

Consultation: personal current accounts and banking services to small and medium- sized enterprises

Provisional decision on
market investigation reference

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Summary

Overview

1. This consultation document sets out the CMA's provisional decision on whether or not a market investigation reference (MIR) should be made in relation to the provision of banking services to small and medium-sized enterprises (SMEs)¹ or in relation to the provision of personal current accounts (PCAs) or in relation to both. The core analysis concerning each of these sectors can be found in the separate market study reports also published today.²
2. Having considered the evidence set out in the market study reports, the CMA has reached the provisional decision that an MIR should be made in relation both to PCAs and to retail banking for SMEs. An overview of our provisional reasons for doing so is in the text box below, followed by further detail in the remainder of the summary and in later chapters.

- These remain sectors which do not appear to be functioning in the way we would expect of effective competitive markets. This leads to poorer outcomes for customers – holders of PCAs and SMEs – and also, given the key importance of retail banking,³ to the wider economy. For current accounts in both the personal and SME sector, customer satisfaction scores for the four largest banks⁴ are below or around 60%,⁵ but, despite this, there is relatively little customer shopping around or switching, leaving both the market concentrated and market shares of providers relatively stable over time. We note, in particular, that the larger banks, with relatively lower satisfaction levels, have not significantly lost market share, while banks with higher satisfaction levels have not been able to gain significant market share, which is not what one would normally expect to find in well-functioning, competitive markets.

¹ That is, any business with an annual turnover not exceeding £25 million.

² www.gov.uk/cma-cases/review-of-banking-for-small-and-medium-sized-businesses-smes-in-the-uk.

³ See paragraphs 4.6 and 4.7 below.

⁴ The four largest banking groups are: Barclays Bank PLC (which we refer to as 'Barclays'; HSBC Bank plc ('HSBC') which includes the HSBC, Marks & Spencer and first direct branded banks; Lloyds Banking Group PLC ('Lloyds' or 'LBG') which includes the Lloyds, Halifax, Bank of Scotland and TSB branded banks; and The Royal Bank of Scotland Group plc ('RBSG') which includes the NatWest and Royal Bank of Scotland brands.

⁵ These are *Which?* customer satisfaction scores for PCAs (see Chapter 2 in the market study update on PCAs, July 2014) and Business Banking Insight average satisfaction levels for SMEs (see Chapter 9 in the market study on banking services to SMEs, July 2014). The 'below or around 60%' figure refers not to the banking groups, but to the four main UK branded banks, Barclays, HSBC, Lloyds and NatWest.

- The fact of such stable market shares and limited customer shopping around and switching seems to reflect continuing high barriers to entry and expansion, including the continuing need for an extensive local branch network to be a scale competitor in either sector (despite increased usage of online and mobile banking) and apparent difficulties for smaller banks in gaining access to key inputs such as payment systems. The low levels of switching by customers themselves constitute a barrier to entry and expansion, making it difficult for smaller and newer providers to acquire sufficient numbers of profitable customers.
- We also consider that there is a mutually reinforcing pattern of demand-side problems (including customer inertia, problems in understanding the pricing structures and a perceived lack of differentiation between banks) and supply-side problems (resulting from market concentration and high barriers to entry and expansion). These issues seem to combine, and contribute to one another, in a complex pattern which gives rise to markets characterised by features which prevent, restrict or distort competition.
- There have been positive developments in recent years, particularly in PCAs (as described in paragraph 6 below), but these do not appear to have had the 'significant impact' that was hoped for when the OFT examined the PCA sector in 2012/13.⁶
- Although there are differences between competitive conditions in the SME banking and PCA sectors (with more evidence of recent and prospective new entry in PCAs), they share many common features. There are also linkages, for example, more than half of SMEs obtain their business current accounts (BCAs) from their current PCA provider, limiting those providers' incentives to compete intensively for new BCA customers.

3. Our proposal that there should be an MIR in respect of both the PCA and SME banking sectors is a provisional view that we have taken only after carefully considering various relevant factors which we set out in this document, including recognising that a market investigation should be proportionate and 'add value' over and above what might be achieved using

⁶ The OFT's decision not to make an MIR of the market for PCAs, in May 2013, said that there were developments happening or expected 'in the coming months' that 'could potentially have a significant impact on the effectiveness of competition in the market' (see paragraph 1.2 below).

alternative approaches. We are fully conscious that a market investigation involves considerable cost (for example, of time, effort and resource) for businesses in the sectors under investigation and other interested parties – such as the banks, other financial service providers and customers – and indeed for the public purse. Making a reference is not a decision to be lightly undertaken by the CMA.

4. In addition to the factual information we have received, we have had the benefit of many helpful submissions, some of which advocated an MIR and some of which advocated that there should be no MIR, including a number of substantial submissions from several larger banks arguing that there are no significant competition concerns in relation to these sectors. The four largest UK retail banks have also, while maintaining that there are no significant competition concerns, submitted ‘in principle’ proposals for some behavioural ‘undertakings in lieu of a reference’ (UILs) as a way of addressing any competition concerns in relation to the SME banking sector (no UILs have been proposed to us to address competition concerns in relation to the PCA sector). Having had regard to all these matters, we have reached the provisional view that, rather than accepting UILs at this stage, there should be an MIR. We very much welcome views on this provisional decision, which we will carefully consider before taking a final decision regarding an MIR. We expect to take that decision in the autumn.

The CMA’s provisional view on the ‘reference test’

5. In order to make an MIR,⁷ the CMA must first have reasonable grounds for suspecting that any feature, or combination of features, of a market in the UK for goods or services prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK (in this document we call this the ‘reference test’).⁸
6. The CMA recognises that in recent years there have been various positive developments in terms of competition in these sectors including some new market entry, improvements in the regime for authorising new banks, and the introduction of a seven-day current account switching service (CASS). The CMA’s provisional view is that there remain reasonable grounds to suspect that features of the markets for SME banking and PCAs prevent, restrict or distort competition and that the reference test is therefore met.

⁷ The CMA has adopted the guidance prepared by the OFT: [Market investigation references: Guidance about the making of references under Part 4 of the Enterprise Act](#), March 2006 (OFT 511).

⁸ Section 131(1) of the Enterprise Act 2002.

7. Features which the CMA considers there are reasonable grounds to suspect prevent, restrict or distort competition concerns in the SME banking sector, and which we provisionally consider meet the reference test, individually and in combination, are:
- persistent levels of concentration and relatively stable market shares among banks in respect of the provision of both BCAs and general purpose business loans
 - a market structure characterised by close linkages both between PCAs and BCAs, and between BCAs and general purpose business loans
 - continuing high barriers to entry and expansion in the supply of BCAs and general purpose business loans to SMEs, such as acquiring sufficient numbers of profitable customers, the continuing need for an extensive network of local branches, and alleged difficulties and excessive costs for access to key inputs, particularly payment systems
 - SMEs not being easily able to access, assess and act on information about the banks' offerings (eg comparing pricing or service standards), and reluctance by SME customers to shop around between banks for alternative offerings and to switch banks
8. Features which we suspect give rise to competition concerns in PCAs, which we also provisionally consider meet the reference test, individually and in combination, are:
- persistent levels of concentration and relatively stable market shares among providers
 - continuing high barriers to entry and expansion, in particular the need for a branch network, alleged difficulties and excessive costs for access to key inputs, particularly payment systems, and to some extent overcoming customer inertia to consider an alternative
 - relatively low levels of switching and shopping around by customers for alternative offerings
 - lack of transparency in charging structures, particularly for overdrafts
9. It is also possible that, particularly for PCAs, there is a degree of cross-subsidy, which may be distortive of competition. Indeed, the free if in credit model often involves cross-subsidy by other revenue streams for PCAs such as overdraft charges. In addition, we were also told by some banks that PCAs

as a whole were loss-making. If this were the case, this could suggest the existence of a cross-subsidy from other retail banking products.

10. We have set out our provisional conclusions on whether the reference test is met in relation to SME banking and to PCAs separately (as above).⁹ However, our overall conclusion, as we set out in this document, considers both these sectors together and finds that the reference test is met in relation to both. This reflects the CMA's provisional conclusion that many of the features which the CMA considers there are reasonable grounds to suspect prevent, restrict or distort competition are common to both sectors and that the products are closely related – for example, the majority of SME owners obtain their BCA from their PCA provider and the same banks are prominent in both sectors.

Customer outcomes

11. Consistent with these features which the CMA has identified may prevent, restrict or distort competition in the PCA and SME banking sectors, we note that outcomes for customers appear poorer than they would be in well-functioning competitive markets (see Chapter 9 of the SME report and Chapter 7 of the PCA report):

SMEs

- Just 13% of SMEs trust their bank to act in their best interests and only 25% feel supported by their bank.¹⁰
- SMEs, on average, would be unwilling to recommend their bank.¹¹
- SMEs rate banks lower than energy and telecommunications companies for satisfaction – in particular, some 80 to 90% of SMEs of telecoms and energy services are very satisfied or satisfied, compared to levels that range from 47 to 72% in SME banking. Satisfaction scores for BCAs are also around 60%.¹²
- These overall ratings reflect deeper and specific concerns about at least some banks, as indicated for example by Sir Andrew Large's recent report on RBS's lending practices to SMEs.

⁹ See below, paragraphs 3.3 to 3.5 for SME banking, and paragraphs 3.6 to 3.8 for PCAs.

¹⁰ CMA market study on banking services to SMEs, July 2014, Chapter 9.

¹¹ *ibid.*

¹² *ibid.*

PCAs

- For PCAs, there were 600,000 complaints in 2013 alone.¹³
 - Customer satisfaction levels for the largest four banks are less than 60%.¹⁴
12. Significantly, poorer satisfaction levels at some larger banks are not reflected in loss of market share, nor are smaller banks with higher satisfaction levels quickly able to acquire market share; again these are not what we would expect to see in well-functioning competitive markets.

The CMA's provisional position on the four discretionary criteria

13. Once the CMA has provisionally concluded that the reference test is met, there are four particular criteria which the CMA considers to guide the exercise of its discretion as to whether or not to make an MIR. Our assessment against these four criteria is briefly summarised here:
- **Scale of the suspected problem:** These are substantial markets in terms of size and importance, and the workings of the retail banking sector have a very significant effect on the welfare of consumers, businesses and the economy as a whole. Moreover, the features of concern are widespread and relate to both the supply side and the demand side, and as such, affect a significant proportion of the sectors. Additionally, we consider that the features we identify are longstanding in nature, with each being specifically considered by various competition inquiries over many years. Given the available evidence, and notwithstanding recent positive developments, we provisionally consider that these concerns are likely to persist.
 - **Availability of appropriate remedies through an MIR:** We have conducted an initial assessment of the likely availability of behavioural and structural remedies following a market investigation (in the event that an MIR were to be made). In respect of both the PCA and SME banking sectors, we consider that certain appropriate behavioural measures, including enhanced transparency and regulation of bank conduct, could be available. Furthermore, we have considered submissions from a range of different parties indicating that, in their view, structural remedies may be needed to address long-standing features of concern. We have considered these submissions, balancing them with concerns about the potential costs and the feasibility of any structural remedies. We consider that, at the end

¹³ Financial Conduct Authority data. CMA market study update on PCAs, July 2014, Chapter 6.

