COMPETITION AND MARKETS AUTHORITY
RETAIL BANKING MARKET INVESTIGATION

Notes of a hearing of a Banking Roundtable
held at Competition and Markets Authority, Southampton Row, London
on Tuesday, 24 November 2015

PRESENT:

FOR THE COMPETITION AND MARKETS AUTHORITY

Alasdair Smith - Chairman
Tom Hoehn - Member
Philip Marsden - Member
Jill May - Member
Ed Smith - Member

FOR THE STAFF

Joanna Benison - Inquiry Director
Julie Bon - Director of Economics
Colin Garland - Director of Remedies, Business and Financial Analysis
Veronica Mansilla - Assistant Director of Economics
Victoria Palmer - Assistant Legal Director
Robert Whithard - Economist
Chris Whitcombe - Assistant Director of Economics

FOR BANKS

Julia Cattanach - Tesco Bank
David McCreadie - Tesco Bank
Sarah Williams-Gardener- Starling Bank
Richard Hemsley - Virgin Money
Andrew Emuss - Virgin Money
Ben Ruffels - Virgin Money
Jay Sheth - Virgin Money
Ant Warrington - Yorkshire Building Society
Sarah Alton - Yorkshire Building Society
Paul Lynam - Secure Trust Bank
Will Curley - Tesco Bank
David Rockliff - Tesco Bank
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THE CHAIRMAN: Welcome to all of you. Thank you all very much for coming to this meeting. This is the first of our series of roundtables and hearings in response to our Provisional Findings and Remedies Notice.
We are obviously very keen to hear views, from everyone interested in retail banking, on our work so far. That would be a major assistance in guiding the rest of our programme of work.
A very warm welcome to you all let us start with introductions and then I will hand over to Joanna, who is going to conduct the meeting. I am Alasdair Smith, I am the chair of the retail banking inquiry group.
Q. (Ms Benison) Joanna Benison, I am one of the two inquiry directors on the investigation.
A. (Mr Lynam) I am Paul Lynam. Chief executive of Secure Trust Bank
Q. (Mr Smith) Ed Smith, inquiry member.
A. (Ms Alton) Sarah Alton, Yorkshire Building Society.
A. (Mr Warrington) Ant Warrington, from Yorkshire Building Society.
Q. (Ms May) Jill May, inquiry member.
Q. (Ms Mansilla) Veronica Mansilla, assistant director of economics.
Q. (Mr Garland) Colin Garland, director of remedies, business and financial analysis.
Q. (Ms Palmer) Victoria Palmer, assistant legal director.
A. (Ms Cattanach) Julia Cattanach, for Tesco.
A. (Mr McCreadie) David McCreadie from Tesco.
Q. (Mr Hoehn) Tom Hoehn, inquiry member.
Q. (Mr Marsden) Philip Marsden, inquiry member.
A. (Mr Hemsley) Richard Hemsley, chief banking officer, Virgin Money.

A. (Mr Emuss) Andrew Emuss, general counsel, Virgin Money.

A. (Mr Sheth) Jay Sheth, head of economics, policy and public affairs, Virgin Money.

A. (Mr Ruffels) Ben Ruffels, head of public affairs, Virgin Money.

A. (Mr Strachan) Michael Strachan, head of communications, Tesco.

A. (Mr Curley) Will Curley, director of transactional banking, Tesco Bank.

A. (Mr Rockliff) David Rockliff, Tesco Bank.

Q. (Mr Whithard) Robert Whithard, economist.

Q. (Mr Witcomb) Chris Witcomb, assistant director of economics.

THE CHAIRMAN: Okay, thank you very much. Joanna, over to you.

Q. (Ms Benison) Thank you. Welcome and, as Alasdair said, this is one of the first response roundtable hearings that we are conducting following the publication of our Provisional Findings and Remedies Notice.

We have sent a presentation to participants in our roundtable and we very much hope you that you had a chance to look at it. This will set the scene for what we are trying to cover today. Our main objective is to talk about what is next. What remedies we are proposing and what we can do.

THE CHAIRMAN: Sarah, welcome. I am afraid you have missed the round of introductions and I think we will not do it again but people have their names in front of them. Welcome, I am glad you are here.

Q. (Ms Benison) Just to continue, so the focus of today is to get your feedback on our proposed remedies but, we would really welcome your views on Provisional Findings as well, so we will try to make sure that throughout today we have sufficient time to cover everything.

Just a very brief overview of where we are in the process. You might have seen it in the slides. I am looking at slide number three, so as I said we have just published our Provisional Findings and Remedies Notice and the next big milestone in our 18-month inquiry is provisional decision on remedies and that is planned to be published in February. That will then be followed by our final report and the statutory deadline and that is 5 May next year.

The objective today is to discuss our remedy proposals. The way we structured the conversation is very much around those proposals, so we would like to first focus on our remedies around shopping around and switching, particularly on PCAs, given the participation today, but also, if we can, on BCAs as well.

In particular, we will cover the consumer journey, starting from the awareness then moving to assessing and accessing information around available products and then moving to acting on it and the actual switching. As you may remember from our Remedies Notice, our package of remedies is structured around that consumer journey.

We will also like to cover today SME lending. We realise that not all the attendees have business in this area but if we can still try to cover certain questions around that that would be appreciated. Towards the end, we will also try to give the floor to you to talk about the remedies that we may not have thought about. We would really welcome any fresh ideas from the participants today and also talk about what we highlighted in our Remedies Notice that we are not at this stage minded to pursue. However, as it is a provisional stage and for remedies it is a very early thinking, then obviously there is an opportunity to move the agenda forward and introduce or revisit what we have done so far or potentially introduce new ideas.

I would like to also remind everybody that you are in the presence of your competitors, so can you please keep that in mind in making your statements. As is our usual practice, as you can see the conversation is being recorded and will be transcribed and that transcription will be published on our website. You will obviously have an opportunity to look at the transcription before we publish it.

I will try to keep an eye on the watch and move the conversation forward as much as we can but today is really for our Panel Members to explore with you any questions that they have. With that in mind, unless there are any questions?

We will obviously take a break at some point and we will have lunch around 12.30 pm. We plan to finish at 2.00 pm, so we will try to keep that lunch to a minimum and have a working lunch if possible, depending on the conversation, but I will let you know as soon as the conversation reaches that point. That is it from me, are there any questions?

A. (Mr Emuss) Just in terms of the time allocations, between the various topics and you said towards the end we will talk about remedies not pursuing or other potential remedy options, what sort of time period will we allocate to that?

Q. (Ms Benison) The time allocations are very much equal among the various agenda items, so we will just make sure that there is a huge chunk of time that is allocated to that.

If there are no other questions, I suggest we move to the first agenda item, which is around shopping around and switching. Tom will start with some questions around awareness and our remedies related to prompting customers to look around and switch.

Q. (Mr Hoehn) Thank you. This is very much to start off the discussions and we would like to hear from you. What we want to discuss are the various remedies, particularly those measures to promote engagement and get customers to consider switching to alternative providers. The two remedies that I would like to focus on or ask you to focus on are first the Remedy 1, prompting customers to review providers at certain times, then, looking at increasing awareness of potential savings, improvements in quality of service, rewards if you were to switch.

First of all, I am interested in your views on the proposed general approach of using triggers to prompt customers and we can maybe first talk about PCAs. So over to you, what do you think are the main trigger points that would lend themselves for PCAs? Anyone to go first?

A. (Mr McCreadie) I can give a few thoughts and comments, if you like. I think we have supported anything that can find this greater engagement so that more people will at least consider whether there is a better option out there for them. It is quite clear from our experience and our research that most customers feel that money going in and money going out to their PCA, current account, tends to work pretty well most of the time but probably does not open their minds enough or, through lack of transparency, to what the alternatives might be.

We think some of those ideas around potential trigger points around service failure or IT systems etc could be helpful, but I am not sure why we would just restrict to when there has been an incident like that. I think it would be better to try to engage a wider population of consumers in actually just understanding the alternatives better.

Certainly, we would probably favour a view where once a year there is a requirement to let customers know what it has cost them, in that prior 12-month period. All aspects of costing, for having their time with their existing provider. That gives some introduction to the fact there might be alternatives that may better suit their needs. I think maybe the concept of a once a year reminder of what might be out there and the fact that a switching service exists and no doubt later on we will get the chance to talk about our traffic light labelling system, we have suggested. That might be a package of things. Why restrict it to consumers when they have felt a failure. Why not just try to promote it to everyone, the fact there might be a better option out there.

Q. (Mr Hoehn) Any other comments about being proactive once a year?

A. (Mr Lynam) Yes, can I just endorse some of what David said. I think it is worth bearing in mind that even though Royal Bank of Scotland and Natwest suffered its catastrophic failure of IT in 2012, it did not suffer a vast outflow of business either in the PCA or the BCA effectively. Those banks that are gaining net market share tend to be those banks that paid a highest bribe to customers to come and join them.

So Halifax and Santander which have been the two biggest net gainers and Halifax are paying £150. Just recently, you saw Nationwide paying £200 to get people to join them. There is a differential, I think, between the prompt and the pull. The systemic banks that already enjoy significant benefits are best placed to use their inherent firepower to bribe customers.

The prompting could actually make things worse instead of making things better. The other point in the context of the implicit cost to the consumer, I think you have, as David said, quantified that at £70 per customer per annum. If base rates go back to 5 per cent, a 1000 per cent differential between current base rate and 5 per cent, the inherent cost to the consumer could rise quite considerably. Unless the consumer knows either by receipt of some form of invoice or statement that details how much they are implicitly paying, I do not think prompting in isolation is going to be a particular effective remedy.

A. (Mr Hemsley) I would certainly echo from our perspective that final point that Paul raises that prompting, in and of itself will drive objectivity into the market. It has to have a purpose and needs to have information about the financial cost or opportunity wrapped around it, to make it effective. We think that transparency around costs is still materially lacking in the current account market and it is unlikely to be addressed through the range of options that are currently on the table.

Q. (Mr Hoehn) Very much a combination of Remedy 1 and 2, is what you are saying, Richard.

A. (Mr Hemsley) That is it.

Q. (Mr Hoehn) Yes.

A. (Ms Williams-Gardener) The other thing that I would add is you had in your report quoted the 4 largest banks have collectively loss less than 5 per cent of their customers over 10 years. One of the things we have found from research that we have done is the reason people are not switching, triggers or no triggers, is because 85% say there is not very many alternatives offered out there. They see all the big banks as being the same.

In order to energise the market and one of the reasons why Starling and some of the other new entrants are coming into the market is to offer something that is very, very different.

A. (Mr McCreadie) I think from our perspective, I do not think I would concur with the view that there is not a lot of different options out there. The issue is actually more just about transparency of those options to consumers. You have seen a number of new entrants come into the market, more will follow where there might be something quite drastically different but I think the core issues remains the transparency, and therefore the comparability of what the different options out there are. Whereas if you compare it to certainly other markets where we have had some ability to grow, let us say car insurance and credit cards, it is much clearer what the comparison is you are making, as a consumer.

