Competition & Markets Authority

Making banks work harder for you

9 August 2016

Making banks work harder for customers

1. We have now published the final report of the market investigation into Retail Banking.

2. Our report sets out our analysis of the shortcomings of competition in the markets for current accounts for personal customers and for banking services to small businesses. It also sets out the actions we believe must be taken in order to fix the problems we have found.

3. There are long-standing concerns with the banking market and this is not the first review of these issues. We have drawn from those past reviews and received extensive input from a wide range of interest groups, in addition to banks and regulators.

4. We have found many positive developments. There has been entry by new banks with some entrants adopting new business models, offering specialist products and exploiting opportunities offered by new technologies, such as digital-only banks. Mobile banking is now widely adopted and growing fast. New types of payment services, lending and financial management services are now available from providers which are not banks.

5. Despite these welcome developments, we have found that many problems remain. Essentially, **the older and larger banks, which still account for the large majority of the retail banking market, do not have to work hard enough to win and retain customers and it is difficult for new and smaller providers to attract customers.** These failings are having a pronounced effect on certain groups of customers, particularly overdraft users and smaller businesses. They also mean that the sector is still not as innovative or competitive as it needs to be. Banks will only invest in new products or services or reduce their prices and improve service quality, if they expect to win business as a result, or fear losing business if they do not.

> “The sector is still not as innovative or competitive as it needs to be”

6. We are putting in place a wide range of measures to provide a coherent package that will target the problems we have identified. Many of our remedies build on those introduced by past reviews and on recent positive developments. But we are now in a position to significantly accelerate the pace of change by harnessing technology. In particular, we are requiring banks to allow their customers to share their own bank data securely with third parties using an open banking standard. This change, together with our other remedies, **will help customers to find**

and access better value services and enable them to take more control of their finances. This will also enable new entrants and smaller providers to compete on a more level playing field and increase the opportunities for new business models to develop.

7. Our remedies package is grouped into the four elements listed below. Our 'Foundation measures' will underpin increased competition in all the markets we have examined. These will be accompanied by measures specifically directed to certain aspects of the market: current account switching, PCA overdrafts, and the needs of small business. More detail on our package of remedies is set out below, but first we set out the problems we are seeking to tackle.

Our diagnosis

8. The main problems that we identified are:

   a. Current accounts for both personal and business customers have complicated charging structures, and the actual cost to the customer depends on how they use the account. Customers generally know very little about the charges and service quality provided by other banks. It is therefore hard for customers to know whether they could get better value and service from another bank or a different product with the same bank.

   b. Personal and business current account relationships are open-ended and do not have regular trigger points (like the annual renewal of insurance policies, for example) when customers might be prompted to ask themselves whether they could be getting a better deal elsewhere on their current account.

   c. There is now a reliable and efficient Current Account Switch Service (CASS). This makes it easy for customers to switch current account from one bank to another, but the service is not widely known, and does not command as much confidence as it deserves. The account opening process for small businesses can also be lengthy and onerous.

   d. Charging structures for overdrafts are particularly complicated, making it even harder to compare providers. Customers worry that if they switch they might not get the same overdraft from their new bank. Moreover we found that many customers underestimate their overdraft use.

Overview of the remedy package

Foundation measures

- Open banking standard
- Service quality information
- Customer prompts

Current account switching measures	PCA overdraft measures	Additional banking measures for small businesses
• Better governance of guaranteed switching service • Extended redirection of payments following switching • Customer access to transactions history • Customer awareness and confidence	• Overdraft alerts with grace periods • Monthly maximum charge • Improved account opening and switching process	• Competition to develop comparison tools • Loan rate transparency • Loan price and eligibility indicator • Standard information requirements for BCA opening • Sharing of SME information • 'Soft' searches • Role of professional advisers

e. Over half of start-up businesses open their current account at the bank where the business owner has their personal account. There is also a strong link between business current accounts and lending: **90% of small businesses get their business loans from their main bank,** with little or no shopping around for other lenders. It is hard for small businesses to find out who is the best lender for them. As their existing bank already knows a great deal about them, it is usually easier and quicker to get a loan from their existing bank and harder for other potential lenders to accurately assess and price lending.

f. Getting new customers is therefore difficult and costly for banks. This means that banks which have been around for a long time have advantages over new entrants and smaller banks wishing to expand.