¹⁴ Which? customer satisfaction scores. CMA market study update on PCAs, July 2014, Chapter 2.

of a 'Phase 1' market study, we cannot rule out the possibility that structural remedies may be necessary. Consequently, we provisionally conclude that appropriate remedies are likely to be available that are not available at Phase 1. We also consider that there could be significant benefit in undertaking a comprehensive and independent market investigation in these sectors where there are widespread public concerns; this could identify whether adverse effects on competition concerns exist and, if so, what measures should most appropriately be taken to remedy, mitigate or prevent such adverse effects.

- **The availability of UILs:** We have carefully considered in principle proposals for UILs made by the four largest UK retail banks, during the course of the market study of SME banking, offering potential behavioural remedies with a view to addressing competition concerns in SME banking (no UILs have been proposed to us to address competition concerns in relation to the PCA sector). We have carefully considered the 'appropriateness', 'effectiveness' and 'feasibility' of these proposals. While we welcome the initiative of these banks, we have provisionally concluded that we cannot be confident that these UILs could provide as comprehensive a solution as is 'reasonable and practicable' to the features that the CMA has identified may prevent, restrict or distort competition in the SME banking sector. Specifically, the CMA's provisional assessment is that:
 - Accepting such behavioural UILs would not be appropriate as it would rule out the possibility of structural remedies at a stage when we cannot reasonably be confident that structural remedies are not necessary (as noted above).¹⁵ We are not saying that structural remedies are probable following a market investigation but, rather, that in these markets at this time one cannot reasonably rule out the possibility of structural remedies at 'Phase 1' without the further in-depth analysis that a 'Phase 2' market investigation can provide. Our provisional view is that it would not be responsible or appropriate to accept UILs that preclude the possibility of a structural remedy without having explored these issues fully in a market investigation.
 - Moreover, we are not persuaded that UILs offering a comprehensive solution could be agreed in a timely way and therefore are not

¹⁵ Indeed, we note that various sources have identified structural concerns in this sector, with many of them advocating structural solutions to the competition concerns they have found – for example, the European Commission's decisions under the EU state aid rules to require divestments by Lloyds Banking Group (LBG) and by Royal Bank of Scotland Group (RBSG) 'as an appropriate means of increasing competition on the concentrated UK retail banking market', and the recommendation in the *Report of the Independent Commission on Banking* (the Vickers report) that the LBG divestment be substantially enhanced.

persuaded that UILs are likely to offer a significantly quicker solution than through the making of an MIR. This is particularly the case given the practical difficulties of negotiating complex undertakings which provide as comprehensive solution as is reasonable and practicable, with multiple parties.¹⁶

We particularly welcome views on this provisional analysis of the availability of UILs.

- **Alternative powers:** We have considered whether alternative powers are likely to be available to the CMA or others to address the features identified. Although we note certain initiatives and developments being led by the Financial Conduct Authority, Prudential Regulation Authority and the new Payments Systems Regulator, we do not consider that these, while important, are likely to be by themselves sufficient to address comprehensively the long-standing aspects of competition concern that we have identified across these complex markets. We provisionally conclude that alternative powers alone are unlikely to be sufficient to address comprehensively the suspected features which the CMA has identified may prevent, restrict or distort competition.

Invitation to respond

14. The CMA is consulting on its provisional decision to refer both the SME banking and PCA sectors for a single in-depth 'Phase 2' market investigation into aspects of retail banking in the UK. As we note above, the CMA welcomes representations from interested parties on the provisional decision set out in this document, including our provisional view that it would not be appropriate to accept UILs of the kind proposed by the four largest UK retail banks in respect of SME banking. We urge respondents to provide evidence to support views they express in response to the consultation. The CMA wishes to stress the importance of the consultation process in assisting the CMA's decision-making process, and encourages all interested parties to engage with the consultation. Respondents may wish, in particular, to address the questions set out in paragraph 1.8 of this document.
15. Such comments must be provided no later than **5:00 pm on 17 September 2014** to:

¹⁶ In this regard, it is worth noting that UILs have never been obtained from any more than three parties in any market since the power was first introduced in 2003.

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Competition and Markets Authority
Victoria House
37 Southampton Row
London
WC1B 4AD

Email: retailbanking@cma.gsi.gov.uk

16. We will publish all responses on the CMA's website, except those responses marked as confidential. Respondents may request that their response be kept confidential. If you would like your response to remain confidential, clearly mark it to that effect and include the reasons for confidentiality. Please see paragraph 1.10 below for more detail.

Structure of this document

Our analysis and provisional decision on whether to make an MIR follows in the succeeding chapters, which are structured as follows:

- Chapter 1: Background
- Chapter 2: Legal framework
- Chapter 3: The 'reference test'
- Chapter 4: Discretion to make an MIR
- Chapter 5: Proposed scope of the MIR
- Annex A: Summary of UILs offered to the CMA in principle by the banks in relation to SME banking
- Annex B: Draft terms of reference

1. Background

1.1 In the following paragraphs, the CMA briefly introduces the relevant background to its provisional decision to make an MIR in relation to the provision of retail banking services to SMEs or the provision of PCAs or both.

1.2 The UK retail banking sector has been the subject of detailed scrutiny by the UK competition authorities and by other bodies in recent years. These have included:

- **Sir Donald Cruickshank's review of retail banking**, published in 2000, which examined whether competition was effective in the markets for money transmission, services to personal customers and services to SMEs. Its conclusion was that 'competition problems were found in all markets investigated.'
- **The Competition Commission's (CC's) market investigation into the supply of SME banking services**, published in 2002, which found that the four largest banks had market shares over 90%, that customers showed an unwillingness to switch and that there were high barriers to entry.
- Previous OFT market reviews have also found in recent years significant competition concerns in the markets for SME banking (a review published in 2007) and for PCAs (a market study in 2008, and a review published in 2013):
 - **The OFT's 2007 review of SME banking** found that, although there had been some potential competition improvements, concerns remained about barriers to entry, low levels of switching in the market and a lack of price transparency for customers.
 - **The OFT's 2013 review of PCAs** found that, since the OFT's last detailed examination of the PCA sector in a market study in 2008, concentration among the large providers had increased, new entry remained infrequent and switching rates were still low. The review found that there had been some specific improvements, in particular from a substantial fall in unarranged overdraft charges. However, overdraft charging structures were still complex, comparing products was still considered to be challenging and consumers lacked confidence in the switching process. Ultimately, a combination of consumer apathy, a lack of competition and low levels of innovation made it a market that did not work well for consumers or the economy. However, the OFT decided not to make an MIR of the PCA market at

that time (May 2013), noting that there were ‘three significant developments happening or expected in the PCA market in the coming months’:

- the divestment of branches from both Lloyds Banking Group (LBG) and Royal Bank of Scotland Group (RBSG), required by European Commission state aid decisions
- the introduction of CASS
- the roll-out of various transparency initiatives¹⁷

In addition, the OFT thought that the launch of the Financial Conduct Authority (FCA), with a primary interest to promote competition in the interests of consumers, might also play a role in stimulating effective competition.

The OFT’s final decision in May 2013 confirmed the provisional decision not to make an MIR. However, in view of its significant concerns about the market, it confirmed that it would return to the question of whether an MIR was required by 2015, if not before.¹⁸

- **The Independent Commission on Banking**, chaired by Sir John Vickers, whose final report (the Vickers report) was published in September 2011,¹⁹ and the **Parliamentary Commission on Banking Standards** (the PCBS), whose report was published in June 2013,²⁰ both expressed concerns about competition in SME banking and PCAs. Specifically:
 - The Vickers report highlighted that the problems first identified in the markets for PCAs and SMEs by the Cruickshank report in 2000 remained. These markets continued to be concentrated, there were high barriers to entry, switching rates were low and there was a need for greater transparency around products.²¹
 - The PCBS found that the retail banking market was characterised by high concentration, high barriers to entry and limited switching between providers.²² Three particular challenges facing new entrant banks were

¹⁷ In fact, the LBG divestment (of TSB) is taking place over the period June 2014 to December 2015, and the RBSG divestment (of Williams & Glyn) has been postponed and is now expected to take place in 2016/17. The effects of the new current account switching service and of the roll-out of the transparency initiatives are considered in the market study report into PCAs which the CMA is publishing today.

¹⁸ Paragraph 43.

¹⁹ Paragraph 8.93 of the Vickers report.

²⁰ PCBS (2013), Volume 1, paragraph 22; Volume 2, paragraph 67.

²¹ Paragraph 6.7 of the Vickers report.

²² PCBS (2013), Volume 1, paragraph 22; Volume 2, paragraph 167.

high capital requirements, the bank authorisation process and access to the payments system.

- 1.3 As demonstrated, these reviews report significant concerns about the effectiveness of competition in the sector, including:
- the persistence of high levels of concentration and relatively stable market shares
 - barriers to entry and expansion
 - a weak customer response, with customers not being able readily to access, assess and act on information they would need to ensure that they get the best possible deal
- 1.4 Both the Vickers report and the PCBS report recommended that consideration should be given to making an MIR by 2015, if not before, unless there had been sufficient changes in the state of competition in the sector.²³ The Vickers report further concluded that, on the basis of the evidence that it had considered:
- There were features of the PCA market which prevented, distorted or restricted competition. These included market concentration, high barriers to entry, low levels of transparency and high switching costs.
 - There were features of the BCA market which prevented, restricted or distorted competition, and that these features were similar to the PCA market in nature, and are present to a similar, and in some case greater, extent in the BCA market.²⁴

These assessments and recommendations, while forming a part of the relevant background to the market studies, are, of course, not binding on the CMA. The CMA's provisional decision is based solely on our current assessment of competition in the sector, reflecting the analysis that has been undertaken during the course of the market studies.

Current CMA work programme

- 1.5 The CMA announced on 11 March 2014 that it would complete a short programme of work into aspects of retail banking, consisting of:

²³ See [Vickers final report](#), paragraph 8.93, and [PCBS \(2013\)](#), paragraphs 65–68.

²⁴ See [Vickers final report](#), paragraphs 8.90 & 8.91.

- completion of the OFT's market study into SME banking, which was a joint project with the FCA:
 - the study was launched by the OFT in June 2013, with a final position on scope published on 27 September 2013²⁵
 - the market study report ('the SME report') is published today
- a short market study update into the supply of PCAs:
 - the study was launched by the CMA in April 2014 to provide an update following the OFT's 2013 review (as described above in paragraph 1.2)²⁶
 - the market study update ('the PCA update') is published today

1.6 The CMA's decision to bring together work in relation to PCAs and SMEs reflected important similarities in competition issues between these segments of retail banking, in particular:

- the way that PCA and SME customers consume banking services, including levels of customer engagement with banking providers
- how the dynamics of competition seem to operate
- the same banks are prominent in both markets

1.7 The CMA announced that it would publish the findings of its work on both PCAs and SME banking during summer 2014, including this provisional decision regarding an MIR.²⁷

Consultation and next steps

1.8 The CMA welcomes representations from interested parties on the provisional decision set out in this document. The CMA wishes to stress the importance of the consultation process in assisting the CMA's decision-making process, and urges interested parties to engage with the consultation. Respondents may wish to comment on either PCAs, or SME banking, or both. In doing so, respondents may wish to consider the following key questions:

²⁵ See OFT1507, [Update on proposed scope for SME banking market study](#).

