Competition and Markets Authority: Retail Banking Market Investigation – Notice of possible remedies

Response from the Social Market Foundation

November 2015

The Social Market Foundation welcomes the opportunity to respond to the CMA's proposed remedies for the retail banking market. Our comments concentrate on the remedies proposed for the personal current account (PCA) market as this has been the focus of our research in this area.

The SMF broadly agrees with the provisional findings of the investigation and supports the CMA's proposed remedies.

There are clear problems in the PCA market at present. As the CMA has identified, low income customers and those who rely on their overdrafts are poorly served. But other segments of the market are working better, as the SMF's recent report *Playing the Field* established. Older, financially confident and affluent consumers are successfully shopping around, multi-banking or switching providers to take advantage of higher interest rates on credit balances or cash bonuses.[1] Consumers who engage with the market can get a very good deal.

But too many consumers aren't active in the market – and they are often those with the most to gain from switching. The complexity of the market at present disempowers some of these consumers, making it very difficult to compare offers and nerve-wracking to switch. The CMA has correctly identified the issues on the demand side of this market, and is right to focus on interventions which are most likely to help this group of more vulnerable. Our responses on specific remedies are below.

Broadly, the SMF are optimistic about the possibilities that consumer data and related tools offer in this market. We believe that technological developments will make it much easier for consumers to search for the right PCA and could also help motivate them to search. But we would call on the CMA to consider recommending the introduction of a partial switching service, accelerating moves to force banks to share data with third-party providers and put a clear deadline for the development of an API standard for the sector in place, to ensure the consumers can benefit from the stronger competition we think these innovations will unlock.

Remedy 1 – Prompt customers to review their PCA or BCA provider at times when they may have a higher propensity to consider a change.

The SMF would support this remedy in principle. In other financial services markets where consumers are prompted to renew their contract on a regular basis, for example car insurance, competition is stronger[2] and there is significant evidence that proximate messages such as text messages are particular effective at changing consumer behaviour in financial services.[3] In our opinion, these messages should be seen as a regulated communication, in a similar way to terms and conditions, with protecting consumers and promoting competition given equal billing in the FCA's remit. On this basis the content of these messages should be standardised to ensure the framing problems discussed by the CMA do not arise. Furthermore, the CMA should stipulate that these messages should include a prompt for consumers to access the improved midata service set out in Remedy 3. A direct URL embedded within a text message, an in-app notification or email would be the most direct way of encouraging consumers to take action. Rather than linking to the original provider or a price comparison website, consumers could initially be directed to a landing page holding a list of all sites offering comparison services using midata. This should be hosted be on the FCA's website, as part of their competition remit.

In the SMF's view, these messages should be sent by providers to their customers around the trigger points listed in the Notice of Proposed Remedies. Forcing providers to inform customers of their ability to shop around, and handing them the tools to do so, particularly at times of trouble, may have the secondary benefit of encouraging banks to invest in IT and other elements of customer services to reduce the threat this poses to their business. And given that providers already have the ability to market their own products to customers in this way this does not represent a disproportionate burden on firms.

Existing research shows that the way in which these messages are sent, the tone and the content can have a dramatic impact on effectiveness. We would thus expect significant trials of these messages to maximise the benefit of this relatively costly intervention. The SMF believe that prompting done well, for example by text message when a consumer goes in to their overdraft, can help consumers take control of their PCAs. But we would note that there is inevitably a limit to the effectiveness of these interventions – many consumers won't respond to even the best placed messages. If we are expecting firms to bear the costs of this intervention, it's key that it is designed in such a way as to maximise consumer benefit.

Remedy 3 - Facilitate price comparisons between providers by making customer-specific transaction data more easily available and usable, including by PCWs

The SMF wishes to express particular support for the CMA's proposed Remedy 3. As the CMA have correctly identified, consumers' difficulties in accessing and assessing information about the cost of their PCA and the relative cost of services offered by other providers is a significant barrier to competition in this market.