9. Understandably, many customers see little to be gained from spending time thinking about whether they are on the right account or are with the right bank for them or any business they run. It is difficult for the individual customer to work out whether they are getting good value from their existing bank. As a result, **only 3% of personal customers and 4% of business customers switch to a different bank in any year.**

10. In itself, a low level of switching need not be a reason for concern – if customers are happy with their bank which many are, they might think there is little reason to go to the trouble of shopping around and switching from one bank to another. However, there are big differences between and within banks in the prices and quality of service they offer. We found that **many personal customers, in particular overdraft users, could make significant savings by switching to a different current account.** But, in order to be able to find the best deal, customers need: the right easily accessible information on banks' charges and service quality; data on their own usage; easy to use comparison tools to combine banks' information with data on their usage; and a switching service they have confidence in.

> "Customers could make significant savings by switching"

11. In many respects, small businesses face more deep-rooted problems with banking services than personal customers. There has been limited new entry, with most entry by specialist lenders. There has also been less innovation than in personal accounts. Typically a new small business will get free current account services for a period, but when account charges kick in, few of them shop around or switch. There are many reasons why small businesses do not shop around for their accounts or loans. Like personal customers, many say they are satisfied and do not feel that they will gain from switching. In addition many believe that staying loyal to their bank will be an advantage as and when they need lending. It can be time consuming to open a bank account and small businesses are understandably concerned that by switching accounts payments might go astray. When it comes to lending, small businesses often need quick decisions. They do not want to spend time speaking to lots of different providers all asking for different information.

12. Most personal customers are on standard accounts for which they do not pay monthly fees or transaction fees. However, they do incur charges when they go into overdraft or need additional services and they do not receive interest on their balances. These accounts, sometimes referred to as "Free-if-in-credit" (FIIC), are therefore not really 'free'.

13. Customers with modest bank balances who manage to stay out of overdraft and only occasionally make foreign exchange transactions get a reasonable deal under FIIC. The FIIC model also facilitates having more than one bank account and makes it easier to try an account before switching. We looked at whether the FIIC model makes it less likely that customers will switch and we did not find this to be the case. Levels of engagement in other markets where customers pay monthly or annual current account fees are just as low. We also looked at whether it was lower income customers who were paying more under the FIIC model and, again, did not find that this was so.

> Older banks have advantages over new entrants and smaller banks

14. Banking can be expensive for those customers who use overdrafts, with fees and costs that often seem disproportionate to the actual amount borrowed. Overdraft users are not on average from lower income households but, whatever their incomes, they pay higher prices than they would in a competitive market. Customers who incur overdraft charges, especially the high charges on unarranged overdrafts, could make worthwhile savings by switching accounts and if banks helped their customers avoid such charges.

Barriers to entry and expansion

15. We looked at a number of possible difficulties that new entrants and small banks might face compared to older larger banks in addition to acquiring new customers. Several, such as the regulations for authorising banks, the cost of IT and the cost of establishing branches, which have in the past been thought of as problems, we do not find stop banks from entering or expanding. Access to payment systems has also previously been identified as a problem because the payment systems are owned and operated by the larger older banks. However, the Payment Systems Regulator has been recently established with a primary objective of ensuring that the payment systems operate in a pro-competitive fashion and is undertaking an extensive work programme looking at these issues. We did not think it was sensible or desirable for us to duplicate its work.

16. We found that older banks have access to cheaper retail deposits from their existing customers which they can use in their lending businesses. This gives such banks an advantage over new banks and the more customer deposits a bank has the bigger that advantage. In addition, some banks have been regarded as too important to the UK economy to be allowed to go bankrupt, often referred to as 'too big to fail'. This became a particular problem during the financial crisis. Banks which are viewed by investors as 'too big to fail' are seen as lower risk and therefore benefit from lower wholesale funding costs compared to smaller banks.

