review by a senior industry independent authority." The main elements are:

a) "Lead" Reviewer

The Lead Reviewer will ensure an annual review of the Appeals Process is undertaken. On production of the annual Review report (see below) the Lead Reviewer will act as the public face of the Review team in discussions with Trade and Government bodies supported by the Operational Review team and the BBA. The role will focus on the factual outcome of the report. It will not engage in discussion or speculation on any other aspect of banking services.

b) "Operational" Reviewer

The Operational Review team will undertake an annual review of the Appeals Process **within** each Bank to ensure Appeals are considered in line with that Bank's Appeals Process as defined in the Principles & Definitions of the Appeals Process and meet the designated Quality and Service standards. There will also be consideration of the Appeals Process **across** Banks to ensure consistency of approach.

c) The Annual Review

A detailed onsite operational review will be undertaken annually. (In the first year, there will be a half- yearly review to ensure that the Process is "bedded down" in each Bank. On completion of this initial review, Banks will take the lessons learned from the Operational and Lead Reviewers from the first 6 months and refine their Process as appropriate).

The review will assess the overall effectiveness of each Bank's Appeals Process by reviewing the handling of individual Appeals against their defined Process using a sample of Appeals cases. The Reviewer will also consider Management Information provided by the Bank and, should they wish, speak to individual customers. The Review will also evaluate the Appeals Process across Banks to ensure consistency of approach.

d) Annual Report

The Operational Reviewer will produce a report of their findings to be agreed with individual Banks, the BBA and the Lead Reviewer. The Lead Reviewer will present the Report findings to Trade and Government bodies with support from the Operational Reviewer and the BBA.

2) Communication of a Declinature to the Customer and Appeals Trigger

An application is "in scope" when all relevant information enabling a decision to be reached has been expressly provided and the Bank is satisfied that the application is complete in order to progress to credit scoring.

The Appeals Process is only for declined applications: where a Bank has made an offer but the customer outcome with the relevant relationship centre and if still not satisfied, the customer will be directed to the Banks' internal complaints process

Applications declined due to breach of regulations/Government/AML factors/Sanctions will not be a part of the Appeals Process.

When a Bank declines an Application, they will communicate with the customer setting down:

- Reasons for declinature;
- Signposts to alternative sources of finance;
- That the customer has a right to appeal; and
- What the Appeals Process is.

3) How the Appeals Process will Operate:

If the customer takes up the right to Appeal, the following process will ensue:

a) Where **Automated Application Processing** involved and the Bank's lending criteria are not met, the process will operate as follows:
   i) The Bank will sense check the Application and also review to see whether any additional
   Information could be provided by the customer;
   ii) Where appropriate the Bank will work with the customer to achieve a favourable outcome.

b) Where **Manual Application Decisions** are made and the Bank's lending criteria are not met, the process will operate as follows:
   i) The bank will review the decision – including obtaining any additional information from the customer- using a "Four Eyes" principle;
   ii) The principle of a customer being able to appeal will similarly apply even where the original application has been declined by a credit panel consisting of a number of expert lenders;

iii) **"Four Eyes" criteria:**

(1) The original decision will be reviewed by another person (i.e. original decision maker + additional person = "4 Eyes")
(2) That person will be internal to the Bank
(3) That person will NOT have been involved in the original decision
(4) That person will be an experienced lender.

4) Appeals Timescales

The Customer is required to appeal to the Bank within 30 calendar days of receiving the decline from the Bank. If the appeal is beyond this timeline, the Bank will treat the appeal as a new Application.

The Bank is required to respond to the customer within 30 calendar days of receiving the appeal from the customer.

8.3 Annexe C – Minimum Standards

I. Completeness
1.1 Available to all business customers with a Group Turnover below £25m
1.2 Applicable to all business lending products
1.3 Businesses in support and recovery are ineligible to Appeal
1.4 Businesses in breach of regulations/Government/ AML factors/sanctions are ineligible to Appeal
1.5 Applicable to all formal complete credit applications
1.6 Only for declined applications where no offer has been made
1.7 Scheme launched on April 5, 2011
II. Transparent
2.1 Reasons for application decline to be communicated with customer
2.2 Signposting declined customers to alternative sources of finance
2.3 Eligible customers to be informed of Appeals Process
2.4 Appeals decisions to be communicated in writing with an explanation of findings
III. Fair
3.1 Automated applications to be sense checked
3.2 Automated applications to be reviewed in case additional information is required
3.3 Manual applications to be reviewed using "four eyes" principle. Reviewer will not be involved in the original decision
3.4 Reviewer will be an experienced lender
IV. Prompt
4.1 Customer required to Appeal within 30 calendar days of original application being declined
4.2 Bank required to deliver Appeal decision within 30 calendar days of receiving Appeal
V. Consistent
5.1 Basic MI to be provided including: Number of applications received Number of Applications Declined Number of Appeals Received Number of Appeals Overturned (in favour of the customer) Number of Appeals where Decline is Upheld
5.2 Relationship Managers to receive training to ensure awareness of Lending Principles and the Appeals Process