This stems not just from the complexity of pricing structures used by banks, but also from consumers' difficulties in understanding their own behaviour. As we increasingly understand the psychological processes behind this behaviour[4], it is right to design policy around the true behaviours of consumers rather than for hypothetical rational homo economicus. The problems consumers face in understanding how they use their own account – for example the tendency to underestimate overdraft use – mean that simply providing customers with price information, even in a simplified form, will not be sufficient to improve outcomes.

The SMF believes that technology presents a solution to these issues.[5] Rather than presenting consumers with price information, which we know they won't be able to process, an improved midata service would allow consumers to receive personalised recommendations on the basis of their own past use. While past behaviour isn't always a good guide to the future, in this case it will at least allow consumers to accurately compare the costs they could face across a wide range of accounts and providers. Midata also has potential to improve the ability of banks to advise potential customers on their overdraft eligibility, by giving them access to much the same data as current providers use to make these decisions.

As the CMA recognises, however, the current iteration of midata fails to provide these potential benefits to customers. The UK's banks are already working together to develop an API standard which should avoid these difficulties. Given the centrality of this development to strengthening competition in the PCA market and that some market players may have a vested interest in making it harder for consumers to access this data and delaying progress, a clear deadline for the development of the API standard is needed. The SMF would suggest that a failure to meet the specified deadline should induce financial penalties across firms – which could be used to pay for further consumer advertising of the current account switching service (CASS) and midata. Rather than pushing for interim measures, which we know, given levels of financial capability[6] and consumer responsiveness to these messages are unlikely to be effective, the CMA should instead encourage banks to focus on accelerating the midata programme as much as possible.

Though midata is a positive development, we must recognise that provision of comparison tools will only increase competition to the extent that consumers are motivated to access these tools. When 46% of consumers have never even considered changing their current account provider[7], it isn't clear that improving access to information on alternative offers, even with more and more timely prompting to do so, will change consumer behaviour on a significant scale. However the SMF believe that other, day-to-day uses of consumer PCA data could help engage these otherwise inert consumers.

One such possibility is the growth of financial aggregators. These tools, such as Mint and OnTrees, allow consumers to summarise all their financial activity across a range of products in a single interface and provide mobile budgeting tools. The day-to-day usefulness of these tools means they may be taken up by a wider section of the population, including those consumers who would not usually consider switching. But, with access to customers' usage data, these tools can also offer suggestions of other products which may provide better value, in the same way as a price comparison website with midata could. As such, these aggregators could potentially help consumers both to become more aware of and modify their own financial behaviour, and to find better value products without needing to specifically set out with the intention of shopping around. They could help overcome the motivational barriers to switching, as well as the information problems.

At present, however, take up of financial aggregators is much lower in the UK than in other advanced economies, particularly the US and Canada. This appears to be because some providers consider the use of these tools, which use online banking log-in details to gain read-only access to an account, to be a violation of terms and conditions, leaving consumers who use them potentially liable for any fraudulent activity on the account whether or not it is related to the use of the aggregator. With most aggregators using the same data platforms as the banks themselves, this seems unnecessarily strict and appears to be reducing consumer willingness to adopt these otherwise valuable tools. In its final recommendations the CMA may wish to consider whether UK banks' attitudes towards these tools is an attempt to block the competitive threat they may pose by reducing ability to cross-sell and educating consumers about products from other providers. While the implementation of PSD2 should remedy some of these issues within the next two years, we would argue that this is already significantly reducing consumer value and that the CMA should push for more prompt action to ensure consumers have access to aggregator services.

Remedy 5 – Enable consumers and SMEs to make comparisons between current account providers on the basis of their service quality

The SMF would support the CMA's assertion that there is, at present, a lack of competition between UK banks on the basis of behaviour. Our research finds that although consumers know how they want banks to behave, they struggle to identify which providers are best meeting those expectations.[8] While information on quality of customer service is available from organisations such as Which? and Fairer Finance, consumers must go and hunt for this information. There is a clear need for information on the broad behaviour of the UK's financial services providers to be more easily accessible so consumers can properly translate their preferences on service quality into purchasing decisions.