Current accounts are more complicated, certainly, our research has indicated it is about the value and the cost that customers really want to understand. It is very difficult for me to actually grasp information and have a true comparison with other products.

Q. (Mr Hoehn) This is a question of assessing and comparing which is what we cover in the Remedy 3 etc. So let us just stay, if you do not mind, on the prompting of customers and raising awareness. Now, who should actually be the source of that prompt? Would it be your own bank that prompts consumers? Should it be a regulator? Should it be another independent organisation? Could it be a rival? What is the view on that?

A. (Mr McCreadie) If you are talking about an annual statement, as an example. If you look what happens there on the credit card market, there has been an agreement reached by card issuers that once a year they will provide an annual statement. I think it should come from the bank, but there needs to be something that indicates there are alternatives out there for you to consider.

Q. (Mr Hoehn) Once a year. We have seen submissions that argue for a more frequent prompt or maybe a statement that comes from the bank. Any views on the frequency with which these prompts would be issued?

A. (Mr Warrington) Once a year is a good frequency to have a regular statement. I would agree with that point. The open-ended nature of the current account relationship is part of the problem here, so there is no sort of contractual end date by which the consumer necessarily needs to shop around at that point. I definitely support a view that at least an annual statement is important.

I did like the idea of prompting at key trigger points. Service points, if you take the RBS incident that is quite a good example. Whether RBS should have been duty bound to do something to notify its customers that there were alternatives. I do not know whether that would have made any difference to any consumers at that point, but I certainly feel that something more frequent at key inflection points when the consumer might have had a bad experience or when the bank or financial institution is doing something different perhaps could be clearer, more pointed. They are changing prices -- all banks and building societies would be duty bound to notify consumers about that but whether that sort of communication could be clearer about the alternatives.

Q. (Mr Hoehn) Failure of service is one obvious trigger but you mentioned, for example, a change in interest rate. Could that be a trigger point?

A. (Mr Lynam) The interesting question is if people do not even change their bank accounts when they cannot get their money out of their bank account because of IT failures, will receiving a letter once a year make them? Will that actually make any fundamental difference?

You can see on the TV every night, lots of different banks advertising in your face. You cannot ignore such advertising in the same way as you might ignore a written statement from your bank. Most communications to most customers from most banks get ignored. I do not think this, in isolation, is going to make any real marginal difference. I am sorry to say that but that is my view.

I would also like to understand the answer to this question, which is what exactly will be a critical measure of the success or failure of this investigation. Will it be a quantum increase in switching? Will it be a quantum increase in the number of competitors on the high street? How will we know whether this has been more successful than its predecessor? Maybe come back to that.

THE CHAIRMAN: We could come to that later, but if we just stick with -- I understand why you say that routine communications from banks get thrown away by most customers and indeed the research by the FCA that annual statements and credit cards have not had an impact. What kind of communication? You say the RBS failure did not have an impact either. What kind of communication would have an impact in your view?

A. (Mr Lynam) I do not think any communication will have an impact. Those banks that are gaining net market share are those banks that are incentivising customers to move. They are positively incentivising them. This is not going to positively incentivise people.

Q. You are saying we should forget about prompts?

A. (Mr Lynam) I am, yes. As well as another number of issues.

A. (Mr McCreadie) I still think with other things added to it, not in isolation, I think a prompt once a year could be helpful, but I do not think it is going to revolutionise the way the market operates on its own. There would need to be some clearer guidance given around cost, value, alternatives and what you should be doing in considering those, on its own, I would agree.
A. (Mr Warrington) I would agree. I would just go back to the other point I made which was I do not know whether you looked at, for example, a current account being a fixed term type of product.
Q. (Mr Hoehn) Then you would have an automatic renewal.
A. (Mr Warrington) Well then something has to happen.
Q. (Mr Hoehn) Like in car insurance for example. It is an annual insurance and it comes up for renewal. You get a letter saying ...
A. (Mr Warrington) I am not saying that -- that may or may not work but that would be a more radical step perhaps.
A. (Mr Hemsley) I think there is a frustration here in terms of if we walk through remedy by remedy, we are individually, I suspect, going to look at these remedies and say there is a huge question out there to be resolved - that this review today seems to have identified the issues but individually and in aggregate, I think the sense is that the remedies will not have an impact. If we go through the remedies one at a time, we will end up with a view that Paul has expressed that says looking at it, the remedies might be useful and might cause a few people to reconsider on an annual basis or at an IT incident, but they are not either individually or in aggregate going to fundamentally change the dynamics in the market.
Walking through them one at a time -- of course if that is what you would wish

to do, we can do that but I think you will get a somewhat repetitive response. Certainly, from our perspective, which is "useful but it will not change the marketplace".

THE CHAIRMAN: Obvious follow-up, what would change the marketplace?

A. (Mr Hemsley) We have articulated our perspective on a number of occasions but I also think to a degree is there not an onus on your perspective that says look at multiple industries, you have the expertise, the knowledge and the resources? To a degree, yes, I am very happy to go through our perspective as well, but some of that should be coming back through the review.

Q. (Mr Hoehn) What about rivals? Could rivals be more proactive? So you could try to create an awareness that you have a better offering. That it is attractive to switch. That is advertising, right?

A. (Mr Lynam) We cannot succeed in business unless we do that. So by definition if we are running businesses, as we are, we would be not doing our job if we were not trying to stimulate people to move to us. Clearly, they are moving to us on a majority of cases from the big banks because these guys have most of the customers. The question you have to ask yourself is fundamentally why is there not a level playing field in UK banking and without a level playing field; can these things, in isolation, make a difference?

Some of the recommendations, for example, a comparison site on service quality, let us just think that through in practice. As Metro Bank and ourselves said to you on 3 July, in this office, we are beholden on the large bank, who we clear through, to deliver our quality of service. By definition, we can be no better than them.

In actual fact, what happens is when they have outages, which they do quite regularly, they sort out the problems for their customers first and we end up as tail end charlies. Therefore, if you have a comparison website the big guys are always going to be better than the small guys because the small guys get the worst service from the big guys. So that just does not work, full stop.

Therefore, the only way to address that would be a radical solution whereby you have a single clearing system owned by a common utility, a bit like National Grid, where everybody gets exactly the same service and pays on a pay as you go basis. Now, that is radical. A service comparison website is not radical. I am sorry to say but it is not and it is doomed to fail.

The same goes then for a price comparison website on SMEs. The big banks have huge capital advantages and huge funding advantages. Creating a price war will only give them a huge advantage, so why would you do that? That will make competition worse not better. I could go on but I would rather not.

Q. (Mr Hoehn) You mentioned SMEs and maybe this is the moment to just look at that customer group. Is there a big difference between SME customers and BCA provision and PCA provision in terms of the ability to prompt, the need to get prompts, the need to raise awareness. Can you comment on that?

A. (Mr Lynam) We would not provide an SME current account unless we could use some of the balances that we would receive to lend more to SMEs because we did not have the same disproportionate capital burden that we have in lending to SMEs. All this comes back to the four causes of problems in this market, which is disproportionate capital requirements on smaller banks, more expensive funding, access to payments infrastructure and proportion of regulation. All of that is then further compounded by the tax surcharge for the smaller banks.

THE CHAIRMAN: We are going to come to capital funding issues and indeed the banks' tax surcharge later on in the agenda. As far as payment systems are concerned, as we discussed in our provisional findings report, we currently take the view that these issues are very important. They are very important issues for competition retail banking, but they are at the centre of the remit of the Payment Systems Regulator. It did not seem to us to make sense for us to be replicating the work of the Payment Systems Regulator when it has just started work and is looking at those issues. So, if you want to put arguments about having a completely different kind of system that is not owned by the banks, but is run as a utility, that is on the agenda of the PSR and it should be addressed to the PSR.

A. (Mr Hemsley) That is at one level where it should be addressed in terms of an outcome. But the research and the findings - I would have thought that you have aggregated them over the period of this review, would have led you to be more conclusive and directional to the PSR in terms of the review that they are undertaking.

Q. I am happy to respond to that but the question. I think the competition questions in relation to the payment systems are perfectly clear. It does not need a lot of research from us, or indeed from the PSR, to say that when the payment system is owned by a subset of large banks, there are questions that whether this is fair for small banks. The interesting questions are the cost of changing that system.

So moving to a completely different payment system would be a complete change in the plumbing of the whole payment system with the possibility of account number portability as a by-product and all of that. The questions about that require a huge research programme which the PSR has the possibility of undertaking. It would not have been sensible for us to devote a lot of resources to the questions of the cost of changing the payment system when another payment agency is doing exactly -- when that is their agenda.

A. (Mr Lynam) You are trying to do the best of a bad job.

Q. Paul, I am afraid I think that is an unfair comment. No, we are not doing the best of a bad job. We are saying there are two -- we are a public agency, a regulator. Participants in markets do not like having multiple sources of regulation. It is not a sensible use of public funds for two public agencies to tackle very big and complex questions.

The future of the payment system is a big and complex question, which is in the remit of the Payment Systems Regulator, and I have no apologies at all about us not taking it on. I think had we taken it on, we would have been subject to absolutely fair criticism of not making best use of public funds and having two regulatory systems running in parallel. So it is not making the best of a bad job, it is doing our job properly.

A. (Mr Hemsley) That was not the point I was trying to make.

Q. I am responding to what Paul said.

A. (Mr Hemsley) The point I was trying to make is in terms of the wealth of information that has been collected on payment systems and, for example, what Paul would raise in terms of some of the service capability that we cannot provide because of that dependency. Is that aggregated and concluded on in an appropriate way to feed into the PSR review?

Q. (Ms Benison) I will respond to that question. That is very much what has been done. We collected information from the participants in the market at the beginning of the inquiry, to inform us on a variety of issues that we were looking at. Those included access to payments systems and that information then led us to articulate competition issues that we then discussed with the PSR and we made sure that they are covering exactly those issues.

What the inquiry team and the members did was to not just assume that they are doing it but throughout the investigation we had hearings with them and we made sure that they are. In other words, the competition issues that we identified are certainly, to the best of our knowledge, going to be addressed by the PSR.

The question was then, who is addressing these questions and there was, as Alasdair mentioned, a choice of two regulators doing exactly the same thing at the same time or letting the regulator, who was established for the purpose of addressing those issues, do their job.

A. (Mr Lynam) I have not had any engagement with PSR. I cannot say that based on my engagement with PSR, they are picking up these issues, so that is why I make the comments that I made. If we have a very clear direction that these are issues that you would like to see -- specific issues as opposed to general ones.

THE CHAIRMAN: The PSR is conducting consultations on the payment system.

A. (Mr Lynam) They might be. They have not spoken to me.

Q. (Ms Benison) They are inviting everybody, who has issues, to raise them -- to make those points.

A. (Mr McCreadie) Since we are going to move on in this, I am sure, but I guess going back to your point about prompt and other service or whatever, I guess in isolation there seems to be quite a common view that it is not going to do much. I guess it will only have breakthrough at some point. In our opinion, it is being much clearer about the value and the cost to consumer of the product they have and the alternatives that are out there for them.

I think that needs to be where we focus on transparency and comparability.