²⁶ See the [market study notice of 4 April 2014](#).

²⁷ See press release of 11 March 2014, '[CMA announces programme of work on banking](#)'.

- Do you consider that the CMA's analysis of the suspected features of concern in the market for PCAs is correct (see paragraph 3.6)?
- Do you consider that the CMA's provisional analysis with respect to the exercise of its discretion to refer the PCA market is correct (see Chapter 4)?
- Do you consider that the CMA's analysis of the suspected features of concern in the SME banking sector is correct (see paragraph 3.3)?
- Do you consider that the CMA's provisional analysis with respect to the exercise of its discretion to refer SME banking is correct (see Chapter 4)?
- Do you consider that the features which the CMA has identified that may prevent, restrict or distort competition, are capable of being effectively and comprehensively remedied by UILs (undertakings in lieu of an MIR) given by the banks (see the features in paragraphs 3.3 and 3.6)?
- Do you have any views on the CMA's provisional analysis regarding proposals for possible UILs being offered in principle by the four largest UK retail banks in relation to SME banking, particularly on the appropriateness, effectiveness and deliverability of such UILs (see paragraphs 4.58 to 4.71 and [Annex A](#))?
- Do you consider that a potential solution to any competition concerns identified may need to consider alterations to the structure of the markets in addition to (or in place of) remedies focused on increasing customer engagement?

The CMA would particularly welcome any specific evidence from respondents in support of their views.

1.9 Such comments should be provided no later than **5:00 pm on 17 September 2014** to:

Retail Banking Team
 Competition and Markets Authority
 Victoria House
 37 Southampton Row
 London
 WC1B 4AD

Email: retailbanking@cma.gsi.gov.uk

- 1.10 We will publish all responses on the CMA's website, except those responses marked as confidential. Respondents may request that their response be kept confidential. If you would like your response to remain confidential, clearly mark it to that effect and include the reasons for confidentiality. Please restrict any confidential material in the appendices to your response. Personal data received in the course of this consultation will be processed in accordance with the Data Protection Act 1998. Our use of all information received (including personal data) is subject to Part 9 of the Enterprise Act 2002 (the EA02) and the Freedom of Information Act 2000. Further information on the CMA's obligations regarding the protection and disclosure of information under the EA02, Freedom of Information Act 2000 and Data Protection Act 1998 can be found in CMA guidance 'Transparency and disclosure: the CMA's policy and approach'.²⁸
- 1.11 Following careful consideration of the responses to this consultation, the CMA will publish a final decision on whether or not to make an MIR, in respect of either or both of SME banking and PCAs. The CMA intends to do so later in the autumn.

²⁸ *Transparency and disclosure: statement of CMA's policy and approach (CMA6)*.

2. Legal framework

- 2.1 A reference under section 131 of the EA02 is a decision of the CMA Board to make a reference to the Chair of the CMA for the constitution of a group²⁹ (the Group) if it has reasonable grounds for suspecting that any feature, or combination of features, of a market in the UK for goods or services prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK (in this document we call this the 'reference test').
- 2.2 For the purposes of the reference test, the relevant market features can be either structural in nature or can relate to the conduct of suppliers or customers. In practice, there might not be a clear division between structural features and those relating to conduct.³⁰
- 2.3 It is important to note that the reference test is a 'reasonable grounds to suspect' test and does not require the CMA to have concluded that there are, in fact, features of a market which prevent, restrict or distort competition. This point was made clear by the Competition Appeal Tribunal in *Association of Convenience Stores v OFT*:

There is, if we may say so, some risk that one may mistake the height of the hurdle which s131(1) presents. It is a 'reasonable grounds to suspect' test. The scheme of the Act is that a full investigation is carried out at the stage of the Competition Commission not at the stage of the OFT, although admittedly the OFT has to address the matter sufficiently to decide whether there are reasonable grounds 'to suspect'.³¹

- 2.4 Where the reference test is met, the CMA has a discretion whether to make an MIR, rather than a duty. In its guidance on MIRs,³² the CMA sets out four criteria which help to guide its exercise of that discretion:
- **Scale of the suspected problem:** whether the scale of the suspected problem, in terms of its adverse effect on competition, is such that an MIR would be an appropriate response to it

²⁹ By virtue of [paragraph 36 of Schedule 4 to the Enterprise and Regulatory Reform Act 2013](#). The group of independent 'members' of the CMA selected to conduct a market investigation and drawn from the panel of such members which has been constituted under statute to conduct and take decisions on 'Phase 2' market investigations and merger investigations and certain other matters.

³⁰ [OFT 511](#), paragraph 1.9.

³¹ [CAT 36](#) [2005], paragraph 7.

³² [OFT 511](#), Chapter 2.

- **Availability of remedies and value of a market investigation and report:** whether there is a reasonable chance that appropriate remedies will be available or that an MIR report will, more generally, be of value
- **UILs:** whether it would be more appropriate to address the problem identified by means of UILs
- **Alternative powers:** whether it would be more suitable to deal with the competition issues identified by applying the Competition Act 1998 or using other powers available to the CMA or to sectoral regulators

2.5 We apply this criteria to our findings from the market studies in the subsequent chapters.

The MIR process

2.6 If, following the consultation we refer to above, the CMA decides to make an MIR, then the Group will, in the course of the ensuing market investigation, consider whether any feature, or combination of features, of a relevant market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK³³ – that is, whether any such feature has an adverse effect on competition. A market investigation must be decided within 18 months of the making of the MIR, although there is provision for an extension to 24 months if there are special reasons for doing so.

2.7 If the Group has decided in a market investigation that there is an adverse effect on competition, it must decide whether action should be taken by it or whether to recommend action by others. In doing so it should have regard to:

- the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition
- any detrimental effects on customers so far as resulting from the adverse effect on competition
- the effect of any action on any relevant customer benefits of the feature or features of the market(s) concerned

2.8 Where a report on the market investigation has been prepared and published³⁴ and contains a decision that there is one or more than one

³³ [Section 134 of the EA02.](#)

³⁴ [Section 136 of the EA02.](#) The report must be prepared in accordance with [section 137 of the EA02.](#)

adverse effect on competition, the CMA must take such action as it considers reasonable and practicable to 'remedy, mitigate or prevent' the adverse effect on competition and to 'remedy, mitigate or prevent any detrimental effects on customers' so far as those effects have resulted from the adverse effect.³⁵

- 2.9 In order to achieve that, the CMA may accept undertakings from appropriate persons or may make an Order³⁶ under section 161 of the Act. In doing so, the CMA has potentially wide-ranging powers to impose remedies, potentially applicable to several or all market participants.³⁷ The CMA has a six-month period in which to implement remedies following a final report, although that may be extended for a further four-month period.

³⁵ [Section 138 of the EA02.](#)

³⁶ [Sections 159 & 161 of the EA02.](#)

³⁷ [Schedule 8 of the EA02.](#)

3. The 'reference test'

- 3.1 In this chapter, we set out our provisional conclusions regarding whether the reference test is met. In doing so, we consider first whether the reference test is met in relation to each of SME banking and PCAs, before considering both sectors together.
- 3.2 In undertaking this assessment, the CMA notes the important similarities in the competition issues found in SME banking and PCAs (this is set out in paragraph 3.11), which we consider to be relevant for our analysis.

SME banking

- 3.3 In relation to SME banking, as set out in the accompanying market study report, we provisionally consider that there are a number of features of this sector which we suspect give rise to competition concerns. These are:
- **Persistent levels of concentration and relatively stable market shares** among providers of both BCAs and general purpose business loans (see the SME report, Chapter 4, including a description of the theory of harm on this issue).
 - **A market structure characterised by close linkages both between PCAs and BCAs, and between BCAs and general purpose business loans**, limiting the scope and speed for newer or smaller providers to expand and develop their business models (see the SME report, Chapter 4).
 - **Continuing high barriers to entry and expansion in the supply of BCAs and general purpose business loans to SMEs**, particularly the inability of smaller or newer providers to develop their businesses outside of niche, specialist areas (see the SME report Chapter 5). Such barriers include:
 - the difficulties faced by new or smaller banks to acquire sufficient numbers of profitable customers to establish a credible SME banking business, partly in consequence of low levels of shopping around and switching by SME customers as referred to below
 - the continuing need (despite a very significant increase in online and mobile banking) for an extensive local branch network to acquire new customers and distribute products effectively
 - limited access to key inputs by smaller or newer banks, particularly some evidence of concerns about access to payment systems at

commercially attractive rates (also being considered by the Payment Systems Regulator), and to information on the creditworthiness of SMEs

— regulatory barriers arising from the methodology used to assess capital requirements imposed on banks

- **Demand-side issues**, with SMEs not easily able to access, assess and act on information to ensure that they get the best deal, manifested in low levels of shopping around and switching activity (4% annually for BCA customers despite the introduction of CASS). This particularly reflects limitations in transparency and the comparability of information on the offers of different providers and SME customers' 'inertia' (ie reluctance to shop around between banks and to switch banks) (see the SME report, Chapters 6 to 8). Survey evidence of SME customers suggests that the reluctance to shop around or switch at least partly reflects a widespread belief that better alternatives are not available and that there are significant frictions in the switching process.

3.4 The CMA provisionally considers that these features, alone or in combination, meet the reference test. In particular, we provisionally consider that this sector is characterised by a mutually reinforcing pattern of demand-side problems (including customer inertia, problems in understanding the complex pricing structures and a perceived lack of differentiation between banks) and supply-side problems (resulting from market concentration and high barriers to entry and expansion). These issues seem to combine, and contribute to one another, in a complex pattern (see Chapter 10 of the SME report).

3.5 The SME banking market study (see for example, Chapter 9 of the SME report) has identified that these features may apply differently between the largest and smallest SMEs, such that competitive dynamics between these groups may well vary. In particular, we have seen more evidence of greater competition between providers for larger SMEs. Nevertheless, we continue to have reasonable grounds to suspect that competition is prevented, restricted or distorted across the SME sector. This is particularly the case in respect of concentration and aspects of demand-side issues (with, for example, some evidence of impediments to switching arising from the deeper relationship between larger SMEs and their bank).