The SMF would argue that the Banking Standards Board (BSB) could helpfully lead this work by forming an umbrella body with other industry stakeholders including consumer organisations, academics and regulators. The BSB is already collecting much of the data that would be needed to help consumers track bank behaviour, and bringing this together with the information collected by organisations like Which? would help consumers access all the information they need to make an informed choice in one place. Presenting this information in a consumer-friendly fashion, for example, as a dashboard, league table or kitemark, would help consumers interpret it, and avoid duplication of effort between organisations. We hope that making this information more visible and comparison simpler would increase the salience of bank behaviour as a dimension of competition and incentivise better behaviour across the board. In addition to online publication, scores should be clearly displayed at the point of sale and on relevant literature, much like energy ratings on electrical products, to help consumers make an informed choice.

Remedy 7 – Make it easier for prospective PCA customers to find out, before initiating the switching process, whether the overdraft facilities they were seeking would be available to them from another provider.

The SMF agrees with the CMA's conclusion that consumers using overdrafts are particularly disadvantaged in the PCA market at present. We agree that the inability of a consumer to know if they will be offered the same overdraft, or indeed any overdraft, before switching, is a significant barrier to competition for these consumers, and that they have substantially more to gain from switching.

We believe that requiring banks to provide customers with a firm decision on an overdraft before initiating the switching process would be a significant step forwards. But rather than considering separate actions, we suggest that the CMA should investigate whether midata could be used to this end. With access to information about the consumer's spending habits, use of their current PCA and overdraft, banks should be able to undertake the same assessment processes as used with their existing customers. Incorporating overdraft comparisons fully into midata would avoid the need for additional intervention, while ensuring that consumers have the information they need to make an informed decision about their PCA.

Measures to improve the switching process – Remedies 8, 9, 10, 11

The SMF would agree with the CMA that lack of consumer confidence in CASS remains a barrier to switching. However we would urge against the adoption of account number portability (ANP) in Remedy 8. As consumers increasingly interact with their banks through mobile phones and specialist apps, account numbers are likely to become less relevant over time. Already consumers can send payments through their mobile phone numbers or twitter handles without needing to share account numbers and sort codes. There is little evidence that ANP would encourage switching, given that most barriers appear to be at the search stage rather than at the actual switching process, and given the likely costs we do not believe this would be an effective intervention. Using non-bank identifiers, like mobile numbers or twitter handles, could mirror the system successfully used in Sweden, where consumers have a separate identifying number which can be moved between bank accounts by providers.[9] This does require a separate tier of infrastructure, however as banks are already building the capacity to direct transfers using twitter identities and mobile numbers the cost of this is likely to be reasonable. This solution also avoids the problem of payments being directed to the wrong account, and negates the need for an extension of redirection.

The proposal to require banks to retain and provide ex-customers with details of their PCA transactions over the five years prior to their account closure on demand (Remedy 9) is imminently sensible. As with midata, the SMF believes that data should belong to the user, rather than the provider, and as such should be freely accessible to consumers to allow them to leverage it to get the best deals. Given that consumers already have a right to this data, but may have to pay and face a significant delay for papers to be sent, we would support the proposal for customers to be automatically sent their data when closing an account, when ensuring they have a record of their activity is likely to be the last thing on their minds. In the recent SMF report *Should switch, don't switch: Overcoming consumer inertia*, we propose the development of a unified data portal which would allow consumers to hold all their information about consumer services in one place. While such a system is beyond the immediate remit of the CMA's current review, in future this or a similar system could help to ensure that consumers have full access to their usage data.[10]

We are not convinced of the need for Remedy 10 – Requiring Bacs to transfer continuous payment authorities on debit cards when switching through CASS. Though many consumers do use continuous payment authorities, in reality it's very little hassle to type in a new debit card number when prompted by a service provider. Without any consumer polling evidence to suggest that this is discouraging consumers from switching, the benefit of this remedy seems unlikely to justify the probable costs.