8.4 Annexe D – Appeals Case Review Form

PROMONTORY	PRIVATE AND CONFIDENTIAL FOR PROMONTORY, RUSSEL GRIGGS AND BANK ONLY			
Promontory Ref				
Bank Name	Any Bank			
Site/Location				
Month of Review				
Reviewed by				
Second Reviewer				
SECTION ONE	CASE SNAPSHOT			
Bank Appeal Reference Number				
Company Name				
Company Structure				
Nature of Business				
Business Location (Town, County &/or Postcode)				
Customer Type				
Business Start Date (MMMM-YYYY)				
Date Bank Account Opened (MMMM-YYYY)				
Company/Group Turnover				
Facility Type Requested				
Amount of Facility Requested (Please show "New Monies")				
Lending Product				
If more than one product requested please give details of amount/s and type/s				
Purpose of Facility / Facilities				
Details of any Existing Facilities with Bank				
SECTION TWO	APPEAL SNAPSHOT			
Access Channel				
Type of Application				
Date Application Submitted (DD-MMM-YYYY)		Evidenced		
Date of Decline Letter (DD-MMM-YYYY)		Evidenced		
Date Customer Appeal Received by Bank (DD-MMM-YYYY)		Evidenced		
Date of Appeal Receipt (if applicable) (DD-MMM-YYYY)		Evidenced		
Date of Appeal Outcome Letter (DD-MMM-YYYY)		Evidenced		

SECTION THREE	ORIGINAL DECLINE DETAIL	
Was customer declined all lending in this application?		
How was customer informed of original decline?		
By whom?		
Bank's reason(s) for declining the lending application Please select reason/reasons		
Bank's reason(s) for declining the lending application Free format (additional information)		
Was customer given reasons for the decline in the written communication ? Do these align with the reasons documented in the case file notes?		
Additional Comments / Explanation of reasons given in customer communication		
Was the customer referred to the appeals process in the decline letter?		
Was the customer informed of...	30 days for customer to appeal	
	30 days for appeal decision	
Was the customer signposted to Alternative Sources of Financing?		
Other comments on the original decline detail (decline letter, signposting etc.)		
SECTION FOUR	CUSTOMER APPEAL	
Method of customer appeal		
Appeal Type		
Reason(s) for appeal		

SECTION FIVE	BANK REVIEW OF APPEAL			
Who conducted the review?				
Is this person an Experienced Lender?				
Was this person involved in the original lending decision?				
Overview of review methodology				
Was any additional information requested?				
Additional Customer Documents Requested	Personal Financial Statement		Management/ Audited Accounts	
	Cash flow Forecast		Business Plan	
	Business Profile		Bank Statements	
Any other information requested, please specify				
Appeal Outcome				
If Overturn, actual amount approved				
Rationale for Appeal Decision				
How was the customer informed of the appeal outcome?				
By whom?				
Does the written communication include the reasoning behind the appeal outcome? (If Decline Upheld), do the reasons align with those documented in the case file notes?				
Any other comments				
Note: Freeform Text Boxes highlighted are auto fit row height.				APPEAL REVIEW FORM (31/01/2013)

8.5 Annexe E – Promontory Site Visit Requirements for Appeals Files

Requirements

- Prior to the visit, we need to have a reasonable idea of the numbers of completed and in-scope appeals to be reviewed, and the number overturned by the Appeals Process. This is important for resource management purposes at Promontory, and reduces the need for repeat visits to the same site. Your help in communicating likely volumes for a visit is appreciated.
- For each visit, we need the files to be complete and in date order. Clearly labelled and organised files help us review files quickly and enable us to confirm compliance without undue additional work. Banks should also make sure, apart from the specifics listed below, that they include all other relevant documentation relating to the transaction.
- For individual files, the following information should be included where available:
    - Original application, including documentation that enabled the case to be decided, such as financial statements, account history, business plan, cash flow forecast, credit score outcome, accounts, etc. A summary containing the key data from these may be sufficient
    - Details (inc dates/amounts where relevant) of the customer, location, new business, new to bank, length of relationship, existence of other facilities, turnover/size of business
    - Clear details of what product(s) is being asked for and for how much. Details of existing facilities and terms where topping-up, and a clear purpose of what the credit is being asked for.
    - Details of any internal "4 eyes" process prior to the original decision being given to the customer including notes and dates
    - Names of original decision-maker, including those involved in any "4 eyes" process
    - Details of any referral to "Credit" and any views given by them, also to include dates
    - Copy of the decline letter and any notes of conversations with the customer as part of that process (it is known that more clarity around reasons is often provided in this way)
    - Appeal letter/email/note of call from customer including details of any reason for appeal including "don't agree/not fair"
    - Acknowledgement letter when sent and where part of the process
    - Details of any information submitted with the appeal
    - Name of person who dealt with the appeal
    - Details of the appeal reviewer's assessment/conclusions of the case, including whether any further information was sought from the customer and, if not, reasons why.
    - Details of information given to branch/local RM by the appeal reviewer where appeal outcomes are conveyed locally
    - Appeal outcome letter sent to customer
    - Details of any other conversations with the customer relating to the appeal outcome
    - Where Minimum Standards documentation is missing or the process was not adhered to, there should be an explanation of why it is not available and what is being done to ensure that it will be in future