17. Since the financial crisis, regulators in the UK and internationally have sought to address the problem not just as a competition issue but also to ensure the safety and security of banking. Measures have therefore been put in place since the financial crisis and more are in train, including from 2019 to 'ring-fence' the larger banks' retail businesses from the riskier parts of their businesses.

18. New entrants and some smaller banks expressed particular concerns about the application of the funding rules which seek to avoid a repetition of the 2008 banking crisis. Banks are now required to have a higher proportion of their capital assets provided by their shareholders. This makes it less likely that banks will fail because of unwise lending and if a bank does fail that it has to be rescued at the expense of the taxpayer.

19. Different banks have to hold different levels of shareholder funds depending on how the funding rules apply. The disparity of treatment is particularly striking in the case of residential mortgage lending. Older banks with a track record in residential mortgage lending have to hold smaller levels of shareholder funds to back up such lending compared to newer banks and some smaller banks.

20. These differences are larger for loans whose value is much less than the value of the property against which the lending is secured. Some smaller and newer banks are therefore at a competitive disadvantage in the residential mortgage market as they have to hold more capital against the loan. Since residential mortgage lending is a large and profitable part of the activities of many retail banks, this suggests that capital funding requirements could be a barrier to entry and expansion in retail banking.

21. The CMA does not have powers to alter the capital funding requirements, which are determined by international organisations in which the UK is represented by the Bank of England and the Treasury. These organisations are looking at these issues as a matter of priority to ensure that the competition impacts are given due weight.

22. In 2015, the government reduced the bank levy which was imposed on the largest banks after the 2008 financial crisis, and introduced a corporation tax surcharge on a wider group of banks. Overall, new and smaller banks continue to face a more favourable tax regime than the larger banks, but their tax advantage has been somewhat reduced. Given the positive role which new entry can play in increasing competition in retail banking markets it is important that the Treasury keeps the impact of the new bank tax regime under review and it is reassuring that it has stated that it intends to do so.

Market structure and competition

23. The market continues to be dominated by a small number of high street banks. We have considered carefully how this affects competition.

24. The larger banks in Great Britain have a higher proportion of customers who have been with them for a long time, and tend to have higher prices on average for their personal current accounts, partly because they have a higher proportion of their customers on their higher-priced accounts. This may be because they have had less incentive to compete as vigorously as smaller banks and new entrants for the more active customers. Market concentration may therefore be having an effect on competitive behaviour, but the evidence is neither strong nor conclusive.

25. New entrants and smaller banks have had a positive effect on the market, by introducing new business models and innovative products, but despite this they have only gained market share slowly. Creating new competitors by breaking up existing banks might make the market more competitive, but is a very expensive and lengthy process, as well as being highly disruptive to those customers affected.

26. We believe that the fundamental problem is that even when new entrants and smaller banks introduce competitive products it takes a long time to build customer numbers. The remedies we are introducing will enable customers to be more responsive and reduce the advantages of the existing banks. They will also provide stronger incentives on all banks to compete and make the market more attractive to new banks and other providers, as well as facilitating innovation.

> “Open APIs can transform financial services”

Our package of remedies

27. We are going to tackle the problems we have found by introducing an ambitious, wide-ranging and integrated package of remedies. We recognise that our remedies will have significant implementation costs, in particular for banks, and that the timeframe we are setting is demanding but realistic. We believe, however, that the benefits to bank customers will significantly outweigh these costs.

28. Putting personal and small business customers in control of their banking arrangements is at the heart of how we plan to make these markets work better. Our remedies have been designed to ensure customers get real benefits quickly from the potential provided by technological change. In particular, new opportunities afforded by the timely introduction of open data standards will enable change that is potentially very wide reaching.

The foundation remedies - building on and speeding up technological change

29. Application Programming Interfaces (APIs) are key to the digital services we use on our smartphones and computers. They make life simpler for millions of us every day by enabling us to share information, for example about our location. They are the hidden technological drivers behind digital applications such as Facebook, Google Maps and Uber.

30. Open APIs can transform the financial services sector. There is already a very active and growing FinTech community which has been developing and introducing new products using existing digital technology.