Q. (Mr Hoehn) Simple message that is easily understood and if you want to make a comparison there should be a click, a simple click to go somewhere, where you will get information. What is the simplest way of doing that? Is there a little prompt? Is it an email?

A. (Mr McCreadie) I guess you are talking about prompts again. I am trying to say I do not think the prompts in itself -- it needs to be accompanied by what information.

Q. (Mr Hoehn) So what is the information?

A. (Mr McCreadie) We have put forward what we think is an idea, which we have taken from food retailing around a traffic light system of labelling. Having the two things that customers have told us in research are most important. Credit interests. Do I gain by having money sitting with you? Also, what is the cost in overdraft charges? The reality is that some of the banks that Paul is referring to, in terms of winning share, not only do they have scale benefits of large existing customer bases for a long period of time, they also actually are generally at the worst end in back end fees that are not that transparent, funding some of the upfront incentives.

We need to just be very clear how we break out, for consumers, the two. What you get for having money sitting with the bank, but what the charges are to you when you actually borrow from the bank. I am convinced that there is a need for much clearer transparency. The example of food labelling would be that not only do customers to become more informed and make more informed choices. It does not mean they always decide to change, but they are informed and can make a better -- based on facts, better information.

It has also driven food manufacturers to change the content and ingredient -- and I suspect in financial services that could be the cost to the consumer of some of those elements to end overdraft charging. Something that reflects the value and cost to really bring it in a transparent simple way for consumers to understand, seems to be an idea. If you are prompting you would have to give -- or any advertising on current accounts, you would have to actually have that labelling there. The great headline needs to be balanced with what other features of the account and you could do that in an annual statement or other methodology as well.

A. (Ms Cattanach) It is important that that would be a comparator, so it is not just a statement of these are the costs but actually how does that compare to others. You may think that looks simple and not that expensive, but actually, that is one of the worst in the market. It is making sure that that is clear to customers.

A. (Mr McCreadie) There needs to be an independent governing body.

Q. (Mr Hoehn) Then the question is who. Who would be best placed to do that?

A. (Mr McCreadie) There needs to be some regulatory independent body.

Q. (Ms Benison) One point I just also wanted to make and that is partly related to your comment, Richard, that the remedies in aggregation would not make a difference. I would like to explore that a little bit more because one of the premise of our Remedies Notice – and we hopefully made that explicit - is that we do not believe that those remedies should be implemented in isolation. We very much believe that it has to be a package. To your point that each remedy individually may not work but actually if implemented in a smart and effective way, providing a sort of an easy way for customers to be prompted to actually start looking. It may be not make a huge difference but we believe that it would.

One question in general to supplement Tom's inquiries. How those prompts would work together with other remedies that we are proposing? What would have to be included in any messages around the prompts for this to be a more effective remedy?

A. (<u>Ms Cattanach</u>) I think the prompt is just prompting the customer to then do something. You know customers do not do anything, so that is where the break and the failure is in the Remedy, because you are assuming that all the remedies will aggregate, but the break in the chain is if you ask customers to do something, they will not do something. Because that is what we know from your own research that the nature of current accounts is that people will not do things. How can we change the market assuming a majority of customers will not switch. How can we actually change the market for the customers staying with their own providers?

Q. (<u>Mr Hoehn</u>) Instead of creating a role for us to promote awareness of service, quality, costs.

A. (<u>Mr Warrington</u>) I think there is. I differ slightly. If I took the whole package of initiatives I do actually think, executed well, that package could deliver some increase in the levels of switching. What I do not know and this is the sort of conversation we are going to have with the providers that are in this room. What I do not know is what level of switching, and this has been mentioned before, is the right level. It is down to consumer segments ultimately and some are going to benefit from switching more than others. Therefore, there is a portion of the market that ought to be switching and a portion, which, actually, it is a fraction of the cost and it does not really mean anything to them. It is not clear whether we are shooting for 5 per cent, 10 per cent, 30 per cent in the current account market and therefore whether I am being asked to think whether these remedies would increase us from 2 or 3 per cent today to 30 or 2 or 3 to 5. That is the first point.

The second one, for me, is if I was an incumbent bank in this market, I would think that this would promote more free flow between those sorts of organisations for some of the reasons already said; switching incentives. It will provide more flow between those organisations. What it does not necessarily do is make it easier for a new entrant or a small player to increase scale substantially and that is why we are having conversations around -- and I have the same list of things here. Payments systems, surcharge, funding and capital advantages, those are the things which stop the UK's second largest building society, which has 300 or so branches, being a substantive player in the current account space.

A. (Mr Hemsley) I would not disagree with those points and the one I would add to it is that a number of the remedies are built around engaging consumers in this decision-making, and that is going to be a critical element. Supporting that there has to be a mechanism for transparency and clarity, which – to the point raised to the right – covers both the opportunity value missed, and the cost of overdrafts and those hidden charges.

As your evidence concluded, most consumers are paying more than they need to be paying. The complexity today - even through the remedies the complexity of the consumer first of all engaging with, and then understanding that cost to them, is not broken by what we have on the table. And hence I think we will still end up with the same level of competition amongst the same players in a future market place.

A. (Mr Emuss) Just a further point, in terms of if you are looking at success, not just measuring it by percentage of switching -- to Richard's point about the demographic switching. It is going to be the more financially literate that are going to be incentivised to switch.

A. (Mr Lynam) If you look at what might make a difference -- humans, generally speaking, are lazy and therefore how do you make it as easy as possible for them to do something that might benefit them. We all know we can benefit from more exercise but most of us probably do not do enough exercise. An interesting question would be if on the landing page of an individual's current account, online or on tablets, there was a regular button that posed the question of how much is this bank account costing me and they pressed that button and a number came up. That might be quite an interesting question in terms of would that be something that would prompt them on a continual basis.

Now, ignoring that the big banks will say that is technically impossible, blah, blah, but when we make most of our buying decisions, we do so in a cognisant conscious state that we know exactly how much it is costing. Whether it is cost of the bus fare, the cost of our mortgages, the cost of our groceries. So something that tells people, particularly in a rising base rate scenario, where they will be paying more than is currently the case, might be worthy of further consideration by ourselves. I think that might have more of an impact than some of these paper driven or electronic awareness measures, just as an idea.

Q. (Ms Benison) That is a nice segway to the next topic.

THE CHAIRMAN: Before we leave prompts can I ask about an aspect of prompts that I think we have not discussed and that might link in with a traffic light system or some other system. The idea of sending prompts not when the bank has suffered a failure, for example, but sending prompts when something has happened to the individual bank customer like they have received a charge for an unarranged overdraft. Would that be a suitable time to send them the prompt that says, "You have just been charged £100 in overdraft charges and did you know that your current provider has a red light for overdraft charges".

A. (Mr McCreadie) I think anything that can help understand. The only thing I would say on there that some of these triggers, these sorts of events might only affect certain groups of customers. We just have to be very clear on what the expected benefit would be of actually implementing them, in terms of costs. Certainly in terms of being more transparent and at the time you may be quite heated and emotional about the fact you have had a large level of charging, would seem like an appropriate point. You might want to think about what the options are, but we just need to make sure it is very clear. It cannot be any level of overdraft charge; it cannot be any level of overdraft interest. There would need to be some regulated level where that would actually kick in.

In terms of supporting, giving more transparency to the two costs then anything like that would be helpful.

Q. (Mr Hoehn) It is based very much on costs, that is your focus, costs and reward. It is monitoring. Can you capture that in a traffic light system?

A. (Mr McCreadie) I think that is very difficult and might mean different things to different people what is good or bad service. Again, you would probably debate for years what would fit in what category. I think there is maybe one or two events such as an overdraft charge at a particular level or an IT failure when you have an IT failure at a particular period of time. That might be easier to regulate, but I keep focusing on costs because it is the one thing because people do not understand the costs and the alternatives.

A. (Mr Warrington) The focus on costs naturally gets us down to a subset of the market and, again, there is a lot of complexities with overdrafts in that while maybe I can prompt you that you have incurred a lot of charges but will somebody else accept your £2,500 overdraft. So, it may not even be possible and that gets us probably into a different debate altogether, but that is an important one for that group of customers, I think. That group of customers are exposed to very high charging and I do not believe it is very easy for them to switch.

A. (Mr McCreadie) Those are not perhaps the value decision in an interesting environment, which is why we put foregone interest onto our monthly statements.

Q. (Mr Smith) I think that does come over. It is interesting because we are at the front end of a whole collection of things and I think, as Paul says, you could say that they were worth more effectively if other things also happen, which the Payment System Regulator, would be looking at.

If we continue that cycle and say, "Well, if you prompt at certain times or once a year or when a student stops being a student or when somebody has a bad experience", you then do naturally move into how do you access and assess alternatives. We then move into some of the things that you might look to, and one of them is to know the cost of your current service, and that could be done through a button or through a requirement to demonstrate what the cost is. Then trying to assess the alternatives through, as we are suggesting, developments in Midata, as to whether you are assessing the cost of alternatives is one thing we put forward. It would be interesting to have your views on whether the further development of Midata, as a part of a solution of comparison, has merit.

A. (Mr Hemsley) One of us in the office actually tried to use Midata. It is very difficult and complex. Again, if we think about the cross-subsidisation that is taking place in the free-if-in-credit marketplace, the people that are probably incurring the disproportionate fees, that are subsidising the general populous that is having free-if- in-credit banking," are those people that will find something like Midata the most difficult thing to use. I think from our perspective, it would be, like the earlier comment -- I am sure that it would be a positive step forward. Again, I do not think it would be material but there is a significant amount of simplification on the ease of use that would need to happen for it to have any chance of being appealing and engaging to the population that would get the most value from it.

A. (Mr Warrington) I agree with that.

Q. (Mr Smith) It can be clunky at the moment.
A. (Mr Warrington) Yes, it is awful.
Q. (Mr Smith) Sometimes things to do start clunky. It does not mean to say you completely throw them out but you then go through what does it mean to make this less clunky. What you do to make it more accessible to those that you say might be -- I will not say digitally dispossessed because quite frankly that is an interesting phrase, but you find that in reality it is less than you think it is.
A. (Mr Warrington) I think that would help. A better Midata would help but again, for me, we are talking about small sub-sets so it is overdraft users. They would benefit from switching. Midata would help them, if it was easier, better, but that will not change the numbers dramatically and they might not be able to switch anyway. The other group of people it might help is if I had a massive balance in my account, but that, again, is a small population. So you are left with the lion share of the market which are not influenced by price, which brings us back to the differences in service. There are actually some big differences in service.
Q. (Mr Smith) I do not want to cut across but if you start to look at a range of solutions and if you at took large credit customers, large overdraft users and you say, "Does Midata do something for that", if simplified, if made easier, then is that a positive or do you just say any disaggregation and any attempt to price comparison and assess will not work. I do not think that is what you are saying.
A. (Mr Warrington) I do not accept that it did. I am just making that point that it is --

Q. (Mr Smith) So then you look at what is left, which is a potentially large proportion and then you go this might not impact on those, so what do you do next. I think we also say are there some service quality attributes that we need to start looking at and how do we look at those. I would be very interested in your thoughts around whether the service quality attribute should also come into play and how you would display those, how you would assess them, how you would communicate them and how people would then make decisions as a result. I would be very interested.

