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Which? response to the CMA's invitation to comment on additional remedy suggestions

Summary

In our response to the CMA's provisional findings and notice of possible remedies, we outlined our view that the existing remedy proposals do not sufficiently address the issues faced by overdraft users.

The CMA's analysis shows heavy overdraft users to be less likely to switch than other users despite having faced much higher financial incentives to switch than other users over a prolonged period. It follows that remedies that focus solely on the switching process cannot reasonably be expected to address the detriment these customers face. As such, Which? welcomes the further consultation on additional remedy suggestions to consider how this consumer harm can be addressed.

Which? proposed a package of remedies that focus on generating a shift in the way customers are treated, and not all parts of our package of additional remedies are included in the CMA's invitation to comment. It is our understanding that the CMA intends to consider the other parts of our package within the context of its initial set of possible remedies. For example, we understand the CMA to be actively considering our proposal about the use of consumer engagement panels as a potential mechanism that could facilitate the implementation of, or otherwise form part of, remedies associated with the development of prompts and service quality measures, and how banks should treat their customers who maybe experiencing financial difficulties.

While we do not object to remedies being considered in this way in principle, our focus in presenting these remedies is not primarily on switching. Rather, we consider that these remedies also need to focus more directly on promoting culture change within banks. Which? continues to urge the CMA to look beyond switching, and to carefully consider how best to promote a culture in which banks treat their customers more fairly. Furthermore, what is meant by fair treatment should itself be subject to adequate consumer engagement and testing.

The issue of how banks treat their customers is inextricably linked to our proposal that the charges for unarranged overdrafts should be the same as for arranged overdrafts. Which? is pleased that the CMA has recognised the measures we proposed to directly address the harm associated with overdraft charges. However, the CMA must bear in mind that this was proposed as part of a wider package of remedies that also included a broader set of measures aimed at prompting and supporting culture change that would result in banks treating their customers in a fairer and more honest way.

As such, it is critical that, when considering the possible impact, or unintended consequences, of preventing a price increase for unarranged overdrafts, the CMA considers

what other parts of a package of remedies should be in place to control those consequences, such as how a bank treating its customers fairly should respond. The CMA must consider how different remedies interact to create a coherent package, and not look at individual remedies in isolation.

Comments on specific remedy proposals identified in the invitation to comment

The Financial Services Consumer Panel's (FSCP) proposal that unarranged overdraft charges should be subject to the price cap for high-cost short-term credit

We recognise the motivation for the FSCP's proposals: comparison with the high-cost short-term credit price cap highlights just how costly it can be to secure short-term credit through the use of an unarranged overdraft, particularly when the level of unarranged borrowing is relatively low but high fixed daily unarranged overdraft charges are applied. However, we do not consider that this remedy would be likely to fully address the harm faced by heavy overdraft users.

The FSCP's proposal would involve carrying across a price cap that was developed as a response to one set of policy concerns relating to 'emergency funds', to unarranged overdraft usage. However, the circumstances of unarranged overdrafts differ markedly from those typically associated with payday lending and other short-term high cost lending contexts. In particular, those contexts involve customers making discrete and clearly identifiable decisions in terms of accessing credit. By contrast, unarranged overdraft usage is often characterised by a lack of clarity and the absence of any specific decision.

Fundamental to the problems associated with unarranged overdraft charges are the circumstances in which they arise. The fact that a customer is seeking to use an unarranged overdraft indicates that they are experiencing some difficulty managing their money, whether that reflects short term issues, or more fundamental and ongoing difficulties giving rise to financial distress. This raises the question of how banks should act when those circumstances arise, and how that compares to how they currently act.

As we have previously highlighted, central to this is the importance of banks treating their customers fairly. In relation to unarranged overdraft usage, banks should proactively develop tools and measures that help customers improve the effectiveness of their account management, including the management of any shorter and longer term financial difficulties they may have. From this standpoint, when a customer exceeds an arranged limit, particularly on a number of occasions, they should expect that to trigger particular proactive efforts from the bank to assist with their position, including through alerting the customer to what that position is, and helping them to identify potentially desirable options.

In practice, however, banks respond to the trigger of a customer seeking to use an unarranged overdraft by applying charges that are many times higher than those which apply to arranged overdrafts (whether or not additional funds are made available). Furthermore, this is in a context where, having shown themselves to be a heavy overdraft user, the customer has signalled to the bank that they are particularly unlikely to switch.

The CMA found that 14% of PCA revenue comes from unarranged overdraft charges, and yet there appears to be little justification for applying any unarranged overdraft charges at all. While there may have been a historic justification for high unarranged overdraft charges to manage exposures associated with the provision to customers of significant pre-

guaranteed funds, this justification now appears to be outdated. Instead, the effect of unarranged overdraft charges now is to target substantial price increases on those who are already struggling in one way or another to manage their finances, and who are least likely to switch.

The extent to which banks earn revenue from the application of these charges undermines the incentives for banks to respond to their customers in appropriate and proactive ways. Our proposal that unarranged overdraft charges be set at the same level as arranged overdraft charges addresses this incentive issue, and provides a basis for banks to focus more on assisting their customers.

First Trust Bank’s proposal for a UK-wide extension of the requirement on certain Northern Ireland banks to provide customers with relevant information including about charges and interest.

This information provision requirement would be unlikely to have a material impact on heavy overdraft users and does not sufficiently address the concerns related to unauthorised overdrafts. In light of the FCA’s assessment of the impact of annual summaries, which found that they had no effect on consumer behaviour in relation to incurring overdraft charges, altering balance levels or switching, it is unlikely that this additional remedy would have any greater effect.