8.6 Annexe F – Promontory Site Visit Feedback

Site: TFB Name
Date: 2013
Attending:

Appeals Reported to Date			Files Reviewed by Promontory to Date		
	Year 1	Year 2		Year 1	Year 2
Received			Total Reviewed		
Overturns			Overturns		
% Overturns	%	%	Reviewed this visit		
Appeals Processed Showing Overturn rates by Month				**Appeals Completed by Month**	
Month	Appeals Received	Overturns	% Overturns	Appeals Completed	Review Sheets Received
Jan - 2012					
Feb - 2012					
Mar - 2012					
Apr - 2012					
May - 2012					
Jun - 2012					
Jul - 2012					
Aug - 2012					
Sep - 2012					
Oct - 2012					
Nov - 2012					
Dec - 2012					
Jan - 2013					
Feb - 2013					
Mar - 2013					

Appeals Process Updates

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•
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Positive Themes

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•
•

Observations / Next Steps / Matters for Consideration

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•
•

8.7 Annexe G – Extracts from OFT Affordability Guidance

1. ‘Whatever means and sources of information creditors employ as part of an assessment of affordability should be sufficient to make an assessment of the risk of the credit sought being unsustainable for the borrower in question. In our view this is likely to involve more than solely assessing the likelihood of the borrower being able to repay the credit in question. We consider that before granting credit, significantly increasing the amount of credit, or significantly increasing the credit limit under an agreement for running account credit, creditors should take reasonable steps to assess a borrower's likely ability to be able to meet repayments under the credit agreement in a sustainable manner.’
2. ‘the impact of a future change in the borrower's personal circumstances: for example, this could include a known end date of current employment due to circumstances such as retirement or the end of a fixed term employment contract - either of which may lead to a fall in the borrower's disposable income. The possibility of being made redundant, when it was not known at the time that the assessment of affordability was undertaken that this would happen, would not be a matter that the OFT considers creditors could be reasonably expected to take into account
    - the vulnerability of the borrower: for example, whether the borrower is known to lack - or is reasonably believed to lack - the mental capacity to be able to understand information and explanations provided to him and make informed borrowing decisions based on his understanding of such information and explanations at the time they are provided.’

3. ‘Creditors may employ the use of a variety of types and sources of information to assess affordability which might, depending on the circumstances, include some or all of the following examples (this is a non-exhaustive list):
    - record of previous dealings with the borrower
    - evidence of income
    - evidence of expenditure
    - a credit score
    - a credit report from a credit reference agency
    - information obtained from the borrower, whether on an application form or separately (this would include information derived from 'personal contact' with the borrower – for example, during a meeting with a potential borrower at his home).’

4. ‘As previously stated, in the OFT's view, the extent and scope of any assessment of affordability, in any particular circumstance, should be dependent upon- and proportionate to- a number of factors - which may include some or all of the following as appropriate:
    - the type of credit product

- the amount of credit to be provided and the associated cost and risk to the borrower
- the borrower's financial situation at the time the credit is sought
- the borrower's credit history including any indications of the borrower experiencing- or having experienced financial difficulty the borrower's existing and future financial
- commitments including any repayments due in respect of other financial products and significant non-credit commitments