PCAs

3.6 In relation to PCAs, as also set out in the accompanying market study update,³⁸ we consider that there are a number of features of this sector which we suspect give rise to competition concerns. These are:

- **Persistent levels of concentration and relatively stable market shares** among providers (see Chapter 2 of the PCA update).
- **Continuing high barriers to entry and expansion**, in particular (see Chapter 2 of the PCA update):
 - the continued importance of a branch network to distribute products effectively, despite the recent increase in the use of online and mobile banking
 - recent or potential entrants propose that customer inertia is one of the most important difficulties they face when trying to expand in the PCA market, due to relatively low levels of switching and shopping around referred to below
 - limited access to key inputs by smaller or newer banks, particularly some evidence of concerns about access to payment systems at commercially attractive rates (also being considered by the Payment Services Regulator)
 - the capital requirements issue referred to above for SMEs, applies also to PCAs (and indeed mortgages, personal loans and credit cards)
- **Demand-side issues**, including relatively low levels of switching and shopping around, which may be regarded as symptomatic of a ‘sticky’ market with relatively little incentive on providers to compete. Despite the launch of CASS, annual switching rates remain at only about 3% annually for PCA customers, and this is exacerbated by difficulties faced by PCA customers in comparing costs and benefits between different providers’ PCAs. Survey evidence of PCA customers suggests that the reluctance to shop around or switch is largely based on a widespread belief that better alternatives are not available. (See Chapter 4 of the PCA update.)
- **Lack of transparency in charging structures**, especially for overdrafts which are complex and increasingly varied, making it very difficult for

³⁸ See the report *Personal current account market study update* at www.gov.uk/cma-cases/review-of-banking-for-small-and-medium-sized-businesses-smes-in-the-uk.

customers to choose the best value account for their needs (see Chapter 3 of the PCA update).

- 3.7 The CMA considers that these features, alone or in combination, meet the reference test. In particular, we consider that, in common with SME banking, the PCA sector is characterised by a mutually reinforcing pattern of demand-side problems (including customer inertia, difficulty in understanding the pricing structures and a perceived lack of differentiation between banks) and supply-side problems (resulting from market concentration and high barriers to entry). These issues seem to combine, and contribute to one another, in a complex pattern (see Chapter 6 of the PCA update).
- 3.8 For these reasons, the CMA considers that there are reasonable grounds to suspect that features of the market prevent, restrict or distort competition in relation to PCAs, such that the reference test is met.

Provisional conclusion on the ‘reference test’

- 3.9 The CMA’s findings on market outcomes, particularly in relation to service and satisfaction (see Chapter 9 of the SME report and Chapter 6 of the PCA report), are consistent with this analysis of features giving rise to competition concerns and suggest that SME and PCA customers appear to be suffering poorer outcomes than they would in a well-functioning competitive market. This analysis is, however, based on a ‘Phase 1’ assessment and does not represent a finding that there is an adverse effect on competition arising from the features above.
- 3.10 The CMA’s provisional view is that there are reasonable grounds to suspect that features of both the SME banking and PCA sectors restrict or distort competition and that the reference test is therefore met.
- 3.11 The CMA further considers it appropriate to refer both the SME banking and PCA sectors for a single in-depth ‘Phase 2’ market investigation, to reflect certain important similarities in the competition issues found:
- Many of the features identified are common to both markets.
 - The products are closely related – indeed, the majority of SME owners obtain their BCA from their PCA provider.
 - The same banks are prominent in both markets.
- 3.12 In the next chapter, we consider the factors relevant to the exercise of the CMA’s discretion to make a combined MIR by reference to the products together, rather than individually.

4. Discretion to make an MIR

4.1 As we set out in Chapter 3, once the CMA has concluded that the reference test is met, there are four particular criteria which it normally considers when deciding whether to exercise its discretion as to whether or not to make an MIR. These are:

- scale of the suspected problem and whether a reference would be an appropriate response
- availability of appropriate remedies
- whether UILs would address concerns
- alternative powers available to the CMA or to sectoral regulators

4.2 In considering these factors, the CMA recognises that a market investigation leads to significant costs, both to the CMA itself (and the public purse) and to the parties involved. We understand the point made to us by a number of banks that there would be considerable time (including management time), energy and cost expended in the event of an MIR, which could otherwise be expended by the parties perhaps on competitive commercial action, including innovation. We have of course carefully considered in the application of the discretionary criteria the need for any market investigation to be proportionate and to 'add value' over and above what might be achieved using alternative approaches.

4.3 In the remainder of this chapter, the CMA considers each of the four discretionary criteria in turn, highlighting any differences by reference to their application to each of SME banking and PCAs.

First criterion: scale of the suspected problem

4.4 In determining the scale of the suspected problem, the CMA's guidance identifies three factors of particular significance:

- the size of the market
- the proportion of the market affected by the features
- the persistence of those features³⁹

³⁹ [OFT 511](#) sets out three factors relevant to determining the scale of the suspected problem; however, the CMA may take other relevant factors into consideration as appropriate.

Size of the market

- 4.5 The available evidence we have obtained demonstrates the size and importance of this market, both to customers and the economy more generally.
- 4.6 Each aspect of the two retail banking sectors under consideration constitutes a substantial sector of the UK economy:
- PCA revenues are £8.1 billion annually
 - BCA revenues from SMEs are £2.5 billion annually
 - the value of outstanding term loans to SMEs in Great Britain is some £90 billion⁴⁰
- 4.7 Moreover, the workings of the retail banking sector have a very substantial effect on consumers, businesses and the economy as a whole:
- The sector affects most (if not all) households in the country as holders of PCAs. In 2013, there were approximately 80 million PCAs, of which 65 million were active.
 - The sector affects most (if not all) SMEs (4.5 million SMEs in the UK), which typically hold bank accounts (well over 3.5 million were held in 2013). According to the Federation of Small Businesses, nearly 60% of the UK workforce is employed by SMEs.⁴¹
 - Retail banking is part of the essential infrastructure of the UK economy, facilitating personal and SME transactions and the flexibility, adaptability and viability of SMEs.
- 4.8 Given the size and importance of this sector, we provisionally consider that even small restrictions on competition would be likely to have a significant overall effect and that even small improvements in competition could therefore generate substantial benefits to SMEs and consumers.

The proportion of the market giving rise to the features

- 4.9 The available evidence demonstrates that the features of concern are widespread in nature and relate to fundamental aspects of the operation of

⁴⁰ Information on the relevant sources for the market size figures can be found in the separate market study reports.

⁴¹ See the Federation of Small Businesses [press release](#), 28 May 2014.

these sectors that have been described here, including on both the demand side and the supply side.

- 4.10 We therefore consider that a large proportion of the market gives rise to the features of competition concern.

Persistence of the features

- 4.11 In relation to both SME banking and PCAs, the available evidence demonstrates that the features we identify are long-standing in nature (with each being specifically considered by various inquiries in the sector over many years – see paragraphs 1.2 to 1.4) and, in our provisional assessment, likely to persist.

- 4.12 However, notwithstanding these concerns, during the market studies the CMA has carefully considered a number of recent initiatives and developments across retail banking which may, potentially, diminish the features of concern identified in Chapter 4. The main recent initiatives and ongoing developments can be categorised as follows:

- initiatives or developments which might directly reduce concentration
- initiatives or developments to reduce barriers to entry and expansion
- initiatives or developments to facilitate switching
- initiatives or developments to enhance transparency and comparability

- 4.13 Each of these categories of initiatives or developments, and their impact on the persistence of the feature to which it most appropriately relates, are considered below.

Persistence: initiatives or developments which might directly reduce concentration

- 4.14 The most significant, direct, structural changes which are intended to reduce concentration arise from the proposed divestments:
- of TSB from the LBG (Project Verde)
 - of Williams & Glyn from RBSG (Project Rainbow)

- 4.15 These divestments were required under EU state aid rules and are intended to facilitate the entry of new competitors or the reinforcement of a smaller existing competitor in UK retail banking.⁴²
- 4.16 As we set out in each of the relevant sections of the market study reports (see Chapter 4 of the SME report and Chapter 2 of the PCA update), the CMA notes that, although concentration levels will be reduced once each of these divestments is completed, the markets will still remain concentrated, particularly those in Scotland.⁴³ In addition, the OFT's advice to the Chancellor of the Exchequer in September 2013 on the then proposed divestments concluded that 'our market share analysis indicates that the divestments will only have a limited impact on overall structure in PCAs and SME banking'.⁴⁴
- 4.17 Moreover, in the case of Project Rainbow, the process for completion of that divestment has been delayed for several years, following the European Commission's decision of 9 April 2014, and is now not required to be completed before the end of 2017.⁴⁵
- 4.18 In addition to these proposed divestments, new entrants have emerged and these could have an effect on concentration levels in the future:
- Metro Bank has entered and expanded in both the SME banking and PCA markets, albeit so far on a relatively small scale, with a current network of 26 branches and plans to expand significantly (but not to the scale of the larger banks in the medium term).
 - Tesco Bank launched its PCA in June 2014. The account pays interest on credit balances and is linked to the Tesco Clubcard. Tesco plans to use its stores to raise awareness of the product; however, the account is sold online. Customers can carry out certain transactions (such as cash deposits) at the customer desks of Tesco's largest 300 stores, but the account is designed to be accessed primarily online.
 - Virgin Money has announced that it is developing a range of current accounts but the details of the offering have not been made public yet.

⁴² See http://europa.eu/rapid/press-release_IP-09-1728_en.htm and http://europa.eu/rapid/press-release_IP-09-1915_en.htm.

⁴³ The Northern Ireland markets remain unaffected by the divestments and therefore remains highly concentrated after Project Verde and Project Rainbow.

⁴⁴ See [letter to the Chancellor of the Exchequer](#), 11 September 2013.

⁴⁵ In April 2014, the European Commission allowed Royal Bank of Scotland Group to delay the disposal of Williams & Glyn from December 2013 (for an unspecified time, understood to be several years). [European Commission press release IP/14/410, State aid: Commission approves amendments to restructuring plan of Royal Bank of Scotland](#), 9 April 2014.

- The Post Office has conducted a pilot scheme involving 100 outlets (account servicing is available nationwide) in the East of England operating PCAs in partnership with the Bank of Ireland. Following the trial, the Post Office is now set to double the number of branches offering current accounts and by the end of September it expects that the number of branches in the scheme will rise to 239.
- It was announced in the spring of this year that there is an intention to launch a new bank (Atom Bank), which would provide SME banking services and PCAs through an online-based offer. We understand that the intention is to launch in the first half of 2015.

4.19 The CMA also notes that, in relation to SME banking, Aldermore, Shawbrook and Handelsbanken continue to expand in relation to specific customer groups or product lines. However, this is fairly small scale: the largest of these three providers, Handelsbanken, accounts for less than 1% of SME main banking relationships.⁴⁶

4.20 The developments identified above are certainly positive and promising. Furthermore, there are some encouraging signs in relation to PCAs, in particular that the seven-day switching service has been introduced and is reported to be working well, new products have been launched and there is also new entry. Nonetheless, we remain concerned that entry and expansion is on a small scale and focused on servicing particular customer groups for SMEs, and that although entry into the PCA market is inducing innovation by the larger banks, the scale of such entry is open to question. Many entrant banks maintained that PCAs were a particularly complex product to develop and that they expected only relatively slow growth after launch. As a result, we provisionally consider that such entry, expansion and product innovation is insufficient to alleviate our concerns.