The partial switching service considered in Remedy 11, by contrast, could be of substantial value. The close-and-switch service offered by CASS at present works for providers, but it can make the process seem final in a way which is daunting for customers. We know that substantial numbers of consumers are already choosing to switch partially, or gradually, moving payments manually over time to avoid disruption. For some groups – those most vulnerable to cash flow issues, with low credit scores or reliant on overdraft lending – this type of switch is likely to be preferable. Building a switching system which gives consumers greater control over what they switch when, therefore, should be an immediate goal for the industry. This may encourage multi-banking, which is already driving stronger competition and encouraging banks to make more compelling offers across a certain strata of the market, helping a greater number of consumers to benefit. Though the incentives on offer for switching may be lower for partial switchers, these incentives largely aim to 'pull' customers from other providers. A partial switching service, by contrast, may empower a greater number of consumers to switch on the basis of 'push' factors such as poor customer service.

Remedies the CMA is not minded to consider further

The SMF welcomes the CMA's efforts to remedy failures in the PCA market at source, rather than relying on output controls. Price controls, whether maximum overdraft charges, minimum interest rates on balances or a ban on free-if-in-credit (FIIC) banking would all be difficult and costly to implement in this market. As the CMA notes, there is little evidence to suggest that FIIC banking and the lack of a visible price point is the cause of weak competition in the PCA market. We have already seen some market participants move away from FIIC towards fee-based accounts, and succeed in doing so[11], while consumer research from PwC suggest that consumers are aware that they already pay for their PCA in other ways, and prefer to do so.[12] Moreover, the CMA's proposed remedies, if implemented correctly, would provide a simple, personalised way to compare the costs and benefits of accounts. Combined with prompt messages and reminders of the midata service, as proposed above, this would increase the visibility of the cost of a customer's account, without needing to broach the difficult technical (and costly) questions of how to calculate foregone interest etc.

The CMA is equally justified in their decision to avoid taking further structural action. Although the UK's incumbent banks do continue to have some advantages, these are increasingly being eroded by technology – and strengthening demand side competition through initiatives like midata and prompting consumers should accelerate this process. The structural break-ups proposed and implemented in the UK to date have done little to change real levels of competition, instead creating smaller versions of similar banks. Rather than considering this further, the CMA may wish to consider the likely impact of the forthcoming bank surcharge on smaller providers, and the role of the FCA in promoting diversity as well as competition.

Issues we would advise the CMA to consider further

The SMF would challenge the CMA to be more future-focused in their work. While the CMA has done well in exploring the way today's technologies could strengthen competition in the PCA market, the pace of change means these could look very different in only a few years. If the remedies set out by the CMA are to have lasting value in promoting stronger competition in the PCA market, it is important the CMA keeps looking ahead.

In particular, we would argue that the CMA has failed to engage with the growth of organisations acting as gateways to PCAs, for example third-party payments services providers and aggregators. Over the next few years, these organisations are likely to play a growing role in the way consumers manage their money. Platforms like Apple Pay, Paypal, along with aggregators like OnTrees and Money Dashboard, are going to substantially change the way consumers interact with their current accounts. We can easily see a future where the first port of call for a transaction is not a bank but the type of intermediary described above.

Firstly, by allowing customers to manage several different accounts from one platform, these intermediaries may help to strengthen competition in the current account market. With access to consumers' usage data, they could also begin to perform market search activities and recommend lower cost products that would meet the customer's needs, in the same way that price comparison websites could do this with midata. The growth of these intermediaries could also change the nature of the relationship consumers have with their PCA providers; banks become less visible to their customers as intermediaries take up the front line functions of payments management. This could boost competition by giving consumers the tools and confidence to shop around, knowing that the third party interface they rely on day-to-day would stay the same even if their provider switched. But it could also reduce their oversight of banks, and lead to a reduction in service quality.