8.8 Annexe I – General Tables

Table 13
Appeals by Government Office Region – (Apr 2011 – Mar 2013) - Combined

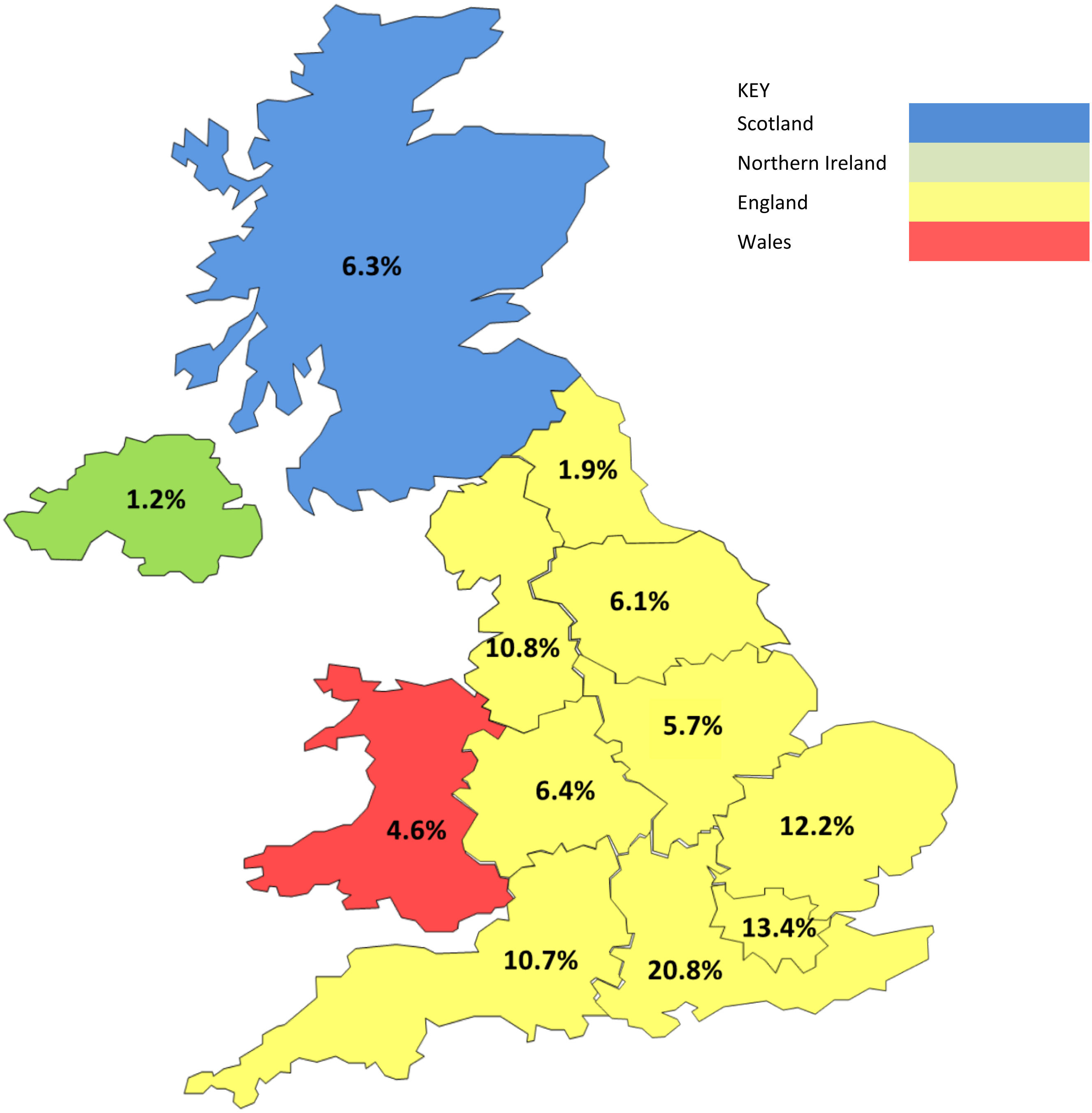


Table 14

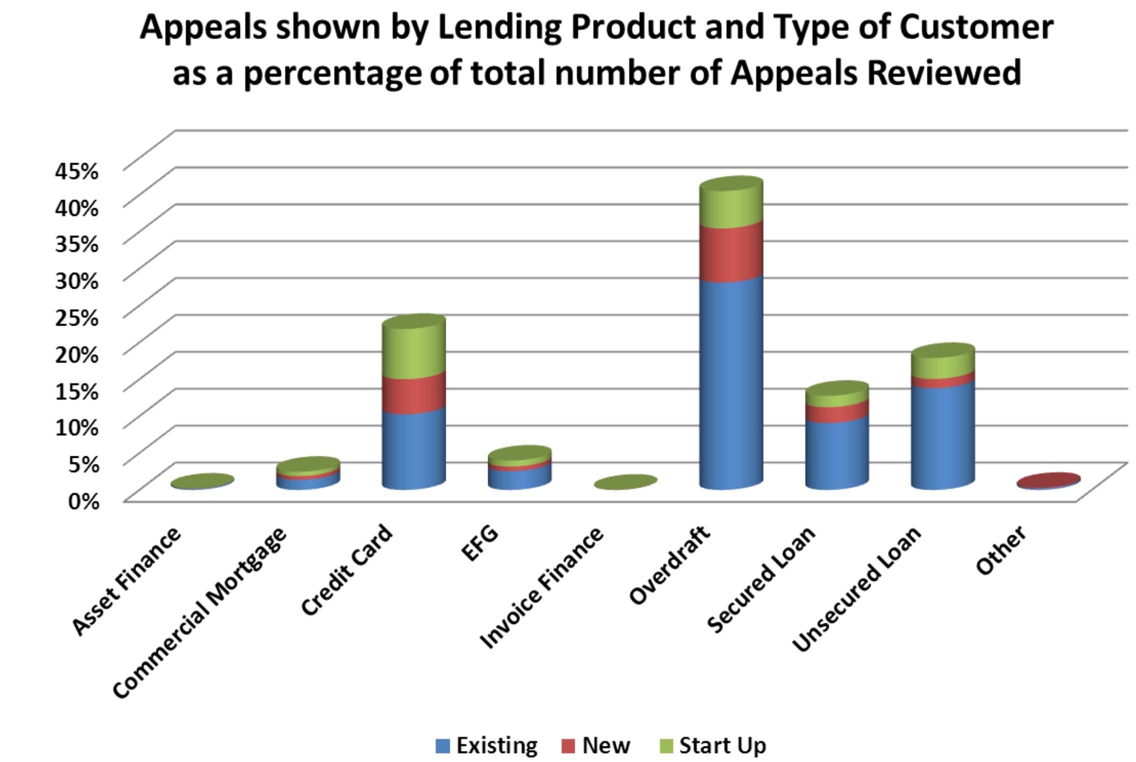
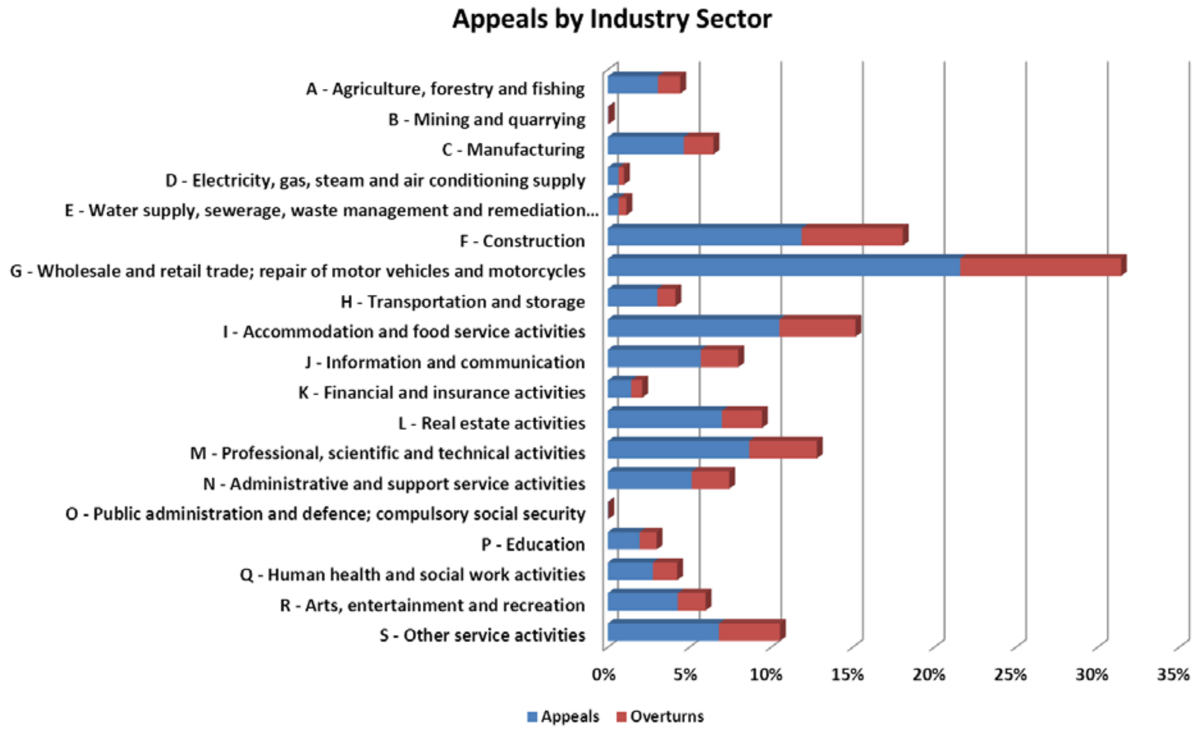


Table 15



8.9 Annexe H – Credit Scoring Leaflet (Final Draft)




BUSINESS CREDIT SCORING EXPLAINED

What small business owners need to know about managing their applications for finance






HOW THIS GUIDE CAN HELP YOU

This short guide has been designed to help you as a business owner understand how business finance decisions are made and the factors that affect your application for finance.

By understanding this information, small business owners can increase the likelihood of future applications being successful.

Whether you're a new business that needs start-up funding, or a growing company that needs the funds for expansion, any application for finance will mean that your bank will try and build up a picture of your personal and business circumstances combined with your financial history. This is a critical part of assessing the business and will often be used alongside your business plan and cash flow projections.

For further information about an application for finance, please contact your bank relationship manager.

BUILDING UP A PICTURE OF YOU AND YOUR BUSINESS

Usually a bank will use three sources of information to build up a profile of you and your business.