31. Requiring the banks to adopt and maintain a common open standard will accelerate the pace of this change. Without our intervention, the process of developing open APIs cannot be guaranteed and could take a long time, with the effect of denying customers the early benefits of these new services. We are therefore also imposing a challenging, but realistic, timeframe on banks for this process.

32. The development and implementation of an **open API standard for banking** – our first foundation remedy – will permit authorised intermediaries to access information about bank services, prices and service quality and customer usage. This will enable new services to be delivered that are tailored to customers’ specific needs. The types of new and improved services that will result from this remedy include applications which:

   a. Allow banking customers, through a single application, to manage accounts held with several providers.

   b. Allow customers to authorise the movement of funds between current and deposit accounts to help avoid overdraft charges or to benefit from higher interest payments.

WHAT IS OPEN BANKING?

Open banking will mean reliable, personalised financial advice, precisely tailored to your particular circumstances delivered securely and confidentially.

To provide tailored advice banks need to know how you use your account. Currently, to get personalised advice, you have to hand over your confidential banking information to price comparison websites.

How does Open Banking work?

Open banking uses ‘APIs’ to share information securely, without you having to reveal your password. This is the same technology that tells an Uber driver who and where you are or which lets you sign in to other online accounts using Facebook.

How will Open Banking improve things?

With Open Banking, apps could use your transaction information to find the current account which suits you best. If you run a small business, apps could find the best deals for your business accounts and loans. Apps could even help you avoid overdraft charges by moving cash into your account when it dips into the red.

c. Let customers make simple, safe and reliable price and service quality comparisons tailored to their own usage patterns.

d. Monitor a current account and forecast a customer's cash flow, helping to avoid overdraft charges.

e. Use a small business's transaction history to allow a potential lender other than their bank to reliably assess the business's creditworthiness and offer better lending deals than they would without this information.

33. When it comes to customer data, privacy and security concerns are paramount. Only when customers are satisfied that the right safeguards are in place and give consent will their data be shared with anybody. Open APIs will give customers control over what data is shared and with whom.

34. To ensure that enough time is available to work through the important details of this remedy, particularly those that ensure that customers' data is secure at all times, we are requiring that the release of information under this remedy takes place in stages. The least sensitive information – for example about banks' prices, terms and conditions and branch location – will be made available by the end of March 2017. We expect that all aspects of an open banking standard will be up and running in early 2018.

35. Service quality can be just as important as price for customers when making decisions about banking services. Customers need trustworthy and comparable information about service quality in order to form an accurate view of how different banks perform relative to each other. This will, in turn, increase the pressure on banks to monitor and improve their own levels of performance.

36. Our second foundation measure will therefore ensure that customers get much **better information on service quality** than they currently have. We are requiring banks to publish core indicators of service quality based on customers' willingness to recommend their bank to friends, family or colleagues. Banks will also be required to collect and publish a wider range of additional quality measures, which they will make available through open APIs so that intermediaries can use them in new kinds of advisory and comparison services.

> "Customers need trustworthy information about service quality"

37. Most financial products have annual renewal dates which provide a natural point for the customer to consider whether they should switch provider. Bank accounts are not like this, so banks are not under the same competitive pressure as, for example insurers. Our third foundation measure is therefore for personal and business customers to receive **occasional reminders ('prompts'),** at suitable times, to encourage them to review their banking arrangements. Some prompts might be triggered by specific events affecting the customer such as the closure of a local branch; others might be periodic, such as a reminder included in an annual statement.

38. The effectiveness of these prompts will depend on how they are designed, and needs to be based on careful consumer research. We are therefore asking the FCA to undertake a programme of customer testing to identify which prompts will be most effective in changing customer behaviour and then to implement these prompts.

Making switching even easier

39. Many personal and small business customers would benefit from switching banks but they need to have confidence in the switching process. The risk of something going wrong is of particular concern to those small businesses which make or receive many payments directly to their bank account.