A. (Ms Williams-Gardener) When you look at data, and I come at this more from a technology perspective than I do from a financial perspective, but when you look at all of the data that you can collect on your customers, we believe, there is no reason why you cannot help those people to manage their money better and therefore be a little bit more proactive about preventing an overdraft scenario.

I agree with lots of things that are being said. Make it easier for people whether it is traffic lighting or not but make these things really easy for people to understand. One of the things that we will be looking at is proactively working with our clients to prevent them from going into an overdraft scenario, so you could, all based on the information you have, help them manage their money more efficiently. One of the remedies that you talk about is this ease of understanding whether the overdraft facilities they were seeking would be available to them from another provider, we whole-heartedly accept that. We would love to and will look to work with people to say if they are going to be in an overdraft scenario, this is what it will cost you unless you take some different actions to prevent that.

The Midata information helps but I think we are generally, as a financial institutions and someone who has had a bank account -- we are not helping people manage that information well enough and I think there is an awful lot that can be done from that perspective.

A. (Mr Hemsley) It is a point I would have made at the end of the session, but a number of these remedies are made more complex – and it is difficult to believe that they will be successful - because they are still within the context of free-if-in-credit banking. The very notion of free-if-in-credit banking, and the subsidies and the social issues that that perpetuates, makes things like a price comparison site more complex for people to use. If you do not address the issue of free-if-in-credit, it makes these things harder.

A. (Mr Lynam) It is a question about equality. If I go back to that if I am at the end of the food chain by the clearing banks, my service quality is always going to be worse than they provide to their own customers. Why would we want to flag that, I am not entirely sure.

Q. (Mr Smith) I accept that the point you make that your service quality score is not entirely in your control. In which case, why do you do anything around quality?

A. (Mr Lynam) If I can give you a real life example, last week we submitted a BACS file to our clearing bank. We found out 48 hours later that they had failed to process that BACS payment so the submission was in our control but not the processing. On that day, I then had to have four staff manually key thousands of faster payments for which my clearing bank charged me 40p for each payment which only arose because of their service failure.

Q. (Mr Smith) That is fine, but I look around the room and you have some great brand names here who I think actually would say service quality does go beyond the technology flow.

A. (<u>Ms Cattanach</u>) What do you mean by service?

Q. (<u>Mr Smith</u>) What do you mean by service?

A. (<u>Ms Cattanach</u>) Is any measurement of service quality going to look at different kinds of business models and different engagement with customers and still compare them and say that they are equal because if you have a digitally oriented service model, it is not going to feel the same as a branch orientated service model and I would not want the service quality score to be low on engagement with staff, because actually if customers are engaging with staff it is usually because something has gone wrong.

In a branch based service model, you would say that is a great thing that customers are engaging with our staff and it is very difficult to work out how you would measure service without prejudicing some business models over others. I mean, if we are saying service quality, well you can go in the App Store and tell which Apps are better rated than others. Is that a key measure of service quality? It is already available.

Q. (<u>Ms Benison</u>) That's what we are looking at, so what would be those indicators and I am appreciating the fact that they may not be the same across all the different participants.

A. (<u>Ms Cattanach</u>) It depends what kind of customer you are. It is difficult to choose one service quality measure.

Q. (<u>Mr Smith</u>) Is it not therefore for you to determine the business model that you think is best for the target market.

A. (<u>Ms Cattanach</u>) The service quality measure may actually skew the results.

A. (Mr Warrington) For me, we are hitting on why there is a lot of inertia, which is -- it is incredibly complicated when you get out of the realm of just price. You get into, you know, do they have branches. Is there a branch near me? Do I like the digital offering? Is there a mobile app? Does it have the same things as my account history? You know there are all sorts of things where people just go ...

Q. (Mr Smith) I will stay where I am.

A. (Mr Warrington) Yes, so all of that information is difficult to obtain, despite consumers potentially benefitting from it.

A. (Ms Cattanach) It is quite similar to cost of information today that consumers find -- there is too much choice. It is in too many different combinations, therefore it is too hard to prepare so that is what drives some of the lack of engagement. If you want to create complexity again on the service that may also create the same disengagement.

Q. (Mr Hoehn) We looked at two measures in our report, one is satisfaction ratings and then net promotor scores. So what do you think of net promoter scores, is that a good way of ranking suppliers?

A. (Mr McCreadie) There is about 500 different definitions of what a net promoter score is. It is very difficult to get a simple understanding, even within an organisation, never mind across an industry, on how you measure it. Again, these things are very difficult to -- a common thread.

Q. (Mr Smith) Let us go the other way then and talk about if you think service quality is an important component of supporting information for the middle ground bank account holder to assess whether he or she is happy, what type of information should be provided that is not so much that people give up?

What are the top four or five things that you would point to and is there any consistency across the marketplace on those? Is it transaction security? Information security? Not having down times or is it something like the digital offering for the younger generation?

A. (<u>Mr McCreadie</u>) I think these things become a hiding factor -- nobody around this table is going to sit there and say and we are quite happy competing just on price and accept my service is going to be poor. Customers will not accept it. I think all of us would have an aspiration to keep improving how we service customers. There might be some experiential occasions when there is a failure and we do not do what we said to customers what we would do and that will be common across the industry. I suspect when there has been a breakdown in service, I do not think anyone scans the market and think other than one, there is no evidence that they are growing. I think people then look and say, "What is the cost? What is the service? Is it is a branch or not if that is important to me? ". It is the things that we are trying to get to the root cause of transparency, again.

It might be an emotional reason for pushing you away from your existing provider, I do not know there is enough evidence that you could get to a common measurement that would then attract. Nobody is going to sit there and accept they are going to be offering worst service than a competitor. Now, it might happen from time to time, I accept that but it is not what you are setting out to achieve.

A. (<u>Mr Lynam</u>) David hit the nail on the head earlier on which is by and large most of the time, most of the clearing banks do a pretty good job and the consumer perceives that they are not paying for that, therefore when there is an occasional blip, "I have not paid for it, so I will live with it". That is the reality of the situation.

The way to overcome that inertia is to look at those banks that are actually gaining net switches, and they are ones who are positively incentivising things as opposed to negatively incentivising based on service failures or whatever because most people would just say, "I am not paying for it, so I have to expect this from time-to-time", that is just human nature.

Q. (Mr Smith) Your views would be that it is largely about price.

A. (Mr Lynam) Price is a huge -- depends what you can qualify as price. Does that include the financial incentives to move in the first place or is it the ongoing transaction or is it the opportunity cost. It is quite a broad question.

A. (Mr McCreadie) If you look at the public data on switching and switching is only a minority of the market. If you look at the evidence from the switching stats, nobody is net gaining unless there is some form of better offer for the customers. Whether it is an upfront incentive, credit interest, whatever. Nobody is gaining.

Those who are not and generally the big leaders are losing because of the apathy and there is no transparency about actually what those customers they are retaining today are paying or losing out on.

THE CHAIRMAN: Can I pursue that thought that what the customers think they do not pay makes them unresponsive. We now have a significant fraction of current account customers who do pay. Who have signed up to accounts with monthly charges and interest payments and current account balances. Do we have any evidence that they are more sensitive? Maybe you are not the right group of people to ask this, but do we have any sense that those customers are more sensitive to quality issues?

A. (<u>Mr Lynam</u>) I do not know if you are specifically referring to the Santander 123.

Q. That is only one of many that are in the market.

A. (<u>Mr Lynam</u>) They have been very successful at it. There are a lot of competitors like this, so fair play to them but generally speaking the monthly fee that the customer pays is offset by the benefits that they get. Therefore, so net they gain. So it is not quite the same as paying for an account with Natwest, for example, where you do not get the same amount of 123 benefits as you would do with a Santander.

A. (<u>Mr McCreadie</u>) If you look at that particular example that Paul refers to, if you look at the public information that that bank is putting out there in terms of investor reports etc, through the period of success of the growth in that account, have done to their mortgage price increases in customers and their deposit price decreases in customers. You can look at it isolated and say, "Looks like a great success", but other people are paying and it is the existing customers who have apathy who are paying and they are putting the investment into the front offer to attract new business. Squeezing out competitors who do have that to compete with.

A. (<u>Ms Cattanach</u>) Squeeze out competitors and increasing their dominance in other markets.

A. (<u>Mr McCreadie</u>) They are deliberately managing their deposit pricing and improve their margin, despite that offer. We have certainly done a lot of detailed analysis on their mortgage P&L and the changes they have made there, and that has significantly allowed them to fund a front big offer.

I guess we are talking about PCA, but how you compete is quite difficult as a small provider when you do not have scale in other products.

Q. (Mr Smith) The multi-product holding issue is there.

A. (Ms Cattanach) Yes, it is obviously holding, the market share and the business model, impact on just the current account market.

A. (Mr Warrington) The one point I would add on paying for accounts is -- I mean you are right. There are packaged accounts as well, but we have seen a number of providers entrench their position in packaged accounts and a number of providers remove themselves from packaged accounts because it has become a very difficult area to sell into for regulatory reasons.

As a new provider, for the same reasons, I would not try launching a packaged account into the market even though actually it probably is quite a good area to compete in.

Q. (Mr Smith) Just going back to -- in the event that we think there is some merit for some segments of the market in having price comparison, which I do not think you have said ... is there a big issue around confidentiality of data that is accessible or are all those issues solvable? There is some momentum around the digital world not being as secure as the physical world and all those sorts of things. I think we would be interested in your views on the customer perception of security as well as ...

A. (Mr Hemsley) It is more perception than anything.

Q. (Mr Smith) It is indicative yes. We have this, do we not, in health. Access to health records and the way in which health -- does the same apply to transaction data in terms of perception of security? What might be done?

You cannot commute like we will never continue with this digital force that is upon us. It is not going to happen is it, the reality is we are going to continue to march down a digital world, so what do you do to alter customer perception and reality?

A. (Ms Williams-Gardener) Changing perception is a very difficult one. Generally, people are really worried when they give up their data but there is an awful lot of work that is being done and everyone round this table will be aware of PSD2, regulation changes that are coming. Under this new regulation Banks are going to have to open up this data and there is a large amount of work being done by the open bank working group, currently, to ensure that there is an open approach to it -- we are a couple of years away, I admit that, but the OBWG are considering that it is done in a secure and open way and that there is a governance model for it.

As people start to see the benefit of amalgamating more of that information for their own use not thinking it is going off to somebody else to cross-sell to them and it is kept in a secure way, then I think there will be this build up -- but trust is going to be very difficult to get from the consumer perspective, especially when you see all of these incidents in the press. TalkTalk was the latest one where all of the customer data had been compromised. It is very, very difficult to give your customers that reassurance, but it is part of the service that you have to give. Open data and more data is coming so I think it is a matter of we need to know how we are going to deal with it rather than saying we are not going to deal with it.

Q. (Mr Smith) As a general view -- we are on that march. How would we work to change customer perception? Is it down to you as providers to change that customer perception? Is there a regulatory lens? What are the combination of things that you would be keen to see in four or five years' time when this just becomes part of life, people are more comfortable.