A good personal credit record is extremely important for any new business. Before a business can attain a credit rating in its own right, all assessments of eligibility for lending are done on the basis of the credit history of the individual, business owners or directors.

Credit Scoring is part of the process used by banks and other lenders to help assess whether they will lend to you. Each bank you approach for credit will calculate a score for you based on the information available to them at the time. The system allocates points for each piece of relevant information and adds these up to produce a score.

When your score reaches a certain level then a bank will generally agree to your application. If your score does not reach this level, they may not.

If you are declined, this simply means that based on the information available, the bank is not prepared to lend at this time. Each bank has different lending policies and systems, and so applications to them may be assessed differently. One bank may accept an application which another may not.

THE TYPES OF INFORMATION USED

Credit reference agencies (CRAs) collect and maintain information on individuals' and businesses' credit behaviour in the UK.

The credit agencies record five different elements of your credit profile, these being:

1. **Your payment History**
2. **Your Total Amount of Debt**
3. **Time and Length of Credit**
4. **The Type of Credit You Have**
5. **The New Credit Applied For**

1 and 2 are likely to contribute most towards your credit rating. You need to get these in order to improve your credit rating in the longer term. Please see below on what you can do to improve your credit rating.

It's important to note that there are many factors that affect a credit score; it's based on more than just whether you pay your bills on time. Your score can be affected by the amount of available credit you have with your bank, credit cards, the length of time you've had a credit history, the number of inquiries made on your credit profile and more.

As your business builds up a track-record and history in its own right then the balance of future borrowing decisions becomes more about the business than the person. Credit Scoring may also be used in conjunction with some local assessment by your relationship manager.

Sources of information about You and Your Business

- Electoral Register
- Companies House
- County Court Judgements
- Payment History to Utilities and Telecom Companies
- Bankruptcy Orders
- Trade Credit Information
- Previous applications to banks/building societies
- Past and current bank/building society account conduct
- Finance and Leasing Companies

WHAT YOU CAN DO TO **IMPROVE YOUR CREDIT SCORE**

- Make any credit payments **on time** and for the required amount.
- Ensure you are on the **Electoral Register**.
- Ensure that if you are a limited company, you file full rather than abbreviated accounts at the Registrar of Companies.
- Always **ensure the balance** on your account or approved overdraft limit is sufficient to **cover any payments** due from your account (e.g. cheques, standing orders, Direct Debits, debit card and online payments).
- **Build up use** of your business bank account over time to **demonstrate your turnover** (e.g. don't pay business receipts into your personal bank account).

WHAT TO **AVOID**

- Making several requests for finance applications at once over a short period of time will result in 'multiple searches' (also known as 'footprints') showing on your credit record which could affect your credit rating.
- Exceeding your agreed credit limit without approval or going overdrawn without agreeing a limit with your bank/lender first.
- Missing payments leading to credit arrears.

WHAT HAPPENS IF YOUR APPLICATION IS **DECLINED?**

If a bank does not wish to accept your application, they will tell you.

They will also tell you on request the main reason why they were unable to agree your application and whether this is the result of adverse data held by the credit reference agency. If you did not pass their credit score they will tell you. As credit scoring is based on a range of different factors they may not be able to give you the exact reasons why you did not achieve the score the bank requires.

If a bank has declined your business borrowing application you may contact them and ask them to reconsider their decision. You have the right of appeal and you should contact the bank within 30 days of a decline decision if you wish to do this. If you want to appeal they may ask you to provide additional information.

If you believe that any of your information held by a credit agency may be incorrect, then you should contact them directly to obtain a copy of your credit report. In the UK there are a number of agencies that provide consumer and business data to the banks. Your bank will tell you which of these agencies they used when assessing your request for borrowing.

The contact details are listed on the next page. The credit agency will usually charge you a small £2 statutory fee for supplying details of your credit record.

The Credit Agencies

Call Credit	Call Credit, Consumer Services Team, PO Box 491, Leeds LS3 1WZ 0870 060 1414 www.callcredit.co.uk (Personal credit data only)
Equifax	Equifax Ltd, Credit File Advice Centre, PO Box 1140, Bradford BD1 5US www.equifax.co.uk
Experian	Experian, Consumer Help Service, PO Box 8000, Nottingham NG80 7WF 0870 241 6212 www.experian.co.uk

Business Credit Agencies

Credit Safe	Bryn House, Caerphilly Business Park Van Road, Caerphilly CF83 3GG 02920 886500 http://www2.creditsafeuk.com
Dun & Bradstreet	Marlow International Parkway Marlow, Buckinghamshire SL7 1AJ http://www.dnb.co.uk/
Graydon	66-68 College Road Harrow, Middlesex HA1 1BE 020 8515 1400 www.graydon.co.uk