Provisional conclusion on persistence of concentration levels

4.21 The CMA therefore provisionally considers that, while there have been some potentially important developments, mainly in relation to PCAs, they do not seem likely to alleviate the persistence of the concentration and relatively stable market shares in these sectors.

4.22 Overall, there has been very little movement in market shares although there is evidence that mid-size PCA providers have grown slightly at the expense of some of the larger PCA providers. However, the changes are very gradual,

⁴⁶ See Chapter 5 of the SME report.

and at the current rate they would not reduce the level of concentration back to its pre-crisis level in the foreseeable future.

*Persistence: initiatives or developments to reduce barriers to entry and expansion*⁴⁷

4.23 The CMA has also considered a number of specific developments and initiatives in relation to barriers to entry and expansion, to assess whether the features identified above are likely to persist. A brief summary of our initial assessment, considered further in the market studies, is as follows:

- **Access to branch services (PCAs and SME banking):** As set out in Chapter 2 of the PCA update and Chapter 5 of the SME report, the CMA considers that a wide network of local branches continues to be important for a provider to compete effectively in the sector as a full service provider. We recognise the rapid continued growth and usage of direct means for customers to access banking services through online or mobile channels, and the declining usage of bank branches for transactions. However, the evidence we have seen suggests that most SMEs and PCA customers still place considerable value on having a local branch for their bank. The strategies of most banks in maintaining or developing extensive branch networks (even in the case of larger banks with branch closure programmes) seems to us consistent with this. We provisionally consider that this barrier to entry is likely to persist.
- **Regulatory barriers (PCAs and SME banking):** As identified in Chapter 5 of the PCA update and Chapter 5 of the SME report, the CMA has received generally favourable feedback on the effect of recent amendments to the regulatory authorisation scheme, such that we have good grounds to believe that this concern has been materially reduced. In relation to SME lending, however, concerns still arise in relation to the impact of certain aspects of capital requirements, notwithstanding recent changes made by the Prudential Regulation Authority (PRA). We provisionally consider that these are likely to persist.
- **Access to payment systems (PCAs and SME banking):** As identified in Chapter 2 of the PCA update and Chapter 5 of the SME report, the CMA has heard widespread concerns from newer or smaller banks about the actual or believed ease and cost of access to payment systems, particularly Faster Payments. These relate both to the costs of obtaining

⁴⁷ While we have provisionally found that customer inertia is a barrier to entry, we consider this issue in relation to developments or initiatives to facilitate switching and transparency rather than in this section.

direct and indirect access, and to the service offered to those accessing the payments system through indirect access. While the evidence on this issue is currently insufficient to conclude that smaller or new banks are in fact disadvantaged, the extent and frequency of concerns about the lack of competition in indirect access to payment systems indicates at least that there is an issue to be investigated. As we discuss below, the Payment Systems Regulator (PSR), which will become fully operational in relation to the regulation of payment systems in April 2015, is already examining access to payment systems.⁴⁸ It is currently devising its regulatory approach, such that it is not possible to say at this point how it may address these concerns. However, we note the PSR's wide-ranging powers to address concerns in relation to payment systems. In particular, we note the focus of the PSR on access issues in the call for inputs.

- **Information asymmetries on customer creditworthiness (SME banking):** While a lack of information on creditworthiness of potential applicants for SME lending products appears to restrict the ability of newer or smaller banks to compete effectively with established providers (see Chapter 5 of the SME report), the government has introduced legislation to Parliament to facilitate wider access to such information. Should the legislation be enacted and then implemented, the CMA considers that these proposals are likely to address concerns arising in relation to this issue.

Provisional conclusion on persistence of barriers to entry and expansion

- 4.24 The CMA therefore provisionally considers that, while there have been some potentially important developments, they do not seem likely overall to prevent the persistence of high barriers to entry and expansion, including the continuing need for an extensive branch network to be a scale competitor in the sector.

Persistence: initiatives or developments to reduce barriers to switching

- 4.25 The most potentially significant initiative in relation to this issue has been the introduction of CASS, which was launched in September 2013, following the recommendations of the Vickers report in 2011. As we set out in the PCA update, data obtained from the Payments Council shows that in the six-month period to the end of March 2014, there was a 14% year-on-year increase in switching, and in the six-month period to the end of June 2014, there was a 16% increase over the same period. Nevertheless, switching levels continue

⁴⁸ See [call for inputs document](#).

to be low, with around 3% of PCA customers and 4% of BCA customers switching across both markets per year (including switches not made through CASS), a rate which is considerably lower than a number of other sectors we have considered.⁴⁹

4.26 Moreover, there are specific concerns when the figures are considered in more detail:

- The number of customers switching between Lloyds and TSB PCAs is greater than the increase in switchers recorded by CASS. This is likely to be a one-off occurrence, reflecting the wish of certain Lloyds and TSB customers not to be in the bank allotted to them in the LBG/TSB demerger, and suggests that the level of switching excluding the effect of the demerger could be even lower in subsequent years.
- In relation to BCAs, CASS is available for SMEs with a turnover of up to €2 million. Out of a total of over 3.5 million BCAs held by SMEs (with turnover under €2 million), just 4,650 SMEs switched using CASS in its first six months.

4.27 Although CASS has apparently made the switching of BCAs and PCAs an easier process, it has not led to significantly greater levels of switching.

Provisional conclusion on persistence of low switching levels

4.28 The CMA therefore provisionally considers that switching rates have been persistently low, weakening incentives to compete, and that the emergence of CASS, although clearly a welcome development, does not appear to be sufficient to change this fundamentally.

Persistence: initiatives or developments to enhance transparency and comparability

4.29 The CMA's analysis has also covered a wide range of initiatives that have been undertaken to improve transparency and comparability of the prices and services offered by a number of banks.

4.30 In relation to PCAs, these include:

⁴⁹ In other sectors, annual switching rates are typically 10–15% in energy, around 10% in mobile telephony, around 30–35% in car insurance, but less than 5% in digital television. The question of the significance of other measures such as 'churn' rates is considered in the summary of the CMA market study update on PCAs, July 2014.

- OFT recommendations to roll out transparency initiatives such as:
 - providing annual summaries and enhanced monthly statements
 - providing illustrative charging scenarios on unauthorised overdraft charges
- OFT recommendation to enhance the PCA price comparison website on the Money Advice Service website to enable more accurate and detailed comparisons across PCAs
- providing simplified overdraft terminology
- following the government's Consumer Credit and Personal Insolvency Review,⁵⁰ the option for customers to receive text alerts if their balance falls below a certain limit

4.31 The CMA's analysis of these transparency initiatives designed to help consumers understand and control their usage of their own PCAs is included in Chapter 3 of the PCA update.

4.32 Although these initiatives have now been implemented, in some cases this is more than two years after the initial target date. Some (albeit limited) evidence suggests that these initiatives may have resulted in positive changes in consumer behaviour. However, for many consumers, there is still confusion and a lack of understanding about overdrafts. This is primarily because overdraft charging scenarios are complex and difficult to understand. Indeed, the variety of new schemes may well have increased complexity. As a result, we consider that there is still a significant problem with consumers' ability to understand the costs they incur from their own PCAs.

4.33 Mobile banking applications and text alerts are being increasingly rolled out to consumers. There is some evidence that these tools can provide consumers with control over the costs of their PCAs, potentially leading to fewer charging events. However, many consumers still do not have the option to 'opt out' of unarranged overdrafts on many different types of accounts and, as a result, we consider that, although progress has been made, there is still room for banks to improve the level of control consumers can exert over their PCAs.

4.34 We have also found a lack of transparency with charging structures. Overdrafts remain very complex both for authorised and unauthorised charges and they have become more complex. There are a multitude of

⁵⁰ BIS, HMT, [Consumer Credit and Personal insolvency Review](#), November 2011.

charges including monthly fees, daily fees, interest and item charges and this makes it very difficult for consumers to compare the cost of PCAs across providers. This in turn reduces the possibilities of shopping around and weakens competitive constraints. It can also mean that consumers can end up paying relatively high costs for small additional loans.

4.35 Moreover, overdraft revenues overall have fallen by just 3% over the last couple of years, despite bigger falls in wholesale funding, indicating that the pricing of overdraft lending is not particularly responsive to changes in funding rates. We are concerned that banks are unlikely to have the incentive to compete on overdraft charges.

4.36 The CMA is also aware of two transparency-related developments regarding PCAs. These developments and our assessment of them are below:

- As part of the MiData initiative (see Chapter 3 of the PCA update and Chapter 7 of the SME report), a number of banks⁵¹ have agreed to provide customers with detailed account data which they can upload to comparison websites to achieve ‘bespoke’ comparison information. In June 2014 the government announced that it had secured agreement on the industry standard format for PCAs and that account providers would make it available to their customers by the end of March 2015. The downloads will include a year’s worth of PCA transactions in a single file that can be read by online tools. The government noted that comparison tool providers were already looking to create online tools that used the information. As envisaged, we consider that this should be a positive step forward and will allow consumers to compare accounts meaningfully based on their likely account usage. Nonetheless, the precise usage and effect of such a tool is uncertain, and as such, we have not attempted to predict its likely effectiveness.
- Forthcoming EU legislation on payments and banking (the Payment Accounts Directive) is designed to enhance transparency and facilitate the creation of comparison tools for PCAs (see Chapter 5 of the PCA update). Although the CMA considers the Payment Accounts Directive as a positive development, it does not go materially further than existing or planned regulatory developments in the UK.

4.37 There have been fewer initiatives regarding transparency and comparability of information for SMEs. It remains the case that there are no effective price comparison tools (we consider proposals from the banks in relation to this

⁵¹ The banks committed to MiData are as follows: Barclays, HSBC, LBG, Nationwide, RBSG and Santander. See: www.gov.uk/government/news/government-to-make-it-easier-to-check-that-youve-got-the-right-bank-deal.

issue below). However, as we set out in Chapter 7 of the SME report, the CMA welcomes Business Banking Insight, a service comparison website promoted by the Federation of Small Businesses and the British Chambers of Commerce, which enables SMEs to compare their existing bank's service offering with that available from other providers. However, this initiative is very recent, with roll-out only taking place on 28 May 2014. It is not possible at this stage to conclude on its effectiveness, particularly the extent to which it is used by customers to drive competition between providers, although we understand that they are looking at ways to improve the service further.

Provisional conclusion on persistence of transparency and comparability concerns

- 4.38 In relation to transparency initiatives in both markets, the CMA provisionally considers that, despite certain positive developments, it is not possible to say with any degree of certainty that they are likely to alleviate the persistence of the lack of transparency.

Provisional conclusion on persistence of the features

- 4.39 The CMA recognises that there have been a number of significant regulatory initiatives and other developments seeking to improve competition in retail banking. We consider that some of these changes – such as in relation to payment systems (assuming that the new Payment Systems Regulator is able to remedy any problem that does exist), authorisation of new banks and information asymmetries – are likely to have the result that the features for which the CMA currently has concerns will not persist into the future. However, in relation to the other features identified above – particularly concentration levels and stable market shares, continuing high barriers to entry and expansion, low levels of customer switching and shopping around, and lack of transparency – the CMA provisionally considers that these concerns are likely to persist for the foreseeable future.
- 4.40 The CMA notes more generally that, in these sectors, significant change has often been said to be imminent without in practice materialising.⁵² Given the available evidence, we provisionally consider that recent and forthcoming developments are not likely to cause significant change to the sector.