A. (Mr Hemsley) Experience to date is that the reassurances you can give to customers and consumers only has a positive impact if they progressively use and learn. You can pump out lots of material about security but customers generally only believe that when they have learning with it and experience with it. So I am not sure there is an instant solution to that question other than a progressive development point.

The piece that clearly I think we all know is that one bad experience can undo a phenomenal amount of good work in that particular space.

Q. (Mr Smith) I suspect, as a follow-on, is there a point about they need to see the benefit from doing it. As opposed to just the provision of it, without a benefit, does not do that much for them.

A. (Ms Williams-Gardener) It is the benefit, the convenience and then the trust gets built over time. It is a very slow thing to actually get but it does get built over time and it gets built over recommendations and with the best will in the world, with all the marketing money people can throw at it, you cannot force trust. It is something that is built up by customers over time, so it is a slow thing to get. It does not help when you have stories in the Daily Mail headlines that go against a lot of good work that I daresay people round this table do and lots of other businesses do.

Q. (Mr Smith) The point that Paul made that you are dependent on others for your security as well as your quality.

A. (Ms Williams-Gardener) Quality of service I completely agree with you. You are absolutely down the pecking order when it comes to being dealt with from

those perspectives, but security of data is paramount. It is not just security in the financial market with data and personal information. As we have seen in the telecoms and in other industries as well, it is across industries, so unfortunately it is not just a bad incident in your industry that backfires, it is a poor experience in others.
Q. (Mr Smith) An effect across the whole of personal data.
A. (Ms Williams-Gardener) Absolutely, yes.
Q. (Mr Hoehn) I have to compare the situation with Germany planners and the sharing of transport data is very different from what we are looking at, but that has been very interesting how the government here decided to open up data of its services to app development, as we then start to develop new tools, because the consumer will start to see the benefits. The benefit of sharing, developing trust also has to be seen. It has to be seen in a service we cannot, for the moment, imagine. So managing your own money better -- and if you want to have an app that does that you need to have access to data.
A. (Ms Williams-Gardener) Just building on that fact, Shell, this week, launched their mobile payment app. So you can drive up to Shell and you can pay on your phone with very little interaction and that can only get better. There are sensors being deployed around the globe on a faster basis than I think we are generating data and obviously we are generating data on a very, very prolific basis, on a regular basis.
You link something like the Shell app to automatic number plate recognition and you use with PSD2 and the open API and OAUTH, you authorise a payment to be taken. You do not leave your car. That is great if it is a rainy windy day you wouldn't need to leave your car.

Q. (Mr Smith) You have to fill the tank up.
A. (Ms Williams-Gardener) Shell actually has staff doing that. It goes further, it is this integration of the Internet of things, improving the whole experience for customers, which is going much further forward and obviously that is just one example about paying for your fuel, but you are absolutely right with the transport system. Just tap and go on the tube is great, the congestion charge that you can pay automatically by recognising your number plate. All of these things will come together -- whether it is the payment systems regulator, more to the point, as opposed to yourselves, but, it all comes into providing an experience that is different, that people want to use and that they can build up trust with it. Comes back to the point and the benefits, yes.
Q. (Mr Hoehn) The reason I mentioned this example of journey planners is because it took an act of a governmental body to open up data and make that step. What we are looking at here is also a possible measure where we say via Midata or something -- is there something one could do in order to force everything, enable this innovation to take place, these business model innovations to service innovations.
A. (Ms Williams-Gardener) I think PSD2 is it. An open API and that is well in train and I am sure everybody round this table knows how they want to address that.
THE CHAIRMAN: When you said that is two years away before it is done, does that mean that having a really effective Midata tool is two years away? Do you think Midata could be improved on a shorter time period than?
A. (Ms Williams-Gardener) I am sure it could. As we said it is clunky but things start often in a clunky way and they can, with the right focus -- takes time and

resources, these things can all be improved if the intent is there.

A. (Mr McCreadie) Again, but on its own the reality is once you are engaged, the key thing you get more consumers engaged.

A. (Ms Cattanach) To your point about data sharing, consumers are only comfortable with it if they see a benefit. A disengaged consumer does not see a benefit to their data being shared between banks to market to them products that they are not engaged with in any event. So they will be uncomfortable with that kind of data sharing because they are not seeing that benefit.

A. (Ms Williams-Gardener) That is where the data sharing for their own advantage, whether it is because their car is linked to something that links to their payment system, "That makes my life easier".

A. (Ms Cattanach) That works because it is tailored and it helps.

Q. (Mr Hoehn) It is a virtual circle that you need to start.

Q. (Mr Smith) It is interesting because the point Ant made is one that segments of the market would really benefit financially and then he also made the point that service quality benefits are quite amorphous, quite difficult to measure and quite broad. So, you are sort of going back to the financial benefits and therefore your segmentation and what do you do about this middle space.

A. (Mr McCreadie) Another thing we should be aware of -- I guess there is a risk that PSD2 could even reduce the need for you ever to move your bank account. It is about payments not about core banking, funding, so there will be new business opportunities and having great consumer benefit. It may actually make the need to change bank account even less beneficial to you.

A. (Ms Cattanach) You change payment service provider which overlays your current account --

A. (Mr McCreadie) You do not have to change your bank.

A. (Ms Cattanach) You never use your bank.

A. (Ms Williams-Gardener) Exactly, the use of the banks potentially could be real back-end plumbing and all the front-end could be taken by somebody else.

Q. (Mr Smith) I think around access we have got the point. I think the point you have made about segmentation, looking at financial benefit and the difficulty of service quality has been helpful and I do think, Paul, the point about dependency is one that is a recurrent theme, and has been over the months that we have been doing this that there is only so much that you can do on your own and say, "There is some stuff I could do on service quality regardless of the payment system".

A. (Mr Lynam) That is a given.

THE CHAIRMAN: To pick up what was said a minute ago about people need to -- it is not enough just to have a good comparison service, people need to want to use it and that is where as Joanna said earlier, we see a very strong link between different elements in the remedies package that we have put up for discussion.

Particularly, links between prompts and comparisons, so something happens where you get a prompt and ideally the button on your mobile phone app is a button that says send me to Midata so I can see if another bank will do a better job. So that we ideally want to end up in a system where the prompts were linked to the next step that the customer might want to take.

A. (Mr Lynam) Interestingly enough, the data that we have, we have customers who check out their balances dozens of times a day, it is quite bizarre. It is literally quite bizarre.

Certainly I check on my various apps on my different banks several times, sorry, once a day for each of the banks but that is probably around security as much as it is anything else. If you have something there that is much, much simpler than Midata, which basically says the implicit cost of your bank account is blah. That would be much more - to my personal view - impactful than a lot of these little things in isolation.

Q. Just to emphasise, our minds are open. We have put quite a lot of emphasis on Midata in the Remedies Notice but if a traffic light based comparison tool would actually work better for many people, in some sense, and this is not to put it down at all, it is necessarily a cruder tool than something like Midata that does a very sophisticated comparison. But if it works better, it works better.

A. (Ms Cattanach) Involves less of an effort on the consumer's part.

Q. (Ms Benison) Or maybe it is a stepping-stone.

A. (Ms Williams-Gardner) You take the complexity of Midata but transcribe it to the consumer in an easy way, which might be a traffic lighting system.

THE CHAIRMAN: Getting information about foregone interest is a different kind of information but again if it will work --

A. (Ms Cattanach) That could be part of your tracker. You do not have to present it in monetary terms because we know that turns off some consumers.

Q. (Ms Benison) Another really important point and may be another button on whatever comparison tool we have, is to actually do something about it. That is another example where we really strongly believe that it has to be so. That call for action needs to be there and needs to be done in a very straightforward and simple way. CASS has been introduced already but as our findings demonstrate, it is not working as well as it could and Philip if you can explore other questions around that.

Q. (Mr Marsden) We have probably cantered through to slide 13 now, which is actually having convinced them to perhaps act and any kind of things that may go from that move or cast a shadow over that, so that is how you see various options.

I want to compare in a way the relative merits of account number portability with some of these options on this slide, so there is a longer period of redirection. Could we get the banks to all agree about partial switching with a CASS guarantee or not? How much can you guarantee that people would be able to obtain their past transaction data?

The first one, we probably want to hear your views and I know that Richard is going to start us off on ANP, but in the context of trying to weigh up the relative merits of these various options as opposed to anything on its own.

A. (Mr Hemsley) I am clearly going to come from the perspective of still supporting ANP, and believing that it is a better fit-for–purpose, longer-term solution, but I want to wrap some words around that.

For me, it is not literally about forcing every organisation to be able to accommodate any account number and transport that around those organisations. I think we appreciate that that has a potential significant cost for the industry but we believe strongly that, over a period of time, the core account administration and payments capability should become a utility, and that we want to drive innovation and value at the front-end, if you like, in terms of the consumer experience.

As we have seen from what Cruickshank drove from a telecoms point of view, and as we have seen with the faster payments infrastructure, where we can all get access to it, creating that utility at a UK level has driven significant value in terms of consumer experiences. Therefore we believe strategically, taking that step now to say, "Let us start small but create that infrastructure centrally that allows for the customer to port their account number with them through their career", will not only over the long-term be of value to the financial services industry, it opens up a doorway to allow a customer experience differential which we believe then will lead to the engagement - which will be account switching and people moving their relationships around organisations.

Again, I would come back to the point that says what you recommend from a CASS point of view will have some added value. We believe it is marginal added value in the short-term, but in the longer-term we would still stand behind what has become termed account number portability, in that shared context.

Q. (Mr Marsden) Agreement on feasibility and starting small and growing?

A. (Mr McCreadie) I will just go back first to CASS and I think CASS is fantastic, so I am interested in your comment that it is not working. I am assuming what you mean is there is not enough engagement in it, because if you have actually gone through that experience it does work and it works very well. They key thing is how do we get more people engaged in it. That is one point.

Q. (Mr Smith) Do you think it works for all segments of the market?

A. (Mr McCreadie) There is a seven-day guarantee in the market, regardless of what your segment is in the market. Like partial might be something to discuss and expand on, but it is not differentiating based on who you are as a customer.

Q. (Mr Smith) Habitual overdraft users?

A. (Mr McCreadie) That is something, I think, we are going to come onto. That is something we would like to see an expansion of. So I think some of the incremental points on CASS expansion that I have mentioned, fine. There does seem to be a very emotive piece around overdraft, we will probably come on to it.

Just for the record, but we are not in favour of account number portability. We just do not see it as solving the root cause of the issues around transparency, comparability. Customers are not asking us for it, so it is not seen as a package of measures. Some elements of the principle, which was described, could be helpful but it does not seem to address the core issue for us.

A. (Ms Williams-Gardener) I have to say I think that back to Richard's point it is sort of start small. I think it is the way that this industry needs to go. I know it is a huge change for the industry but I think it is. It is the only way that we saw people moving mobile phone providers was when they could easily take their number with them. That comes back to consumer perception.