Lloyds Banking Group’s (LBG) proposal for additional behavioural remedies

As part of our package of additional remedies, we suggested that the CMA should consider how banks can use additional prompts and control mechanisms to assist customers to manage their accounts.

LBG’s suggestion is consistent with our proposal. However, as we noted in our response to the CMA’s provisional findings and notice of possible remedies, attention should also be given to those who are not assisted by text alerts and mobile apps, particularly given the CMA’s assessment that less engaged customers, who tend to be less financially sophisticated and/or less confident in using the internet, are likely to be particularly affected by competition problems.

The CMA’s invitation to comment says that it considers remedies of the kind suggested by LBG would be variants on its proposed prompts to overdraft users. However, the CMA’s approach to remedy development, as set out in the notice of possible remedies, was focused on switching. That is, the explicitly defined purpose of this prompt remedy was to increase awareness of the potential benefits of switching and prompt further investigation of other current account providers. We agree with LBG that prompts and other tools should be considered as a means of improving customer control of their activities with their existing current account provider, and not simply as a means of promoting consideration of switching.

In our response to the CMA’s provisional findings and possible remedies, we pointed to evidence of the significant impact that text alerts and mobile banking tools have had for some customers in terms of improving their control when using their current account, and in avoiding unarranged overdraft charges. Given this proven success in improving customer control, we urge the CMA to consider how such prompt-based control measures and buffer zones/grace periods may be further used to benefit customers, including those who are less likely to benefit from the existing use of text alerts and mobile banking options.

The CMA should consider LBG's suggestion, but we consider such changes to be complementary to, rather than a substitute for our proposals with respect to unarranged overdraft charges.

Indeed, we consider current unarranged overdraft charging arrangements to be a significant impediment to the effective development of customer tools for account management. With a significant proportion of banks' PCA revenue coming from high unarranged overdraft charges targeted at inactive and inattentive users who are particularly unlikely to switch, bank incentives are not well aligned with the interests of their heavy overdraft using customers.

Without addressing this underlying incentive problem, the impact of behavioural remedies aimed at improving customer control is likely to be limited. Banks will continue to face a strong financial incentive to apply substantial price increases to those who face difficulties managing their account activity and who are unlikely or unable to switch.

Royal Bank of Scotland's (RBS) proposal that banks should be prohibited from providing unarranged overdrafts unless a customer had actively opted in to this

It is difficult to comment fully on this proposal without understanding more details of how RBS envisages it would work, such as the terms of what the customer would be opting in to, and when the opt-in would take place.

However, in a situation where a customer has opted in to overdraft arrangements, it seems odd to describe the outcome to be an 'unarranged' overdraft. Absent other changes, this proposal would create a situation where the bank and the customer make a clear arrangement for the customer to be able to seek access to funds in excess of a defined limit. The bank may then provide that access, and if it does so, will apply charges that are much higher than it would for overdraft usage below the defined limit. Such an arrangement would appear to remain an opportunity for the bank to apply much higher charges for the provision of an arranged 'unarranged' overdraft, without any clear justification.

We would also welcome further details on whether customers would still be subject to unpaid item charges if they choose not to opt in to using an unarranged overdraft. If they were, then they could be worse off than at present: they would be subject to a high charge, but would receive no benefit associated with the potential to access additional funds. As an alternative, in our package of remedies we proposed that unpaid item charges be removed, arguing that they appear to be a relic from legacy payment methods and are no longer justified.

It should be noted that for customers who choose not to opt in, and are able to avoid the currently very high unarranged overdraft charges and not suffer other financial detriment as a result of their decision, this proposal could have some benefit. That said, whether customers would choose not to opt in is likely to depend on how the available options are presented and optimism bias issues associated with overdraft usage are likely to continue to be important. Furthermore, if banks remain able to earn much higher amounts from unarranged overdraft charges, then their incentive is likely to be to encourage consumers to opt in, rather than develop alternative control and flexibility options to assist those who may not want to opt in.

TSB's proposal for a 'credit passport'

This proposal targets the provision of information on the level of arranged overdraft that a customer could expect to be offered by a competing provider. As such, it merits consideration as a potential means of implementing the CMA's existing 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'*.

However, it is highly unlikely that this remedy would address the identified consumer harm faced by heavy overdraft users, where the very high levels of charges are driven, to a large extent, by unarranged overdraft usage.

Tesco Bank's proposal for a standardised traffic light labelling system

Tesco Bank's traffic light suggestion merits further consideration, but as with all other possible approaches to prompting, it is important to subject proposals to consumer testing. Measures that aim to standardise information are welcome but particular difficulties can arise when such highly simplified approaches are adopted, in a context where what matters to consumers can differ markedly. The CMA should only consider this proposal following rigorous consumer testing.

TSB's proposal for a standardised monthly bill

This suggestion also merits further consideration, but also must be subject to consumer testing. This is particularly the case in light of the FCA's findings concerning the lack of impact of the introduction of annual summaries.

The suggested requirement that information on interest foregone be provided in a standardised manner also raises a range of difficult issues concerning how such a figure should be calculated and how consumers are likely to interpret and respond to such information. In the current interest rate environment, and given the CMA's provisional findings concerning where the main consumer harm currently lies, it is not obvious that efforts to develop such an approach would be sufficiently justified or targeted on prevailing problems at present.

Virgin Money's proposal that personal current account providers should be required to pay their customers credit interest on current accounts at or above a minimum level.

Virgin Money's proposal would not address the key areas of consumer harm that the CMA has identified. It would represent a significant intervention in the market, but the justification for such an intervention does not look to be well supported by the CMA's assessment.