⁵² In the context of assessing the argument that the internet had removed the need for an extensive branch network as a barrier to entry, the Vickers report of September 2011 had noted: 'It is worth noting that in 2001, internet and telephone banking were already being pointed to as offering the potential for new entrants to put competitive pressure on incumbents' (see [Vickers final report](#), footnote 34, p176).

Provisional conclusion on the first criterion: scale of the suspected problem

4.41 For the reasons set out above, the CMA provisionally considers that the scale of the problem identified is sufficient to merit an MIR.

Second criterion: availability of appropriate remedies through an MIR

4.42 The availability of remedies and the prospective value of a market investigation is part of the CMA's assessment when considering whether to make an MIR. However, it is not for 'Phase 1' market studies to determine which remedies would or would not be appropriate for the CMA to consider in a 'Phase 2' market investigation, following the detailed analysis that is properly undertaken at Phase 2. Rather, it is sufficient that the CMA believes that there is a reasonable chance of appropriate remedies being available through an MIR by virtue of the CMA's wide-ranging powers to accept undertakings or impose an Order. We assess that question in the following paragraphs.⁵³

4.43 Nevertheless, as a result of the CMA's efforts in this Phase 1 work to consider the kind of solutions that a market investigation might produce, the CMA has had regard to the availability of the following two categories of remedies:

- behavioural remedies
- structural remedies

Behavioural/regulatory remedies

4.44 If the CMA were to find one or more adverse effects on competition following an investigation⁵⁴, it is plausible that there are a number of incremental behavioural and regulatory measures that it could apply and that might address some of the features above. A non-exhaustive list of potential remedies as regards PCAs could, for example, include:

- Enhancing the provision of information to customers through improvements to the statements they receive. Examples would be the provision of more standardised information, and the introduction of annual statements. These might enhance transparency and engagement, and so assist customers' decision-making.

⁵³ See paragraphs 2.8 to 2.9 for an outline of the remedies available to the CMA.

⁵⁴ [Section 138 of the EA02](#).

- Requiring banks to make more charges and other provisions transparent and more easily available on their websites, in order to make it easier for customers to understand what individual bank accounts are offering and compare with other accounts.
- Requiring banks who do not already do so to send their customers text alerts to warn them if they are about to go into overdraft. This may assist customers to control their usage of their account so that they only use overdrafts when it is the best way of meeting their needs.
- Requiring banks to offer their customers the option to opt out from overdrafts at no cost in all fee-free accounts.
- Intervening more directly in the conduct of parties, including the prices they may charge for overdrafts.
- Prohibiting certain charges that are particularly complex for customers to assess.
- improving redress mechanisms for complainants.

4.45 Similarly, with respect to SME banking, certain behavioural and regulatory measures might address our concerns. A non-exhaustive list of potential remedies could, for example, include:

- enhanced information to SMEs setting out BCA costs and usage, to improve the ease with which customers can compare different providers
- introduction of comparison and choice tools, to enable SMEs more readily to perceive differentiation between the offers of various banks
- requiring particular steps to be taken when an SME is sold an SME banking product (for example, a requirement for specific advice), with the aim of ensuring that they are in a position to take a fully informed decision

4.46 Other options, applicable to both SMEs and PCAs, could include compulsory access schemes, such as the requirement for incumbent banks to provide competitors (especially new entrants and smaller providers) with access to their branch network or other assets, such as payment systems, or intervening more directly in the conduct of parties, including the charges that they may levy for the focal products or the services that they must provide.⁵⁵

⁵⁵ This is, of course, similar to the transitional undertakings imposed following the CC market investigation in 2002.

4.47 In the event of a MIR being made, the assessment and design of any behavioural and regulatory remedies would, of course, be the subject of very detailed consideration by the CMA in order to facilitate their effectiveness. This is particularly important in the case of detailed behavioural remedies in complex markets, such as those set out above, where the detailed provisions of any such remedy are critical. Indeed, we provisionally consider that the Phase 2 remedies process, in itself, may be valuable to determine the extent to which effective remedies are likely to be available and, if so, to ensure that remedies are designed in an appropriate manner to facilitate their effectiveness.

Structural remedies

4.48 Structural remedies are generally one-off measures that seek to increase competition by altering the competitive structure of the market. Structural remedies might be used to change market structure by lowering barriers to entry and expansion. These remedies can often be costly and affect the property rights of the parties subject to them, and so they are not imposed lightly.

4.49 The divestment of assets is one possible structural remedy that might be imposed following a market investigation. Examples of this include the European Commission's decisions under the EU state aid rules to require divestments by LBG and by RBSG 'as an appropriate means of increasing competition on the concentrated UK retail banking market',⁵⁶ and the recommendation in the Vickers report that the LBG divestment be substantially enhanced.⁵⁷ However, this is not the only structural remedy available or the default position where there are structural concerns. Structural remedies might take various forms, for instance the structural remedies considered by the CC in 2002 in relation to SME banking (but not adopted) included:

- divestment of branches
- divestment of SME businesses without property
- divestment of SME businesses, with branches

⁵⁶ European Commission decision, [State aid Case N 428/2009 – United Kingdom: Restructuring of Lloyds Banking Group, 18 November 2009](#), paragraphs 179–188, especially paragraph 188. See also European Commission decision, [State aid case N 422/2009 and N 621/2009 - United Kingdom: Restructuring of Royal Bank of Scotland](#), paragraph 244.

⁵⁷ [Vickers final report](#), paragraph 8.13.

In addition, there could in principle be structural remedies to address vertical integration issues (such as banks' interests in payment systems).

4.50 In the context of this market, the CMA is aware of various sources which have identified structural concerns in this sector, and has advocated for structural solutions to address the long-standing competition concerns it identifies. Furthermore, the CMA is aware that such measures have already been mandated to improve competition, particularly in the case of the European Commission's requirements for divestments by LBG and RBSG, referred to above.⁵⁸

4.51 The CMA has also heard concerns about the very significant costs which would be likely to arise from any forced divestments. In particular, various parties have highlighted the direct costs associated with the divestments of:

- TSB by LBG, which we understand were of the order of £1.4 billion to date.⁵⁹ Indeed, the IT costs alone associated with that divestment were of the order of £[redacted]⁶⁰
- Williams & Glyn by RBSG, which we have been informed were of the order of £[redacted] to date.⁶¹ Of that, some £300 million was required to establish the IT systems for Williams & Glyn⁶²

In addition, we are aware of the costs to customers in terms of being forced to switch provider. Moreover, we are aware that there may be significant indirect costs associated with the management time and focus devoted to the implementation of such divestments. Finally, it is by no means certain, given the challenges associated with the divestiture of TSB,⁶³ that there would be a willing buyer for a business with an extensive network of branches.

4.52 The CMA has taken account of these concerns in its consideration of this criterion going to the exercise of its discretion. We note, as we describe above, that structural remedies do not necessarily involve divestments of the nature and scale of those required for LBG and RBSG, but also that such divestments can be required and have been required.

4.53 We also note that the features we have identified appear to us to be potentially serious in nature and long-standing, and may require interventions

⁵⁸ For example, the European Commission's decisions under the EU state aid rules to require divestments by LBG and by RBSG 'as an appropriate means of increasing competition on the concentrated UK retail banking market', and the recommendation in the Vickers report that the LBG divestment be substantially enhanced.

⁵⁹ See [Lloyds Interim Management Statement, Q3, 2013](#).

⁶⁰ LBG submission to the CMA.

⁶¹ Meeting with RBSG.

⁶² See: www.computing.co.uk/ctg/news/2297856/rbs-to-spend-gbp300m-on-williams-glyns-it-system.

⁶³ For example, the failed sale of the Verde branches to the Co-operative Group.

either to address market structure or consumer behaviour or both. At the conclusion of a Phase 1 market study, we therefore cannot rule out the possibility that structural remedies may be necessary, or at the very least be carefully considered by a Group at 'Phase 2' in the event that an MIR was made. This would particularly be relevant if the Group found that greater differentiation between providers was necessary to stimulate greater customer engagement. If that were the case, the Group would be required to take careful account (among other things) of the proportionality of any such remedy in addressing any adverse effect on competition identified.

- 4.54 However, in light of the submissions above, and before taking a final decision as to whether to make an MIR, we would welcome any views from interested parties on the potential viability or necessity of a structural solution, and particularly whether respondents to the consultation consider that a structural solution can, at this stage, already be ruled out as a realistic possibility for any market investigation to consider. The CMA is particularly grateful for any evidence parties may have on this issue to support the views expressed.

Other relevant factors

- 4.55 We do not consider that the current situation cannot be improved. There remain identifiable factors that we have reasonable grounds to suspect hamper, or may hamper, competition, and that it appears possible to ameliorate, such as that:
- SMEs and PCA customers say that they would switch more if they thought that there were better alternatives and greater differentiation in the marketplace (see Chapter 4 of the PCA update and Chapter 8 of the SME report).
 - Switching levels seem to be lower for retail banking than in other, potentially comparable, sectors in the UK (see Chapter 4 of the PCA update and Chapter 8 of the SME report) – which suggests that switching levels in retail banking could in principle increase.
 - There are barriers to entry and expansion, particularly in relation to SME banking, which could be overcome by greater switching, comparability and actual choice (see Chapter 5 of the SME report).
 - Transparency is limited both for PCAs and SME customers. This is particularly the case for overdrafts on PCAs, as the level of charge incurred is dependent upon the specific customers' account usage. As such, transparency for both PCA and SME customers could be improved (see Chapter 4 of the PCA update and Chapter 7 of the SME report).

4.56 Finally, the CMA also provisionally considers that a market investigation is likely to be of value. For a number of years, and particularly since the financial crisis, this sector has been the subject of detailed scrutiny and, most frequently, negative public comment, about the implications of the current market structure and dynamics for competition and for customers. The CMA considers that there may well be merit in a thorough, independent and expert analysis of competition in the market, building on the previous work of the OFT and others.

Provisional conclusion on the second criterion: availability of appropriate remedies through an MIR

4.57 For the reasons set out above, the CMA provisionally considers that appropriate remedies are likely to be available and that an MIR report is likely to be of value.

Third criterion: the availability of undertakings in lieu of a reference

4.58 The CMA has the power under section 154 of the EA02 to accept UILs of making an MIR. Before doing so, the CMA is obliged to: 'have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition concerned and any detrimental effects on customers so far as resulting from the adverse effect on competition'.⁶⁴ As the CMA's guidance notes, such UILs are 'unlikely to be common'. The guidance also refers to the significant practical difficulties associated with negotiating UILs with several parties, where the adverse effects have not been comprehensively analysed.⁶⁵

4.59 During the course of the SME banking market study a number of banks argued strongly that UILs would be an effective, less costly outcome to the market study, if competition concerns were identified. It was also suggested that such UILs would be likely to be capable of quicker implementation than would be possible if an MIR was made. Such arguments about the effectiveness of UILs to address any competition concerns identified were not put forward by the banks in relation to PCAs. As such, we focus the remainder of this analysis on SME banking alone.