Furthermore, these changes are likely to have a significant impact on the PCA business model currently operated by banks. The free-if-in-credit model currently dominating the market is partially funded by charges on payments and through foregone interest. These sources of income could fail as consumers use other platforms for payments and automated services help consumers manage their money to maximise interest; much in the same way that some stores are already offering to monitor use of consumable goods like light bulbs and send replacements automatically, aggregator platforms with their broad data on a consumer's financial situation could set up transfers to meet outgoing direct debits and automatically move cash to where it will get the best returns when it's not needed. This could well bring about pricing changes in the PCA market, and potentially a move away from FIIC banking.

This future-gazing exercise looks beyond the current market situation to consider how competitive pressures in the PCA market may evolve over the coming years. Given the current pace of change, and the importance of data in the CMA's existing provisional recommendations, it would be worth considering these potential developments to ensure the competition policy developed today will remain fit for purpose in the near future.

Given the likely scale and breadth of change in the sector in coming years, it is also crucial that regulators, government and competition authorities coordinate their activities. In finalising its recommendations it is vital that the CMA works closely with the FCA, Payments Systems Regulator (PSR) and the Treasury, all of which have a stake in and are currently undertaking work around data provision and system access. The CMA's goal of an open, competitive PCA market driven by data can only be achieved if all of these agencies work together, and we would encourage the CMA to coordinate these efforts.

ABOUT THE SOCIAL MARKET FOUNDATION

The Social Market Foundation (SMF) is an independent public policy think tank. We are not politically aligned and have members from across the political spectrum on our Board of Trustees and Advisory Panel. Our work spans public service reform and the social market economy, and champions ideas that marry a pro-market orientation with concern for social justice. Since its inception in 1989, the SMF has gained an enviable reputation for the rigour of its research, driving policy debate based on sound argument and clear evidence.

ENDNOTES

[1] Katie Evans, *Playing the Field: Consumers and Competition in Banking*, (London: Social Market Foundation, 2015)

[2] Ben Richards, *Should switch, don't switch: Overcoming consumer inertia* (London: Social Market Foundation, 2015)

[3] Financial Conduct Authority, *Message received? The impact of annual summaries, text alerts and mobile apps on consumer banking behaviour*, Occasional Paper No. 10 (London: Financial Conduct Authority, 2015)

[4] For further details see Ben Richards, *Should switch, don't switch: Overcoming consumer inertia*, (London: Social Market Foundation 2015)

[5] Katie Evans, *Playing the Field: Consumers and Competition in Banking*, (London: Social Market Foundation, 2015)

[6] With one in five UK consumers unable to identify the account balance on a bank statement, according to recent data from the Money Advice Service/ UK Financial Capability Board, it is likely to be unrealistic to expect the majority of consumers to be able to take the prices of various PCA services (for example, arranged vs unarranged overdraft fees), to calculate the charge for their typical usage and to compare this to other providers. UK Financial Capability Board, *Financial Capability Strategy for the UK,* (London: UK Financial Capability Board, 2015)

[7] Financial Conduct Authority/YouGov, *Current Account Switch Service – effectiveness and potential enhancements* (London: Financial Conduct Authority/YouGov, 2015)

[8] Katie Evans, *Good Culture: Does the Model Matter in Financial Services?* (London: Social Market Foundation, 2014)

[9] Australian Government, *Banking Services: Switching arrangements*, (Canberra: Commonwealth of Australia, 2011)

[10] Ben Richards, *Should switch, don't switch: Overcoming consumer inertia*, (London: Social Market Foundation, 2015)

[11] Santander have been the biggest beneficiaries of CASS to date in the PCA market, despite charging £2 a month for their 123 account, as illustrated in bacs CASS facts and figures release http://www.bacs.co.uk/Bacs/DocumentLibrary/CASS_dashboard_-_published_22_July_15.pdf

[12] PwC, *There's no such thing as a free lunch: Why fees are the future for current accounts*, (London: PwC, 2015)