40. The guaranteed Current Account Switch Service – CASS – has already made a positive difference to the switching process and is working well. But many customers either do not know about it or do not have confidence in it. For CASS to fulfil its potential it needs to be widely known and trusted. We are therefore requiring changes to CASS that will improve its performance and increase customer awareness of and confidence in the service. As part of this we are **increasing the scope of services offered by CASS.** For example, we are ensuring that customers' incoming payments will be redirected to their new account for as long as they need it.

> "Customers need to be given the opportunity to avoid incurring charges"

41. A different approach to customer switching would be to require the introduction of Account Number Portability (ANP). ANP would mean that a customer effectively took their account number with them when they switched banks. This change would make switching easier for customers, but it would take a long time to establish and involve substantial and expensive changes to payments systems. Open APIs will themselves fundamentally change customers' experience of banking and reduce the role of bank account numbers. We decided to pursue open APIs, while taking action in the short-term to make CASS work better.

42. Now that many customers no longer keep paper bank statements, difficulties in accessing past records could deter customers moving between providers. This is likely to be particularly important for small businesses, for whom loss of access to their previous transaction history following a switch of banks could make it harder for them to secure business loans. We are therefore requiring that **customers of all current account providers are able to get a copy of their transaction history after account closure.**

Overdrafts

43. Overdraft users make up almost half of those with personal current accounts. Presently, many find it hard to keep on top of their use of arranged or unarranged overdrafts. Failing to do so can be costly, since overdraft users can accumulate high costs from the complicated mix of interest, fees and charges that they face.

44. Overdraft users, like other personal current account customers, have very low switching rates, which is particularly striking, given that they often have the most to gain from switching. One reason for this is that overdraft users can be uncertain about whether they will be able to obtain an overdraft facility from a different bank, or when such a facility would be made available to them.

45. We are therefore introducing additional measures to enable personal customers to take more control over their use of overdraft services as well as improving the switching process for these customers.

46. First, customers need to be given clear notice when they are going into overdraft. We will therefore require **banks to alert their customers, for example by sending a text message, when they are going into unarranged overdraft.**

47. Second, customers need to be given the opportunity to avoid incurring charges. The alerts that banks will be required to provide will also inform customers of a 'grace period' during which they have an opportunity to avoid charges.

48. Third, banks will be required to set a **ceiling on their unarranged overdraft charges,** in the form of a monthly maximum charge (MMC). A bank's MMC will specify a maximum amount that the bank can charge a customer during any given month, taking together all unarranged overdraft charges including debit interest and unpaid items fees that the bank charges. Banks will be required to disclose the MMC associated with each of their accounts, so that customers are fully aware and can use it to compare providers.

49. Fourth, we are recommending that Bacs and the FCA explore ways to make it easier for overdraft users to shop around and switch banks including online overdraft eligibility tools.

50. While we are placing requirements on banks to introduce these measures, we are aware that, to have most impact, they need to be carefully designed; and then monitored and improved in the light of experience. **We are therefore asking the FCA to follow up by undertaking further research on overdraft alerts and grace periods to maximise their effectiveness; and also to look at how the current account opening process could be used to make customers more aware of the features and costs of overdrafts**. This will complement the FCA's work to safeguard responsible lending. Also, we have asked the FCA to carry out work on the effectiveness of the MMC after we have implemented it, and to consider how it might be further developed.

Banking services for small businesses

51. Our foundation measures and current account switching remedies will help business customers as well as personal customers. But we need to do more for small businesses, for whom the competition problems are so deep-seated.

52. Small businesses need much better information about what different banks can offer them. While some useful services, such as the Business Banking Insights survey (BBI), are currently available, there is no existing comparison website providing a comprehensive service. We think that small businesses would be best served by the development of 'one-stop-shops' that would enable them quickly and reliably to compare the price, quality of service and lending criteria offered by a wide range of providers.

53. We are backing the independent innovation charity **NESTA's launch of a 'challenge prize' to enable the development and delivery of comparison services** that will be both innovative and commercially sustainable. We think this is the best way forward, and, to maximise its potential, we are requiring those banks most active in providing services to small businesses to provide both financial backing and technical support to the NESTA project. We expect open APIs to underpin the services developed in the NESTA project, and we will ensure the two projects are properly co-ordinated.