Other sources of information on Finance and help for businesses

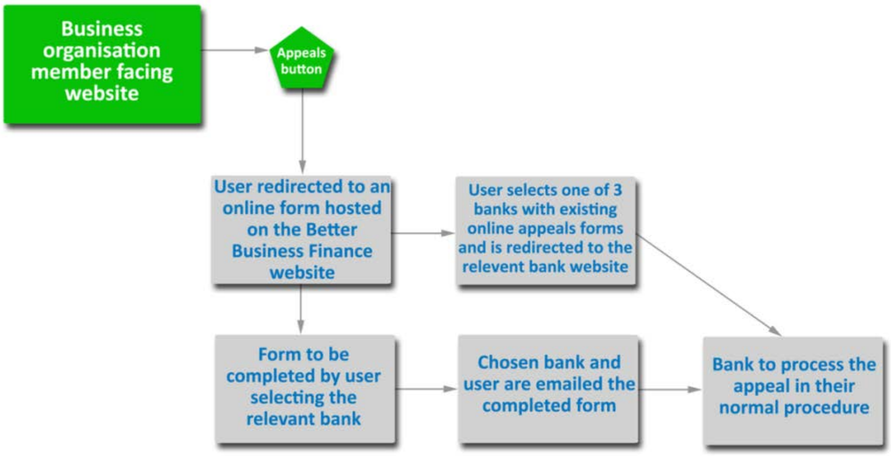
For much more help and guidance around start up business support, mentoring, funding and appeals, please visit www.businessfinanceforyou.co.uk www.betterbusinessfinance.co.uk www.mentorsme.co.uk

For more information about an application for finance or to lodge an appeal, please contact your bank relationship manager.

60 20 220 APR 13 H

8.10 Annexe J – Appeals Form Workflow including Appeals Button

Appeals Form Workflow



The process can be launched through the button and will be available on the BBF site at the below address[10]

[10] www.betterbusinessfinance.co.uk/appeals-for-borrowing

Contact us News Feed Events Feed

BETTER BUSINESS FINANCE.CO.UK

Home | About us | Help & Support | FAQs | Events | News | BBF TV | Contact us |

Home » Contact us

Appeals for borrowing

Business Organisation Logo

If you apply for finance for your business and your request is turned down you can launch an appeal for your application to be reviewed.

Each bank has its own process to handle these appeals but Britain's largest banks have developed a set of commonly agreed principles. These principles will ensure that, across these institutions, all appeals are handled fairly, promptly and transparently.

You can submit an appeal after any formal request for borrowing has been declined - this means any application that has gone through a credit assessment, after the bank has recieved all the relevant information from you to make a decision.

To start the appeal process, please click on the link for the relevant bank below.

Once you have submitted this form, your bank will check your situation and validate your appeal. They may contact you to discuss your appeal and ask you for any further information they require to help make their decision. Following re-assessment of your lending request they will confirm their decision in writing.

Further information about the appeals process can be found here in our factsheet or in the FAQs section of this website.

Help & Support

We have also created a range of factsheets to provide you with more information on the different products and services available and guidance on everything from writing a business plan to managing cash flow.
Read more »

This will link to:
http://www.betterbusinessfinance.co.uk/faqs#faq-66

Please choose the bank you wish to appeal your borrowing decision:

Bank of Scotland	HSBC Bank Plc*	Santander
Barclays Bank Plc	Lloyds TSB	The Royal Bank of Scotland*
Barclaycard	NatWest Bank Plc*	

* You will be taken to the banks own appeals form.

When clicking on an aserixed bank the user will be taken directly to the appeals form of that bank. When clicking on a non-asterixed bank the form will appear below allowing the user to complete.

Business Name:
Company registration number:
Business trading address:
Name of business owner / main contact:
Contact telephone number:
Alternate contact telephone number:
Contact email address:
Sort code / Account number: /
Name of your Relationship Manager:
What lending product did your request relate to?
Date your request was declined
Reason for appeal
Details of any material changes since the original request:

Submit

The decision to decline has not been adequately explained
The bank has not understood my requirements
The bank has failed to take all relevant information into account
The bank's proposed conditions to lend are unreasonable
Other (when selected gives a free text field)

8.11 Annexe K – Appeals Poster

8.12 Annexe L – Appeals Leaflet

There is a range of Government Support for Finance

Just as businesses have different finance needs, there are a range of different Government support products for businesses, from grants to loans for start ups to tax breaks for angel investors.

You can find information on all Government schemes, and a tool to help identify the most relevant ones, at

gov.uk/business-finance-support-finder

Credit Scoring

Many businesses aren't aware that when applying for finance, lenders will check the credit scores of the business- and its directors.

Your credit score can be affected by a range of things, including:

- Unpaid bills (yours or others at your addresses)
- Whether you're on the electoral roll
- Paying suppliers promptly
- Past searches for credit (including getting quotes for finance or utility contracts)

If you've been surprised to be declined finance it may be worth asking credit reference agency for your score- visit bipa.uk.com to find out more

Looking Elsewhere for Debt Finance?