I agree, CASS is a fantastic service, you use the service, you go through it, it is seamless but not enough people want to use it or know it is there or whether the actual switching benefits are enough for them but then it comes down to customer perception. The perception that I have of portable account number, makes me think it is easier to move in the way that it worked with mobile phones moving the numbers around. It is a big change, I get that, we would be in favour of it but it is something that would have to start small and build up.

A. (Mr Lynam) We provide current accounts and as a mechanism for moving accounts from one bank to another it does what it says on the tin, no question. The bigger question is would account number portability -- is it just a more modern initiative beyond what is really required. One of the reasons why people actually change their mobile phone is not because they can keep the number, that is just a factor, they are getting a better service for cheaper from somebody else who happens to be a more vigorous competitor than perhaps their incumbents provide. I do not think the fact that they can move and keep the number actually makes the full mental decision. The decision is made based on other factors beyond the ability to move.

A. (Ms Williams-Gardener) It just gives them that ability to say if someone else is offering something better I know that it is easy to go there and therefore I would say that would be the same within finance.

A. (Mr Lynam) It probably removes a barrier, but I do not think this is actually -- I do not think it is the key decision factor. I am open minded about account number portability. In the context of would this be potentially a beneficial by-product of having a national grid type payments structure and then does that give rise to the competitive opportunities possibly. As I said, when I met with the OFT and they were looking at CASS first time around, in the absence of lots of new current account providers, account number portability is not really going to drive up switching levels beyond that which a reinvigorated marketing campaign would.

A. (Mr Warrington) Just to complete the feedback on CASS. We support account number portability but just in using your framework of access, assess and act. We think there are more problems in access and assess, which we have been talking about than act. CASS definitely allows the fulfilment of it. I do think it does knock down a barrier potentially in terms of the immediacy of it or it has happened straight away and I think consumers are still concerned that during the seven-day switch period, even though nothing can go wrong, something can go wrong in their minds. So the immediacy of it, I think just helps reinforce the positivity that I would focus on that later.

Q. (Mr Marsden) Maybe sticking with a theme of perception that CASS works but people perceive that transactions will be dropped. So, it leads us nicely into these other two or three areas we have been looking at which is obviously the first one being the longer period of redirection. Extending that and the feasible problems that you can think of there or is it something that it is not about feasibility, it is just about making it work and having that combined sort of assurance to the customer as they get familiar with switching. We hear from colleagues and friends that somebody switched fine but this one we hear were there any particular issues?

A. (Mr Lynam) Most people leave things until the last minute, so they need to make sure that the extension period does not go on indefinitely, otherwise people might never get around to doing something.

A. (Mr Hemsley) Technically, you can prevent those. Recommendations are not required technically but they are probably sensible to further improve confidence.

A. (Mr Warrington) That is exactly my point. Even the very existence of redirection means something can go wrong and that I think erodes confidence generally.

A. (Mr McCreadie) I know we will come back to the overdraft point but the emphasis is I hear that is it working but the engagement, awareness, whatever, confidence in it, more can be done to base consumer understanding that it will work.

Seems to me it is working, why would we focus an awful lot of attention to something that is working when we have so many things we have jointly agreed are not working.

Q. (Mr Marsden) Just to bottom out this point about just the very existence of having a redirection period of any length or even unlimited length, versus just giving them the assurance of ANP. Do you think they can have ANP and you do not really need to bother with much of the redirection period? Do you think there is net benefit? Richard, I know where you would be but are there others in the room?

A. (Mr Warrington) Yeah, I would be in that campaign, yeah.

Q. (Mr Marsden) Partial switching, let us move to that now. A CASS guarantee for partial switching and the problems or issues you think you would see in that area.

That would help. Again, we are still in the same sort of area of confidence or are we eroding confidence in allowing that sort of test.

A. (Mr Warrington) I think it is a good thing, but there is a part of me, which wonders whether we are just trying to massage the numbers in a way. So there is a lot of partial switching which goes on outside of CASS anyway. There is a lot of switching which goes on outside of CASS and bringing that in to CASS will obviously increase the numbers and sort of make everything look

better than it was before, without really changing anything at all.
I think it is a good thing to try to neaten up all of those elements. I would like those switches who do not go through CASS, I think they should go through CASS, they will get a much better customer experience. Partial switching I would like to see a guarantee on partial switching but I would not then want that to be perceived as a kind of a super success almost in terms of inflating the overall numbers.

Q. (Mr Marsden) Is it particularly difficult for you, Roger, to have partial switches around? Is that sort of thing difficult? Leaving accounts open and then going back and forth. You do not see any particular problems in that area. It must be commercially in terms of managing your businesses.

A. (Mr Lynam) Most consumers when they open a second current account, they will run one up whilst running one down, so I think like I said earlier on, a lot of switching does not actually go on under the auspices of CASS.

Q. (Mr Marsden) So it is just a matter of just testing a product and then it runs down.

A. (Ms Williams-Gardener) People who do want a second account, whether it is going to take over their primary account or not, there is an element, if you go through CASS, everything gets ported. If you do it yourself you have actually got an opportunity of doing a bit of housekeeping, all of those payments that are currently going through your account. Do you want all of them ported or not? It is a moment in time where actually you are prompted to take a little bit of ownership for things that might have been there for a long time, eg subscriptions. I have been guilty of them, I am sure other people are a little bit guilty of them as well, so it is an opportunity to actually get involved with that process and move it for better money management going forward.

Q. (Mr Marsden) How could we improve switching for PCA customers with overdrafts? You see these sorts of suggestions of overdraft eligibility tools, but then they want a firm decision as well. So how does that balance work and how you think the market is going to evolve in that area, things that you are considering that you can share with us.

A. (Mr McCreadie) We would like to solve that. Again, like everything else we have discussed there are lots of complications when you get under the skin of it. Whether it is a bank's risk appetite, what you know about the customer relative to the incumbent bank. What happens when somebody has got arranged facilities that they are using. I think it would be a great thing to solve and it is certainly something that is quite emotive from customers having that automatically come with them.

Q. (Mr Marsden) Both you and the customers -- what is the more practical option? Something, which allows a firm decision or something that, allows them to click and test and it is nothing firm yet, though. It is just an eligibility for their overdraft.

A. (Mr McCreadie) The process like soft searches could be useful.

Q. (Mr Marsden) Could you build something like that into a PCW, price comparison website or other kind of online tool? Would that be helpful? They are constantly clicking and right clicking, is that something that is feasible do you think or would be helpful?

A. (Mr Lynam) You need to be very careful with price comparison websites. I know I sound like a broken record but price comparison websites will ultimately favour the big utility players who can cross-subsidise those initial headline prices. Therefore, they will be anti-competitive.

Q. (Mr Marsden) Do you think the market will tip towards soft credit searches?

A. (Mr Lynam) It is happening. It happens all the time.

A. (Mr Warrington) The one thing I would add is there is a difference between customers who are in financial distress and incurring fees, I would say with a provider where their credit score is likely to be impacted and they are very unlikely to be accepted somewhere else. For that group, there is some sort of intervention required to cap fees or something of that description. Then for the customers who are credit worthy -- I quite liked the idea TSB put forward of a credit passport. I thought that was a good idea.

A. (Ms Williams-Gardener) Some sort of preauthorisation, again, will prompt the switching. They need to know whether they can take their overdraft with them before they are going to go through the rest of the process, absolutely. That should not then be recorded on their credit rating because actually they are looking to move their account, they are looking to do something positive. That should not always be recorded because people could do this multiple times and you would not want it to be going against them.

Q. (Mr Smith) One of the things we looked at was the considerable complexity and variability of overdraft charges. So even if you have a credit passport, you still have to be able to work out which one is best. How would you start to solve that?

A. (Mr McCreadie) I am going to sound like a broken record here but that is why you need something that allows you to have some level of ranking in comparison. Now, in terms of good, bad, indifferent, red, amber, green, you need to have some way of understanding that and Midata might also be a link into it to give you answers.

A. (Mr Hemsley) The challenge is consumers are naturally more positive about their ability to manage money than the reality. Historic data has probably got to be a feature of that over time.

A. (Mr Warrington) Specifically they need two pieces of information, which is how many days and how much, on average, and then you can probably work it out through some sort of price comparison tool.

Q. (Mr Smith) If you had access to your own data in a way which told you that over the last two or three years I have been ten days in overdraft a month and by this amount and if I were to switch to X, the cost of doing that would be --

A. (Mr Warrington) That would be on some kind of traffic light system. Bright red, you have incurred this amount of charges, I am making this up, and you used this many days and this was the average amount you were overdrawn every day. Those two pieces of information are the ones that you need to input into a comparison tool.

A. (Mr Hemsley) Given the comment, Ed, one of the remedies not being pursued is putting a cap on unauthorised overdraft charges. Just wondered about the logic of that?

Q. (Mr Smith) It is one of the ones that we have not pushed forward. As we said at the start, we are thinking about other things that might make sense as a basket of remedies.

A. (Mr Lynam) The single most important thing with consumers is the overdraft, it is not the price. Only that they have the facility for it, which is in why some cases they will put up with high charges or left field charges coming in. So then one of the reasons why the pay day loan business has been so successful, because people know that they can have the loan and they have paid ridiculous fees. The credit passport is perhaps a little more important than the price so I think as much as we are careful about using price comparison websites, it is probably credit appetite comparisons that you are talking about.

If people know that they are not going to get ripped off because there is a common industry standard, I think that then might be helpful.

A. (Ms Williams-Gardener) They could take that one-step further. They could use the traffic light, say they need to go somewhere else, and then have the facility when you are looking to sign somebody up to say to them well here is the outline questions we need from you and if you want to bring an overdraft to us, this is exactly what it would cost you. Not roughly what it would cost but exactly what it would cost you.

Q. (Mr Marsden) Whether it is a credit passport or ANP, and built into that past transaction history and how much is critical?

A. (Mr Lynam) The single biggest benefit that you have from a current account, whether it is a BCA or PCA, is knowing exactly how the consumer or the business behaves and then using that information to make informed credit decisions as well as cross sales.

Q. (Mr Marsden) If those two or four options we have been talking about in this last 20 minutes or so, that is the one which is mission critical as you say for both sides of the transaction, for you and the customer. The other ones are more about perception, customers's perception about redirection, dropped payments.

A. (Mr Lynam) You cannot make an informed credit decision unless you actually know how somebody has behaved in the past. You can rely upon credit reference agencies to give you a certain amount of data but that tends to be historic and backward looking, whereas the current account shows the level of credit coming in, the level of debits going out, whether there is a hardcore balance, gives you real time highly valuable information. Bearing in mind, consumers are very dynamic individuals and their circumstances change over time and therefore the credit decision needs to be as dynamic.

A. (<u>Mr Hemsley</u>) Just going back to my questions, we can probably wrap a bit more around it. It may not be within the scope of what you feel you have been asked to look at, but my question around capping unauthorised overdraft charges is about a social conscience as opposed to a repetitive charging. It does not feel right.

A. (<u>Ms Cattanach</u>) The customers who demand it, never work. The customers for whom the market can never work because they cannot switch.

A. (<u>Mr Emuss</u>) It does sort of link into transparency as well, because the less financially literate do not have to try to figure what all the jargon is, because they know they are not being charged.