54. While the NESTA process is under way, we are requiring the banks to continue supporting the existing BBI survey.

55. We have high expectations of the NESTA project, but it is not the only thing we are doing for small business banking.

- **a.** We are **improving the information available on loan prices and eligibility.** This will encourage lenders to compete both on price and on their willingness to make loans available. To make this happen, we are requiring lenders to publish their prices for smaller, non-complex lending products, drawing on approaches used under the existing personal consumer credit regime. The largest banks will also be required to develop online tools which allow small businesses to input some information about themselves and receive tailored indications of eligibility and price for lending products.

b. New business account opening processes can be very time-consuming, which in turn can discourage business customers from considering switching, and we are taking steps to make this easier by requiring **banks to adopt standardised business account opening information requirements.**

c. We have asked the Treasury to work with others to implement a soft search mechanism, so that **small businesses can be confident that they can shop around for credit without adversely affecting their credit rating.**

> "Small businesses will be more empowered and less dependent on their existing bank"

d. Our business banking measures will be most effective if more small firms can be better supported to understand the benefits of shopping around for their banking services. Professional advisers, particularly accountants, have an important role in helping small businesses make good decisions, including about their choice of provider. We therefore recommend that the Department for Business, Energy & Industrial Strategy (BEIS) should work with the British Business Bank and professional associations to explore ways in which their members can channel **advice on choice of banks and sources of finance to small businesses.**

56. The development of open APIs together with data-sharing and industry-led initiatives will help small businesses seeking finance by enabling them securely to share their information with potential lenders. We expect the market to respond to these initiatives and our remedies. We recommend that the Treasury should undertake a review of the impact of these developments in two years' time.

57. Our package of measures for small businesses will make it easier to shop around and open a new business current account, will make more information available on the prices and availability of lending products, and will make it much easier to compare both current accounts and loans. The effect of the package taken as a whole will be that **small businesses will be more empowered and less dependent on their existing bank** and will enjoy the benefits of a more competitive banking market. It will also enable other providers to compete more fairly for customers.

What now?

58. Now that we have published our final report, our focus is on putting in place the remedies. This will involve coordinated action by the CMA and a number of other bodies including Treasury, the FCA, BEIS, Bacs, CASS and NESTA to specify and oversee the changes required of the banks.

59. The timetable for implementing our remedies is set out below. Given the scale and ambition of our remedies, it will take until summer 2018 for all elements of the package to come into force, though some remedies will be in place within months.

60. Finally we would like to thank all those who have assisted with our investigation.

WHAT HAPPENS NEXT

Main remedies	Who is Responsible	Order or Undertaking[1]	Commencement date – by or between
Development and adoption of an open API standard	Largest banks in GB and NI	Order	Q1 2017 and Q1 2018
Service quality metrics: core measures	All Banks[2]	Order	Q3 2018
Prompts: cooperate with FCA research and trials	All Banks[2]	Order	Q1 2017
Facilitating switching: CASS governance	Bacs	Undertakings	Q3 2017
Facilitating switching: CASS awareness and confidence	Bacs	Undertakings	Q3 2017
Facilitating switching: CASS redirection	Bacs	Undertakings	Q4 2018
Transaction history for customers	All Banks[2]	Order	Q1 2018
Overdraft alerts with grace periods	All PCA providers[2]	Order	Q1 2018
Alerts: cooperate with FCA research and trials	All banks[2]	Order	Q1 2017
Monthly maximum charge	All PCA providers	Order	Q3 2017
Firm decision to customer prior to switching account provider	Bacs	Undertakings	Q1 2018
Development of a comparison website for SMEs	Largest banks in GB and NI	Order	Q1 2017
Publication of SME lending product prices	All SME lenders	Order	Q3 2017
Development of SME loan price and eligibility tool	Largest banks in GB	Order	Q1 2018
BCA opening procedures	All banks[2]	Order	Q1 2018

[1]Full details of the Orders and Undertakings, and the associated recommendations to be taken forward by HMT, FCA and BEIS to support them, can be found in the Final Report.

[2]Subject to de minimis threshold