4.60 The CMA welcomes the submissions from the four largest UK retail banks and has carefully considered them. As mentioned above, we appreciate that an MIR would not be cost free, either for parties or for the CMA. We have

⁶⁴ [Section 154\(3\) of the EA02](#).

⁶⁵ [OFT 511](#), paragraph 2.21.

therefore given careful consideration to whether we can be confident that UILs would provide as comprehensive a solution as is reasonable and practicable, consistent with our statutory obligations. In doing so, we indicated our willingness to hear in principle from the banks what UILs would cover. We have discussed with (and met) each of the four largest UK retail banks the principle of such UILs. Subsequently, we held a joint meeting with Barclays, HSBC, LBG and RBSG, to discuss their joint proposals for in principle UILs. These proposals consist essentially of three elements, all of which are purely behavioural and designed to enhance customer engagement with their banking provider:

- A website enabling SMEs to compare the price and service offerings of BCAs from different providers. In relation to business loans, the website would primarily act as a 'portal', including a link to loan providers' websites, rather than including an actual comparison of indicative loan prices of different providers because of the bespoke nature of many SME loans.
- Standardised and simplified account opening procedures.
- The development of BCA annual summaries and other activities to stimulate SME engagement (eg promotion of CASS to SMEs).

Further specific detail on these UILs may be found in [Annex A](#).

4.61 Although the CMA considers that there may be merit in the banks' submissions that customer engagement could be enhanced in the ways suggested, the CMA has provisionally decided that we cannot be confident, at this stage, that such UILs would provide as comprehensive a solution as is reasonable and practicable to the adverse effect on competition concerned. In undertaking this assessment, the CMA has considered the following issues:

- the appropriateness of such UILs
- the effectiveness of such UILs
- the feasibility of such UILs

4.62 Our provisional assessment of the UIL proposals in respect of these issues is set out below.

Appropriateness

4.63 Although the CMA has conducted a considered analysis of the operation of the SME banking sector, the analysis it has conducted is only of the depth

that can reasonably and viably be conducted in a Phase 1 analysis. The CMA provisionally considers that an MIR is merited, at least in part, in order to gain a deeper understanding of the effectiveness of competition in the market and the issues affecting it. These include the causes of behavioural concerns manifested in the low levels of shopping around and switching, and an assessment of the significance of concentration and market structure on the provision of banking services to SMEs. The interactions between market structure and customer behaviour are complex. While considered during the market study (see Chapter 4 of the SME report), these interactions have not been the subject of the detailed analysis that would inevitably follow an MIR.

- 4.64 As might be expected in a Phase 1 market study, the CMA has not yet assessed comprehensively the nature and extent of any adverse effect on competition, and so cannot at this stage be reasonably confident that any remedies offered would constitute as comprehensive a solution to the adverse effect on competition as is reasonable and practicable. It is possible that the competition concerns are driven primarily by behavioural and demand-side issues, such that if an MIR was made, it could result in remedies not significantly different in their general nature from what is proposed in the UILs. It also remains a possibility that, following a Phase 2 market investigation, some of the concerns would be more appropriately remedied by structural measures rather than, or in addition to, behavioural remedies (see earlier discussion in paragraphs 2.8 and 2.9 on the possible remedies). To date, no structural remedies have been proposed by any of the banks; indeed, a number of the banks have insisted that no structural remedies are necessary or appropriate.

Effectiveness

- 4.65 In order to design appropriate undertakings which the CMA could be confident could provide as comprehensive a solution as is reasonable and practicable to the adverse effect on competition concerned, the CMA would need to be persuaded of their likely effectiveness. The CMA considers that robust evidence and appropriate testing are likely to be essential before it is possible to engage in detailed design of any remedies.
- 4.66 This is particularly relevant in the case of behavioural remedies in complex markets, such as the SME banking market, where the relative success of the remedies is largely dependent on the effectiveness of their detailed design, and particularly the impact that they have on customer behaviour, which is an inherently challenging process. This is likely to require detailed evidence as to the likely impact of particular measures on actual customer behaviour.

4.67 None of the banks has so far provided sufficient evidence to persuade us of the likely effectiveness of their proposals in respect of UILs. In particular, none has been able to highlight any circumstances in which similar remedies in any other market have had a significant beneficial impact on addressing similar concerns to those which we set out above.

4.68 As we note above, in contrast to a process designed to obtain UILs, the CMA during a market investigation has a well-developed remedies process which is specifically designed to test the effectiveness and proportionality of various potential remedies, including detailed external consultation. Furthermore, the CMA may, following a market investigation, use its order-making powers, which is more likely to be conducive to achieving effective remedies (as well as feasible remedies – see the next section) than the complex negotiations with multiple parties all with different interests which would be required to reach agreement on UILs at Phase 1.⁶⁶

Feasibility

4.69 Moreover, the CMA notes that, in the light of the market study conclusions, which relate to the whole of the UK, at a minimum a UIL package would need to apply to all the large banks throughout each of the geographic markets we have identified in the SME banking market study. This would mean that UILs would likely need to be offered by at least eight banks. While the four largest UK retail banks have approached the CMA with a proposal, this does not include the agreement of any of the banks in Northern Ireland (albeit the agreement of Ulster Bank may be inferred from its position as a subsidiary of the RBSG) or of other banks in Great Britain. The CMA, based on the extensive remedy-making experience of both the CC and the OFT, and as suggested by the MIR guidance,⁶⁷ does not currently consider that it is likely to be feasible to obtain agreement from so many organisations on an effective package of what may well be a complex and wide-ranging set of undertakings, in a highly complex sector. Indeed, the CMA notes that the maximum number of parties which have previously been included in UILs was three, and that was in a considerably less complex field.⁶⁸ An Order following 'Phase 2', on the other hand, could have wide coverage, both of the largest retail banks and other relevant market participants (including any which emerge in the future, but do not currently exist).

4.70 In any event, we note that the banks proposing UILs have also said that the CMA should accept UILs because the banks do not want to delay progress on

⁶⁶ See [Guidelines for market investigations, CC3](#), Part 4.

⁶⁷ [OFT511](#), paragraph 2.21.

⁶⁸ [Extended Warranties UIL \(2012\)](#).

making worthwhile improvements to the operation of the sector. We welcome their willingness to move quickly in this area, and note that it is obviously open to them to take appropriate action outside the context of UILs should they choose to do so. We also do not consider that UILs of the scope proposed would be quick to negotiate and implement.

Provisional conclusion on the third criterion: the availability of undertakings in lieu

4.71 For the reasons set out above, the CMA provisionally considers that it cannot be confident that UILs could provide as comprehensive a solution as is reasonable and practicable to the features that the CMA has identified may prevent, restrict or distort competition in the SME banking sector. However, we welcome views on our analysis of the UILs being proposed by the four largest retail banks in relation to SME banking and, in particular, will carefully consider any submissions and evidence from respondents which specifically address the potential concerns regarding UILs set out above before taking a final decision on this issue. The CMA is also interested in the perspectives of all interested persons on the UIL proposals, particularly the views of SMEs and their representatives. In particular, the CMA would welcome any observations as to the likely effectiveness of such UILs in addressing the features we have identified in Chapter 4. Moreover, the CMA would welcome any observations on what, if any, enhancements to those UIL proposals, or alternative UILs, would be likely to prove effective in practice. Submissions on this issue should ideally set out clearly the evidential basis for the views expressed, where possible, highlighting examples of behavioural remedies that have previously been found to be effective.

Fourth criterion: alternative powers

4.72 Finally, the CMA has considered whether alternative powers are likely to be available to the CMA or others to address the features which it has identified in Chapter 4. We begin by considering the CMA's powers in relation to the competition law prohibitions on anticompetitive agreements or abuse of a dominant position,⁶⁹ before considering the powers available to other regulators, most particularly the FCA, PRA and PSR.

⁶⁹ The Chapter I and Chapter II prohibitions contained in [sections 2 and 18](#), respectively, of the Competition Act 1998 and their counterparts in EU law, Articles 101 and 102 of the [Treaty on the Functioning of the EU](#).

Other competition powers of the CMA

4.73 The CMA has not found evidence of any agreement or conduct that may involve an infringement of the competition law prohibitions. Instead the features of concern we have identified are broader than the issue of firm conduct, which those prohibitions are intended to address, and relate to the overall functioning of the markets.

Other sectoral regulators

4.74 The CMA has worked with the FCA and the PRA as we have developed our analysis in the market studies. The SME banking market study has been produced jointly with the FCA. The CMA also received valuable insights from the FCA relevant to the PCA sector. However, unlike the SME banking market study, which has been a formal collaboration, the PCA report is solely a CMA output reflecting the fact that it is intended as an update of the market review published in January 2013 by the CMA's predecessor body, the OFT.

4.75 Earlier in this chapter we specifically considered whether various initiatives currently being undertaken by those regulators, as well as by government departments, would be sufficient to ensure that the features of concern would no longer persist. As noted there, we have found that, in some instances, these regulators have addressed or are likely to address our concerns, such that the use of these alternative powers would be appropriate:

- The PRA has been, and continues to be, engaged in significant work in making the authorisation of new banks easier and faster.
- The FCA is planning to conduct valuable work on matters that are relevant to the problems we are considering, and on the effectiveness of CASS, and alongside this they will commence a study of the costs and benefits of account number portability as a way of increasing competition in banking. The FCA is also continuing its work on overdrafts and has published the qualitative consumer research⁷⁰ that was carried out as part of its consumer credit work.
- The new PSR (now established and which will be fully operational in the regulation of payment systems in April 2015) is considering questions of access (among other things) and is expected to develop that work further.

4.76 However, despite these initiatives, the concerns we have identified in this market study, particularly that there are long-standing and interlinked aspects

⁷⁰ [Consumer Credit Qualitative Research: Credit Cards & Unauthorised Overdrafts](#), 7 April 2014.

of competition concern on both the demand and supply sides, are precisely the types of concerns which the market investigation regime was established to investigate and, where necessary, remedy. Indeed, the CMA considers that a joined-up approach to the features, rather than focusing on individual aspects, would have significant benefits.

- 4.77 Many of these initiatives (such as the FCA's proposed work on the costs and benefits of account number portability) are unlikely to be complete by the time the CMA decides whether to make an MIR. In any event, a market investigation would monitor and take account of this work.
- 4.78 Moreover, the initiatives being undertaken by the relevant regulators, which we expect to be important and valuable, are unlikely to address the features identified in Chapter 4 comprehensively.

Provisional conclusion on the fourth criterion: alternative powers

- 4.79 For the reasons set out above, the CMA provisionally considers that alternative powers are likely to be less appropriate than an MIR in addressing the features identified above.

Provisional conclusion on discretion to make an MIR

- 4.80 For the reasons set out above, the CMA provisionally concludes that it is appropriate to exercise its discretion to make an MIR.