A. (<u>Mr Lynam</u>) The interesting thing is that the FCA did introduce this year a cap on short-term consumer credit, which kind of seems to be an odd thing to do and that cap is 0.8 per cent a day. But the reality is that the actual APRs of some of the overdrafts, if you have an overdraft for a couple of days and you get charged a fee, these can run to thousands of percent. But because it is not a short-term credit facility, it circumvents this policy, so that might be an interesting thing to look at.

THE CHAIRMAN: It is worth saying that the research that we did on the customer base who use unauthorised overdrafts, they do not look different in income level from other customers. Clearly, some customers who have unauthorised overdraft are financially distressed. There are also lots of financially distressed people who cannot get overdrafts and there are a lot of perfectly ordinary or even affluent customers who run into unauthorised overdraft towards the end of many months and pay a lot of overdraft charges. That is not an argument against capping but it is an argument against assuming that people who have paid unauthorised overdraft charges are somehow an unusual group who are different from the rest of the population. I am looking at Julie to make sure I have that right.

Q. (Ms Benison) In terms of the capping per se, it is obviously one of the potential remedies that addresses the outcomes. All we are saying at this point in time is that because the remedies package that we put forward, we believe, would address the actual features of the market, then the members believe that at this point in time it is worth pursuing them, but obviously this process is for consulting with the parties and what they think about it.

Q. (Mr Marsden) We have talked a bit about CASS obviously but just to focus on governance of CASS. David, maybe you have a point on this, I do not know, but whether you think that would make any change or are there points that would make CASS work even better or at least perceived to be better or help your involvement with CASS, in terms of whether there should be some independent oversight or other issues.

A. (Mr McCreadie) Broadly, it is working but prior to even CASS coming to operation, we have certainly felt there was quite a driver with some of the larger banks on charging structures. Just sort of penalised the gainer of the switch and therefore as a small bank it is another added cost of trying to attract business from a larger bank.

We ended up, through a lot of debate, lobbying etc, resolving that issue but I guess we just need to make sure there is enough independence and challenge in the debates that take place that do not allow for the incumbents to go through the change they perceive as beneficial to them.

Q. (Mr Marsden) Do you think the dynamic currently within CASS is healthy enough that you do not need an independent oversight within CASS to guarantee that challenge?

A. (Mr McCreadie) I do not think we are guaranteed in the current representation that we have not come against issues in the future. We certainly were one -- take a public example, we were able to get the outcome we were desiring for smaller banks. It does not mean, of course, that guarantees success in future debate that would come up. I think it would help to have some sort of level of independence to give that balance.

A. (Mr Lynam) If anything that keeps the incumbents honest.

Q. (Mr Smith) I am not a hermit. When I started this, CASS was new to me. There seemed to be an issue about soft launch, hard launch, public profile of it, consumer awareness. Is that something that is just me living in a shell or was that the reality and was that to do with the genesis of it and the ownership of it and the promotion of it? I do not know. I am just generally asking because I am pretty worldly wise in reality and I did not know about it, so help me.

A. (Ms Williams-Gardener) I can back that up, I did not know about it but is it sort of turkeys trying to sell Christmas, is that the problem?

Q. (Mr Smith) It is an associated question around governance.

A. (Mr McCreadie) I cannot recall back to the initial soft launch or full launch, but certainly more recently when there has been a requirement, we have certainly felt, as a small provider to raise awareness a bit further as the levels of awareness had not been achieved that were set. The larger banks were against putting more money into it, to raise awareness. So that has been an issue, again, because of how the mix now works. We were able to get that pushed through. I think it is a -- I guess it is keeping the large banks honest to Paul's point. If you want more people who are aware of the service and have confidence in it, talk about a more raised profile, it is quite difficult when the bulk of the funding for that awareness are against it.

A. (Mr Lynam) The biggest single impetus for advertising CASS is when the biggest bank feared ANP and therefore as a defensive mechanism there was a lot more money put by that is the truth of it.

Q. (Mr Smith) I ask the question because I think it is a question around governance and ownership.

THE CHAIRMAN: Can I go back to something that was discussed earlier and ask the same sort of question about it. The existing CASS for full switching requires the original bank account to be closed down; it does not allow you to keep it open. Does that also reflect the interests of incumbent banks, that if you are providing a service to allow someone to switch into your bank you want to make sure that they do not keep their existing bank account open? Was that a commercial requirement or a technical requirement?

A. (Mr McCreadie) I think presumably if customers have made the decision they want to switch, they want to switch.

A. (Mr Warrington) The decision was just made that it was just a full switching service and therefore that account would be dormant and closed, but if you want to keep it open that to me, that would fall within the realm of partial switching. Because you used to be able to switch anything and keep it open etc.

A. (Mr McCreadie) I guess experience in other industries would be a complete switch.

Q. (Ms Benison) I was going to suggest, before we move on to the next section to announce the promised break.

(5-minute break)

Q. (Ms Benison) Thank you so much for coming back. We will now move on to the next topic on our agenda and that is SME lending. I would also want to say that if it is okay with everybody, I said that lunch will be at 12.30 pm. It may arrive around 12.30 pm but if we are in the middle of conversation, I will probably stop it at some point when it is a natural break in the discussion rather than at the exact time. We will try to continue with the agenda as we move along.

Q. (Ms May) I appreciate that not many of you are actually engaged in BCAs and SME lending so this might be a fairly single conversation with Paul and maybe amongst others, but we really wanted to look also at the tendency for most SMEs to go to their primary BCA bank when they have a lending need. I think 90 per cent go straight through to their primary bank and we are trying to look at measures, which might reduce the information asymmetries enjoyed by the incumbent bank. As regards both the customer's transaction data and its credit history. And also look as how to promote engagement and make it easier for SMEs to compare the other lending propositions on offer.

What we have looked at in our Remedy Notice is a number of data sharing initiatives, which are in train or in contemplation, and we have also looked at whether some sort of loans price and eligibility indicator on bank websites might make some sort of difference. So we would be interested, Paul, clearly in your views and any other views on whether data sharing remedies might address the issue of this huge apparent advantage that incumbent banks have. In terms of their privileged information on customer credit and behavioural data, and other ways in which we can instigate much more energy amongst SMEs in looking around and comparing what might be on offer.

If we could start off with whether we think that the data sharing remedies that we have proposed will make a material difference to the issues we have identified .... or any other bright ideas. We have talked about credit passports in the PCA world, whether that sort of thing might translate well to the SME market as well.

Q. (Ms Mansilla) You mentioned credit passporting as a way to simplify the lending experience. I would just be interested in hearing a little bit more about your thoughts about what do you think would make credit passporting work in the market because I guess it has been suggested at various points. What would it include, for example, do we need agreement from banks in order to make this work. How would you get SMEs to participate in that? I just wanted to hear a little bit more of your thoughts around credit passporting, in particular, as a way to reduce the information asymmetries between banks and to make the lending process a lot quicker and simpler.

A. (<u>Mr Lynam</u>) If I start and I should just preface this by saying that prior to taking on this job, I ran the SME bank for RBS and Natwest, which had one in three of the UK SME banking. So I speak from a position of knowing both sides of the fence. To answer your question, I do not think credit passporting will work for SMEs because they are highly complex and there are various groups of people. Some are much more like consumers in behaviour; some are much more like corporates in behaviour. There is no real single point of data, which is a real single version of the truth. The vast majority of the UK's 5.5 million SMEs are not required to produce any financial statements whatsoever. Therefore, the premise upon which you could construct a credit passport is not possible.

You then have the issue of data sharing which is one of the questions that you ask which is -- also fraught with technical and legal difficulties. Then you have the issue of just because somebody else thinks that is a good credit risk, does not necessarily mean that I will. Therefore, I do not want my credit decision being imposed upon me based upon the risk appetite of another organisation, which may have a more aggressive or a more prudent appetite than myself. Trying to come up with a panacea I think is commendable but I do not think it is actually operational.

Q. (<u>Ms Mansilla</u>) Just taking a step back, so there is lots of data initiatives around SMEs, so for example we have the sharing of credit data and that is going to be accessible to banks but also trying to think about what other data, on top of the credit data, for example, the transaction data of SMEs. Would that be helpful and do we need to have some greater thinking about how to extend that and open that out.

Q. (<u>Mr Lynam</u>) If an SME comes to see us today, we will ask them typically for, as an example, the last 12 months bank statements from their BCA provider or BCA providers if there is more than one. Quite often, there are more than one, which is interesting.

If they have any management accounts, which the better ones will have then we will ask to see those but none of those are audited and therefore it is critically important that you can cross reference what they have put in the management accounts with what you actually see in their bank accounts, so you can identify potential fraud. In this space, you will be quite surprised that the prevalence potential for fraud. That information is hugely important.

You then will ask a whole series of questions around what the business plans are for the future, if you are making a decision based upon the business's inherent ability to generate positive cash flow with which to repay the loan facility that they require. You need to make a judgment based on past, current performance, as well as what they are likely to do in the future. To an extent, past behaviour is a pretty good indicator of likely future behaviour.

The reason why most businesses go firstly to their business current account provider, is they know that that bank knows more about them than anybody else. Therefore, they are more likely to get a positive answer from that bank than anybody else. That is the reason why they go there. Same as most current account providers, PCA customers will go to their incumbent bank for the initial credit request.

Q. (<u>Ms Mansilla</u>) Providing the market, the rest of market the same access that that main bank has ie the transaction data, that should put you in a level playing field, I do not know.

A. (Mr Lynam) We get that anyway, so we would ask for the statements and the customers have had to produce the statements so they will sit down in our office and they will download their statements from their online bank account or they would use the physical statements, so we get it anyway.

Q. (Ms May) Is there a way, given if I were an SME and I was looking around the market and you are sitting me down saying, "I need 12 months of this, 12 months of that", and then I go to Barclays, is there a way one can make it easier for the SME to have an experience whereby maybe not at a glance but in swifter and more standardised fashion that information can be shared.

A. (Mr Lynam) It goes back to the previous point around how do you encourage, in this case, consumer and businesses as opposed to consumers to input their data into a central repository. And then, once it is in there, what are you looking to do with it, because it goes back to the point if what this is all about is a business price comparison website, what you are doing is massively in favour of the incumbents as they are cheaper for me and they have much lower capital. Therefore, they will cherry pick all the best and the only thing that is left for the banks and the non-banks will be the crap that the big banks do not want. That is the top issue.

Q. (Ms May) What is your sense of SME willingness to consent to data sharing with credit reference agencies or ...

A. (Mr Lynam) I would suggest that most of them will be reluctant and that will be a combination of concerns about revealing too much which they do not want to do and a lot of these businesses, as I have said previously, operate with cash, as opposed to with money that actually goes through a bank account. You need to be able to understand that as well, particularly for the smaller SMEs. The vast majority of SMEs turnover less than £100,000 a year.

A. (Ms Williams-Gardener) We are not doing SME lending, but one of the observations I would share is when you are looking to open an account for an SME, a business bank account, again with the advance of PSD2 and the openness of data, the person who is coming to you for the account could request the authorisation from their bank or anywhere else where you need that financial data. So you would not therefore be relying on them having to print it out, having to bring it to you. You would also know that it was more genuine, they can reproduce some of these statements, I would suggest so you would possibly be in a better position as that part of the market opens up which would give you the data faster.

