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Tesco Bank is one of the UK's leading challenger banks, serving over 6 million customers across the UK. We have been actively engaged throughout the Competition and Markets Authority's (CMA's) investigation, sharing insight from our experience as a new entrant into the Personal Current Account (PCA) market, as well as findings from our own consumer research.

Following the CMA's invitation to comment on the alternative suggestions put forward as part of the Retail Banking Market Investigation, Tesco Bank has a number of comments which we trust will be helpful.

The CMA provisionally found that "a combination of low customer engagement, barriers to searching and switching and incumbency advantages in the provision of PCAs in both GB and in NI is leading to [Adverse effects on competition]". We agree with this conclusion and believe this to be the most significant issue affecting the current account market. It is, therefore, vital that when we consider new remedies, we focus on those remedies that are likely to have the most significant impact on customer engagement.

Many of the proposals detailed in the alternative suggestions paper attempt to engage customers through requiring standardised information to be disclosed to customers, both at the start and during the life of the PCA, in a clear and understandable format. However, we currently have requirements in place for the disclosure of information such as fees, charges and interest payable to customers, including regular statements. These have not resulted in customers actively engaging in their financial planning and can in fact, sometimes result in the opposite outcome, as the disclosure and presentation of charging models can be complex (particularly for overdrafts). Our customer research tells us that this complexity makes it difficult to understand what they pay for their account and what they receive in return and how that compares with other accounts available in the market.

There is a difference between 'transparency' and 'disclosure'. The Financial Conduct Authority (FCA) has found this in their work on Smarter Communications and is working with the industry to identify a simpler way for customers to understand financial products, rather than burden them with complex and jargonistic communications. Looking to increase transparency of the cost of a PCA, for example, can assist customers in making a more informed decision, as the comparison across different products and providers in a simple manner will encourage active assessment and selection.

Tesco Bank has consistently argued that increasing transparency of the true costs customers incur when using their current account (including for overdrafts) is most likely to have a material impact on customer engagement. This is why we have proposed using a simple traffic light labelling system to make it clear to customers both the value and the cost of their account, and critically, how it compares to others in the market.

This 'sunlight remedy' aims to improve consumer awareness, ability to assess value relevant to their own needs and would complement more sophisticated price comparison tools which allow those considering a switch to assess the options available. While we have previously shared details on how the traffic labelling system might work in our previous submissions, for convenience this can be found in the Appendix to this letter.

We note that a number of 'price control' remedies have been proposed by other parties. While we do believe there are examples in the market of banks applying excessive charges, particularly for arranged and unarranged overdrafts, we agree with the CMA's concerns that implementation of price control remedies may bring unintended consequences for customers. Standardising price structures has been tried previously in financial services, such as the introduction of CAT-standard savings and investment products some years ago. This restricted the ability of providers to offer the flexibility and choice that customers demanded with the result that the products were not widely taken up by customers. If we look at the decrease in the cost of unarranged overdrafts over the last few years, this has been primarily driven by the public focus on these costs so that consumers became more aware of them. The traffic light labelling system will drive this further.

Mandating price or price structures can force smaller, challenger banks out of the market. The commoditisation of PCA's will mean the incumbent banks that derive greater benefit from their lower cost of funds, lower capital requirements and scale are able to price the standard products in a way which will compete challengers out of the market. Challengers will no longer be able to compete on more innovative pricing and benefits for customers.

We note the focus on unauthorised overdrafts and the practice of honouring transactions prior to checking if sufficient funds are in the account at that time in the paper. The fact that customers regularly use this service indicates there is a customer need. In particular, it helps consumers deal with unanticipated circumstances. Requiring customers to actively opt-in to this does not take account of consumer biases, which indicate that they are not generally well able to anticipate future changes in their circumstances that might mean they would want a transaction paid (eg an important utility bill). It can also often happen that payments are made when there seems to be sufficient funds in the account, such as when a cheque is paid in and the account credited but does not clear.

We therefore believe that the CMA's focus should be on increasing customer engagement so that customers provide a strong incentive for banks to price fairly. As the CMA's provision findings state, "With greater customer engagement we would expect banks to have stronger incentives to compete and develop products to benefit all customers which are clearer to and valued by customers."