5. Scope of an MIR

- 5.1 In light of the foregoing, the CMA is minded to make an ‘ordinary’⁷¹ MIR, within the meaning of section 131(6) of the EA02, in respect of the markets for the provision of retail banking services to SMEs and the provision of PCAs. The draft terms of reference are set out in [Annex B](#). We would welcome respondents’ comments on that draft.
- 5.2 The CMA is obliged, in the terms of reference, to set out a description of the goods or services to which the feature or combination of features concerned relates. As stated in the guidance on the making of MIRs, the CMA is not, however, obliged to provide a precise definition of the market or markets to which any MIR relates. This reflects the fact that no market definition exercise is typically conducted during a Phase 1 assessment.⁷²
- 5.3 In particular, in relation to SME banking, while the CMA has focused on particular focal products during its market study, it has not determined that they constitute a relevant market or markets for the purposes of determining the terms of reference.
- 5.4 The CMA notes the close linkages between BCAs and various forms of finance available to SMEs (see Chapter 4 of the SME report). This makes the imposition of unduly narrow terms of reference for any MIR inappropriate: at the Phase 1 stage, the nature and extent of such linkages may not have been fully explored. The CMA has therefore not sought to do so in the draft terms of reference in [Annex B](#).

⁷¹ To distinguish this reference from a ‘cross-market’ reference.

⁷² [OFT 511](#), paragraph 2.28.

ANNEX A: Summary of joint UIL proposals in relation to SME banking

1. The CMA met Barclays, HSBC, LBG and RBSG (referred to in this summary as 'the participating banks') on 18 June 2014 to discuss their 'in principle' joint proposals for UILs in relation to SME banking.
2. The participating banks have suggested that their proposals will build on the progress achieved to date in enhancing customer outcomes, specifically by:
 - supplementing existing initiatives and expediting their impact
 - providing an opportunity for a market-wide and holistic approach to any remedies
 - allowing benefits to materialise at least two years in advance of any potential Phase 2 outcomes
 - potentially permitting more flexibility than the Phase 2 process for liaising with the regulators/decision-makers in developing and trialling the proposals
3. The participating banks have said that, if these proposals are supported by the CMA, they would be willing to further develop the detail of the proposals. The participating banks have indicated their interest in establishing a 'user group' to provide oversight of the proposals as these are developed, to maximise stakeholder involvement and to review, 'stress-test' and trial the proposals. They say that participation by other banks would be welcomed and to their advantage given the benefits to customers that the participating banks envisage as arising from their proposals.¹

The joint proposals

4. The proposals are comprised of three elements, each of which is considered to be mutually reinforcing:
 - (a) comparison website and loan portal;
 - (b) account opening standards; and
 - (c) BCA annual summaries and stimulating SME engagement.

¹ RBSG also noted that Ulster Bank, which is part of RBSG, would be happy to participate in principle, although it also noted that the viability of the proposals in Northern Ireland would require a critical mass of banks. With the exception of Ulster, the main banks in Northern Ireland are different from those on the mainland and therefore RBSG has suggested that any Northern Ireland roll-out would be best undertaken as a second stage.

Proposal 1: comparison website and loan portal

5. The participating banks consider that an independent, combined comparison website and loan portal (referred to here as 'the website') for BCAs and standard SME business loans would allow easy comparisons to be made across a range of parameters, including key features and service quality, and (for BCAs) price. The participating banks consider that the website would enhance competition and benefit customers by significantly improving comparability (and, therefore, transparency), reducing search costs and time, and enhancing customer engagement. Moreover, the website would lower barriers to entry and expansion, making it easier and more efficient for existing and new providers to access informed customers.
6. The website would be open access, such that all finance providers would be equally encouraged to participate. The participating banks would seek accreditation by an independent third party and establish a code of practice to offer assurance to SMEs that the website is independent, impartial and reliable.
7. It is intended that the website would be linked to the new 'Business Banking Insight' website,² developed jointly by the Federation of Small Businesses and the British Chambers of Commerce, and the participating banks are exploring how best to achieve this. To ensure the commercial viability of the website, the participating banks would provide subsidy/sponsorship funds to establish the website, with prospective website operators bidding on the level of subsidy in a reverse auction process. The participating banks would commit to promote the website on their own websites, in branch and in customer literature (including referencing the website in the new annual summary – see Proposal 3). The participating banks would anticipate and encourage co-promotion of the website by industry stakeholders such as the British Bankers' Association, the Federation of Small Businesses and the British Chambers of Commerce. The participating banks do not anticipate any ongoing regulatory involvement after the initial start-up phase on the basis that the ongoing effectiveness of the website will be assured by the commercial incentives of the website operator and third party accreditation.
8. With regard to the development and implementation of the website, the participating banks would seek to agree key milestones with the CMA, such as: the appointment of an independent project coordinator (to drive the project forward and provide regular progress reports); the selection of the website

² See www.businessbankinginsight.co.uk.

operator; website design and development; trialling and website refinement; promotion and marketing; launch.

Comparing BCAs

9. SMEs will be able to use the interactive comparison tools to compare standard tariff BCAs, which will benefit smaller SME customers in particular. Having provided certain key data (such as customer details, direct debit/standing order usage, channel usage, cash processing, cheque and card usage), SMEs will be able to compare:
 - price
 - key account features (eg provision of relationship manager, available channels)
 - bank satisfaction ratings/scores from the Business Banking Insight and 'customer-generated' ratings/scores based on feedback from website users (such as that used by the TripAdvisor website)

Loan portal

10. In relation to business loans, the website would primarily act as a 'portal', including links to loan providers' websites. Customers would be able to compare the satisfaction ratings and scores of different loan providers using the Business Banking Insight results and 'customer-generated' ratings/scores based on feedback from website users (such as that used by the TripAdvisor website).
11. The portal would provide links for customers through to (a) loan providers' own websites and (b) other key resources and contacts (eg brokers) and would be intended to become the 'go-to' website for SMEs looking to obtain a business loan.

Proposal 2: account opening standards

12. The proposal is to standardise and simplify BCA account-opening procedures, resulting in a 'common form, common data, common evidence' approach which should streamline the BCA opening process across the sector. Common initial data points and supporting evidence requirements would result in greater standardisation of essential customer due diligence (CDD) requirements, such as 'Know your Customer' and 'Know your Business'. Further, customers can at any time request from their current bank a 'CDD data pack' for submission to a new bank should they wish to switch. The

common form will make clear in advance precisely what information ‘refresh’ is necessary in terms of Know your Customer and Know your Business.

13. The participating banks consider that the potential impact of the streamlined and common account-opening process will be significant – there are about 500,000 new SMEs every year requiring a BCA. In addition, they say that the proposal should enhance competition for start-ups and switchers as customers would be more acquainted with the account-opening process and would know that, for any subsequent switching, account-opening data could be substantially ‘recycled’. It should thus make customer acquisition easier for the banks(s) with the most attractive offers. Non-UIL signatories could choose whether to compete with their own approach to account opening or could opt in to the ‘common form, common data, common evidence’ approach.
14. The participating banks’ intention is for the changes proposed to account opening to be of universal interest and appeal to all banks regardless of size. User group input and testing would be sought and the participating banks are content for the process to create ‘common form, common data, common evidence’ to be under the auspices of the CMA, FCA or British Bankers’ Association as appropriate and at the CMA’s discretion. The participating banks consider that this proposal does not reduce Anti-Money Laundering protections and requires no legislative changes. Nonetheless, the participating banks welcome input from the FCA, CMA and other regulatory bodies.

Expected customer experience

15. For those customers that fall within the low risk category on initial review as determined by the bank to which they are applying (and who are anticipated to represent a significant majority of SME customers), it is anticipated that no further CDD information would be required. Account-opening forms will be made available online for downloading and printing, along with clear instructions as to what is required for verification, either in person at a bank branch, or online or via the telephone.
16. Customers will be made aware that they can readily obtain their ‘CDD data pack’ to present to the new bank for switching purposes to avoid ‘re-inventing the wheel’. The ‘common form’ will make it clear in advance precisely what ‘refresh’ (eg utility bill from the last 12 months etc) might be required to supplement/update the customer’s CDD data pack if the customer is considering switching provider. Importantly, the participating banks consider that this proposal would respond to any potential customer concerns that each bank takes its customers through a different process.

Proposal 3: BCA annual summaries and stimulating SME engagement

17. The final proposal concerns the development of BCA annual summaries and other activities to stimulate SME engagement on an ongoing basis via a customer communication programme. The participating banks consider that this proposal will raise SME awareness of different competitive offerings, improve the ease of comparison, thereby driving greater switching, and encourage the usage and therefore the commercial viability of the proposed comparison website.
18. As part of the SME customer communication programme, participating banks would:
 - regularly promote the account-opening standards, the website and CASS
 - work with the Payments Council to promote CASS to potential users. This may include directing participating CASS funding contributions towards targeted SME advertising campaigns
 - provide annual summaries of BCA usage charges to SMEs, thereby increasing transparency, raising customer awareness of BCA costs and enabling more informed comparisons between offerings and, as such, enhancing the effectiveness of the comparison website (see Proposal 1 above).
19. Promotion of CASS, the BCA comparison website and loan portal (see Proposal 1) and ease of account opening (see Proposal 2) would be achieved via an obligation on each participating bank to prompt SME customers in communications sent on two occasions:
 - Where banks offer an initial period of free or lower-priced banking services and that is about to end: to encourage the customer to consider the bank's services against those on offer from competing suppliers, with links to the comparison and CASS websites and reference to the account-opening standards, together with a brief explanation of how each service works
 - Annually: annual summaries of BCA usage charges would again include prominent reference and explanation of the comparison and CASS websites (with links) and account opening standards

ANNEX B: Draft terms of reference

The Competition and Markets Authority (CMA) in the exercise of its power under sections 131 and 133 of the Enterprise Act 2002 hereby makes a reference to the Chair of the CMA for the constitution of a group under Schedule 4 to the Enterprise and Regulatory Reform Act 2013 for an investigation of the supply of retail banking services to personal current account customers and to small and medium-sized enterprises.

The CMA has reasonable grounds to suspect that a feature or a combination of features of the market for the supply of those services in the United Kingdom prevents, restricts or distorts competition.

For the purposes of this reference:

- 'retail banking services' means:
 - in respect of personal current account customers, provision of an account marketed to individuals rather than businesses, which provides the facility to hold deposits, to receive and make payments by cheque and/or debit card, to use automated teller machine facilities and to make regular payments by direct debit and/or standing order but does not include:
 - an account in which money is held on deposit in a currency other than the official currency of the United Kingdom; or
 - an account in which credit funds are held and offset against mortgage debt or a loan (other than an overdraft facility);
 - in respect of small and medium-sized enterprises, provision of services including but not limited to general purpose loans and liquidity management services, including business current accounts and overdrafts.
- 'small and medium-sized enterprise' means a business that, in respect of a given financial year applying to it, has annual sales revenues (exclusive of VAT and other turnover-related taxes) not exceeding £25 million.