There are many banks providing business finance in the UK, and dozens more organisations providing finance, from peer-to-peer lenders to asset based financiers.

Each lender's regional reach and appetite across sectors differs- so it may well be that whilst one lender can't help you- another might.

The Government and BBA has worked with an array of finance providers to produce a useful directory to help you find alternative finance providers:

businessfinanceforyou.co.uk

Alternatives to banks

Banks are but one source of finance for companies. Equity (where people or businesses provide money in return for shares in the business) helps put your businesses on a sounder footing to access finance and there are generous tax breaks from Government for investors looking to invest in equity.

There are also Community Development Finance Institutions, peer to peer lenders, asset financiers, invoice finance and more that can be accessed through businessfinanceforyou.co.uk and you can find out more at gov.uk/business-finance-explained

When things go wrong

Unfortunately, Ministers or Government officials cannot intervene in disputes with banks. Whilst we do take seriously every issue raised in correspondence, the Department cannot take the place of banks' own complaints processes or the courts. You may also be eligible to contact the Financial Ombudsman Service.

Department for Business Innovation & Skills

Many businesses tell us that it can be a challenge to identify the right finance.

Lending conditions have changed: lenders are looking for more financial information than they once were about the businesses they lend to and their ability to repay.

The Government is working with the private sector to unlock finance. Although <u>only 33% businesses applying for finance are confident of success, 71% of applications are successful.</u>

This leaflet aims to provide answers to the most common questions and highlight sources of help available when raising finance.

Different businesses have different finance needs- and not all of this information may be relevant to your own circumstance, but we hope that it will be of use to you or a business you know.

For more information, please visit us at http://gov.uk, or search the web for "Business in You"

If you have any comments on this leaflet, please contact us via edlynx@bis.gsi.gov.uk

Inside:

- Government support for business
- The banks' appeals process www.betterbusinessfinance.co.uk/help-support/appeal-process
- Finding a mentor (www.mentorsme.co.uk)
- Getting professional advice
- Credit Scoring
- Other sources of help and guidance

Getting Support and Guidance

Business mentors have the practical experience, contacts and expertise to help you make the right choices for your business.

Mentorsme.co.uk (the national mentoring portal which is funded and operated by the BBA) can connect you with mentoring organisations across the UK. If you are a business that needs support or a business professional who can offer support, it can help you connect with each other.

How to identify professional accountancy advice

The Business Finance Advice Scheme enables businesses to identify qualified accountants who can provide expert independent advice on how to access finance, such as bank loans or outside investment. These practices bear the Business Finance Advisor kitemark.

BUSINESS FINANCE ADVICE

You can find a Business Finance Adviser via the ICAEW, ACCA, ICAS websites:

http://www.icaew.com/bfascheme

http://uk.accaglobal.com/

http://icas.org.uk/

Declined by a bank? You can appeal

The major banks* in the UK and Northern Ireland have agreed that if your loan application is declined you have the right to appeal, as part of the BBA Better Business Finance Programme (betterbusinessfinance.co.uk).

When an appeal is raised, the decision will be reviewed by a second person from within the bank who was not involved in the original decision.

The banks will consider all the information originally provided and ask for more where they think it is necessary.

BARCLAYS http://tinyurl.com/BarclaysAppeals

RBS The Royal Bank of Scotland http://tinyurl.com/RBSAppeals

Santander http://tinyurl.com/SantanderAppeals

Lloyds TSB http://tinyurl.com/LloydsAppeals

HSBC http://tinyurl.com/HSBCAppeals

* The banks are Barclays, HSBC, RBS (inc Natwest), Lloyds (including Halifax/Bank of Scotland) and Santander (plus NI banks)

The whole process is monitored and scrutinised by an independent team to ensure the banks are implementing a fair, prompt and transparent appeals process.

In the first year of the programme, **an appeal led to a change in decision in 4 out of ten cases as a result of The process.**

How do I appeal?

If you have been declined finance your bank should have given you instructions on how to appeal with your decline. You will need to instigate an appeal if you feel you have been declined unfairly. **In most cases it can be started with a phone call** to your bank, and there isn't a charge.

An appeal can be made after any formal request for lending has been declined – this means any application that has gone through a credit assessment, after the bank has received the information from you to make a decision.

The bank should explain to you why your application has not been successful, and work with you to reshape the request if possible and give guidance on alternative sources of finance if appropriate. The banks and the BBA are making this as easy as possible.

Where is there more information?

Contact your bank for information on appealing.

Alternatively, the participating banks and the BBA launched the website http://www.betterbusinessfinance.co.ukto provide more information on the appeals process and lending in general.

BETTER BUSINESS FINANCE.CO.UK