Finally, it is Tesco Bank's view that it isn't clear that these additional potential remedies will have sufficient benefit in changing the market to outweigh the cost burden. We are conscious that the costs of implementing these remedies will disproportionately impact smaller players due to the benefits that economies of scale can offer the incumbent banks. The system changes required will have a set cost whether a provider has a large or small number of accounts. Additionally, through increasing operational complexity, the proposed suggestions may also deter potential new entrants. For these reasons, we urge the CMA to focus attention on a small number of remedies that will substantially improve transparency and drive customer engagement. We believe, following customer feedback, that the traffic labelling system would be a simple and powerful tool in driving engagement.

Yours sincerely

David McCreadie
Managing Director, Banking

Appendix 1: Traffic Light Labelling

Why are we proposing a traffic light labelling system?

Over the last 12 months we have conducted extensive research into the current account market, speaking to more than 1,000 customers. The research highlighted a number of barriers to effective competition in the current account market, some of which have been addressed by the industry (for example, ease of switching) and some of which have not.

The research found that current accounts are more than just a simple transactional product. The practical and emotional ties which customers hold in their current accounts are significant and should not be underestimated. It should not, therefore be surprising that switching levels are low.

One of the most significant barriers customers face when they do decide to switch is being able to understand which account is right for them. Tiered interest rates, complex overdraft charging structures and a multitude of different reward and cash back initiatives makes it extremely difficult for customers to understand the value offered by the account they currently have, let alone how it compares to others on the market. And thus far the industry has failed to find a way of effectively communicating this information in a way that makes it easy for customers to make the right choice for them.

As a result, many millions of customers pay more for their bank account than they need to - with the CMA estimating that the average customer stands to save as much as £70 per annum by switching, and heavy overdraft users standing to save as much as £260 per annum.

While we recognise that for many customers price considerations are only one factor in deciding where to bank, we believe that customers have the right to understand exactly what they are paying, and what they get in return. Our research shows that for the majority of customers this is not currently the case and we have proposed the traffic light labelling system as a means of addressing this issue.

What does the traffic light system cover?

The traffic light system has been designed to provide clear and concise information to customers regarding pricing - specifically credit interest and overdraft charges. It focuses on these factors because customers have told us they believe they are the most important considerations when comparing accounts. Furthermore, they are typically the areas where customers can stand to gain the most by switching.

How does the traffic light proposal work?

The traffic light labelling systems we have proposed covers three key price indicators: credit interest, arranged overdraft charges; and unarranged overdraft charges. Credit interest and arranged overdraft charges are both split into three tiers to give customers the best indication of account value based on how they use their account. Each price indicator is assigned a red, amber or green colour code depending on how it compares to other accounts on the market. Figure 1 shows how the traffic light system would be applied to three popular accounts currently available in the market.

The ratings system included in our proposal was designed by Andrew Hagger at Money Comms.

Figure 1



Where would this be displayed?

The labelling system would only have value for customers if it was displayed prominently in customer communications. We would propose that it be included in all PCA marketing and advertising materials, as well as appropriate communications with existing customers.

Has this been tested with customers?

Yes. The system we propose has been designed based on insight from our own customer research and has been tested and refined based on customer feedback.

Why does it not cover other benefits like cashback schemes?

Customers told us that most banks already invest significantly in communicating the details of any benefit schemes associated with accounts. The traffic light scheme has therefore been designed to focus on the aspects of account pricing customers feel are most important but also most difficult to compare.

How would it be implemented?

Customers told us that any rating system would need to be independently managed and could not be set by an individual bank or banking industry body. The independent body would be required to work with the industry to establish the red, amber, green rates. Individual ratings would need to be updated when products change and the rating scheme would need to be reviewed at regular intervals.

What was the research methodology?

Tesco Bank commissioned TNS to conduct a programme of quantitative and qualitative research during the summer of 2015. The research included 7 focus groups which took place in Glasgow, Birmingham and London and a quantitative study which was conducted amongst a nationally representative sample of 1061 current account holders.