Q. (Ms May) The idea of a loans price and eligibility indicator -- I know that I have seen some of your thoughts on that given your thoughts on the advantages that incumbent banks enjoy in other respects, have you thoughts on how as an SME one might get an early indication of what is out in the market in some albeit indicative way.

A. (Mr Lynam) I do not think a blunt instrument such as a willingness to lend indicator is fundamentally going to change things here. I am not sure what your driver is. Whether it is to increase BCA switching or whether it is to increase the availability of SME lending full stop. So I am not sure what the objective is.

Q. (Ms Mansilla) The objective here from our point of view is to open out, at the moment, currently a lot of SMEs go to their main BCA provider and what we would be keen to see is actually a delinking between BCAs and lending and for them to actually consider the wider options of the market. So it may be their main BCA provider, that might be offering a good offering, but also to actually consider other sort of alternatives in the market and that is where we are coming from is that idea of trying to make the process of lending for the SME a lot easier and simpler, so that they do not just revert to going to their main BCA provider. Then also making sure that in the market there are tools there so that they can actually make appropriate comparisons and good financial decisions.

So I think this is where we are coming from and there are lots of activity going around in this area. Around what Government is doing with the referral of the platforms and so it is just really trying to think about there is a lot of things happening for certain sectors within the SME market. Is there more that you can do for if you are not a rejected SME and the idea of the platforms. If you are not a rejected SME is there a way that you can raise awareness about price comparison websites.

A. (Mr Lynam) Almost all of the SMEs that we deal with are rejected SMEs.

Q. (Ms May) Are rejected?

A. (Mr Lynam) They are not going to come to me because I am more expensive. That is the reality of the situation.

Q. (Ms Mansilla) Is that because actually it is more expensive because the credit quality of the SME that is going to you, has already been rejected and so therefore you obviously have to have a premium. But if you had a wider access and SMEs more generally were thinking and shopping around, actually you would get better credit qualities and you would be able to offer them a better price.

A. (Mr Lynam) I know from my previous experience that your average customer, of a large bank, will be paying probably less above base rate than I actually offer to deposit customers. I economically cannot write some of the business that they are writing, therefore I have to operate as many of the other SME operators do in a niche which is outside of the capital sweetpots of the big banks and at a credit appetite that needs to run a bank prudently.

Ultimately, it all boils down to what you have referred to in your very comprehensive reports as the incumbency advantages. These guys have asymmetry of data so they can make the best credit quality decisions. They have the cheapest cost of funding and, in some cases, they have to set aside a wafer thin amount of capital to support that lending than we do. We lose on information, we lose on funding and we lose on capital. That is the reality.

The same then goes to when you look at things buy-to-let. A lot of these specialist buy-to-let lenders are operating in the 80 to 100 per cent LTV range because that is where there is least capital disadvantage relative to the big banks. What we need is the level playing field in funding, in capital and information. That is what would make the difference to UK banking and that is what we had before the current capital regime.

Q. (Ms Mansilla) My final question on information specifically, what exactly is the information that you would need to make it a level playing field.

A. (Mr Lynam) We have the information. The information is not the problem, it is not being able to write the low risk, low price lending because we cannot economically afford to do it. It is not an inability to make a decision and actually make the decision, in some cases, a lot faster than big banks. It is not being economically able to write business that we would ideally want to write. You then have this bizarre situation, which is we have this vicious circle where the smaller banks are growing but they are growing with a higher than average risk portfolio simply because that is the only place within the market that they can operate.

I had this conversation with the FCA a couple of weeks ago. Chris Woolard came out in September and said, "It is lamentable that even now, 80 per cent of the mortgage market is controlled by 6 firms". So we need to break the circle in terms of funding disadvantages and the capital disadvantages otherwise, as I have done in the past, I will be back again in a forum like this in the future, whether it is with the OFT or the CMA or whatever the next thing is called, and really having the same sort of conversation.

THE CHAIRMAN: That is a topic we wanted to move on to next but I want to make sure that Jill has any more ...

Q. (Ms May) Just setting aside the position of smaller banks and new entrants, and just to the point of view of the SME always having been with Lloyds but actually there are other offerings out there be it from Barclays or be it from Metro or whoever it might be, and just whether there were any general observations on how you might break that link between the incumbent provider and the SME by better use of credit rating agencies. Just setting aside the capital issues, which you have highlighted amply, is there still a better way from the SME's point of view that can be more dynamism, more visibility and ease with which you might see that somebody else is looking specifically to lend to agricultural companies and you can actually see that access that and share that data. Just a more general observation on the market would be helpful.

A. (Mr Lynam) I think it is a fair question. Paul Lynam will always be Paul Lynam. Paul Lynam Limited will not always be Paul Lynam Limited because the people running Paul Lynam Limited might change over time and that will drive a difference in behaviour of that particular limited company.
Credit reference agencies do not generally work for businesses in the same way as they generally do for consumers. When you get at the smaller end of the market 500,000 businesses go bust every year and 500,000 new ones are created. It is an incredibly dynamic environment where there is a lot of cognitive bias and physical decision making that is required as opposed to credit score says, "Yes", they have not failed any of the criteria and they have passed through the fraud databases without any difficulty.
We are making, in my business, hundreds of millions of pounds of lending decisions every week in consumers within four seconds and that is because of the availability of information.
You have to, generally speaking, for SMEs apply some physical intervention, which requires skill and experience. To be candid, one of the reasons why Secure Trust and the other smaller banks, lending to SMEs are being successful is that to an extent they have gone back to the old-fashioned way of doing things, which is to give people discretion to make a decision, and they make the decision much more quickly than the big banks do. To an extent, that does give us a chance for a premium price, but it does not circumvent the huge disadvantages in funding and capital.
Q. (Ms May) Last question really is just as an SME, there clearly are advantages to be gained, either perhaps in terms of service quality with Secure Trust or perhaps the latest -- Lloyds push into goodness knows what -- commercial

property. How might one just open up that market and stimulate an appetite amongst SMEs to look more broadly at lending options?

A. (<u>Mr Lynam</u>) If I lend myself at base rate, like the big banks do, instead of 2.5 per cent, I would be able to write a whole lot more business, but I cannot. So the answer to the question is cheaper funding, comparative capital and then normal competitive forces will apply in exactly the same way as we have seen in the supermarket industry where only last week it was announced that Aldi and Lidl have taken 10 per cent of the market. That is because they are not paying more for their raw materials than we are and they do not suffer 5, 6 in some cases 10 times more capital required to open a supermarket than a Tesco and Asda or Sainsbury's. It is as simple as that.

It sounds simple, the solutions are not quite so simple but trying to create initiatives that deal with the symptoms of the problem without addressing the root causes is not actually going to drive ...

A. (<u>Mr Warrington</u>) We do not do business finance but similarly in a prior role I did run a business banking function for a large bank. I agree. I think we are in the same situation we were with the current account market on the scale of challenges. So, if you are a medium sized incumbent, I think some of the things you are suggesting will work. It is all very centralised and the consumer will go to their bank because it is easier. Their bank will be able to make decisions based upon the business current account relationship that they have, where there is cross subsidies, there is already a personal relationship so it is much more centralised than the retail market is. Where you have people like Tesco coming in and offering personal loans or people who are not part of the market coming in and offering loans. It is harder for these reasons for smaller entities to come in.

If you were trying to get more switching amongst incumbents, those sorts of things we have.

Q. (<u>Ms Benison</u>) Just before we move on and it is practically related to what you have just said, one of the implicit assumptions that we made was the remedies package would be potentially implemented across the market. What I am asking is what would be your opinion if some of the remedies could be targeted. Would that make any difference?

So rather than being implemented across the board, they could be targeted to certain participants in the market.

A. (<u>Mr Lynam</u>) I am not very sure what the question is. Which of the remedies -- for example -

Q. (<u>Ms Benison</u>) Paul, you mentioned that some of the remedies that we are proposing would actually quite conversely benefit the incumbent banks to kind of reinforce their incumbency advantages. Putting that on its head, if you like, are there any remedies that would be particularly relevant to change the market by being targeted or being addressed at only certain participants in that market, not everybody else. Just a general question, the answer might be no and that is perfectly okay.

A. (<u>Mr Lynam</u>) Depends on what you are trying to achieve. If you look at why have SMEs being starved of credit post-crisis. The answer to that is the comparative capital requirements that the big banks have relative to mortgages is quite big. If you are a big bank and you can risk a 50 per cent or lower loan to value mortgage at 3.3 per cent and you are starved of capital because of the problems that you have had coming out of the crisis, you are not going to pile into SME lending at a 77% risk weight. That has a societal and an economic impact on the UK.

If you had a broader range of competitors, as we saw in the States, perhaps society would not have had as prolonged a downturn because other banks would have stepped up and filled the vacuum.

You cannot do that unless you have an ability, so if you are looking for -- I suspect George will say tomorrow in his Autumn Statement he wants to do more for SME lending. The way to do that is to help the smaller banks by creating a level playing field.

THE CHAIRMAN: Let us move on to capital requirements. Let me say one thing by way of preliminaries. We well understand the capital requirements issue arises across a range of lending. However, the differential is most striking in the case of domestic mortgage lending, so I want to direct my questions on capital requirements in relation to domestic mortgage lending, just because that makes the issues particularly stark. I realise that risk weights for SME lending are different from IRB banks and standard model banks, but let us just focus on domestic mortgage lending.

I want to ask three questions. One for you. How important is domestic mortgage lending. It maybe that some of you do not do any domestic mortgage lending at all. Starling, you are saying you do not.

A. (<u>Ms William-Gardener</u>) We are current account only, very clear on that.

Q. I imagine Yorkshire Building Society do some domestic mortgage lending. That is the first issue. When we are looking at new and expanding banks, how important is domestic mortgage lending to you.

Secondly, if you do not have IRB status for domestic mortgage lending, how does that affect your lending decisions? Does not having IRB status affect your appetite for doing domestic mortgage lending and your ability to compete in domestic mortgage lending and therefore change your lending book, the shape of your lending book relative to what you would ideally like it to be.

Thirdly, does this affect the overall ability of a bank to enter and expand into the retail banking market? I ask that third question because that is the one that impinges on our terms of reference. Our terms of reference are not about the economics of mortgage lending. We are interested in the IRB issue particularly in relation to domestic mortgage lending as a barrier to entry into the market because for the reasons you have outlining, Paul. If it costs you more to do lending business then that affects the economics of the whole business.

Those are the issues that we are particularly interested in, so Starling are not in domestic mortgage lending at all, but the rest of you are? Would any of you like to say anything about how the extent to which you go into mortgage lending business is affected by the difference in risk weighting.

A. (Mr McCreadie) I will try and answer your three questions. From the market is 45 per cent of banking profits come from mortgages, clearly quite important. Reference back to the point earlier around it is not just about current accounts on their own, it is about actually your mix of business and what income generation you have, what profit you are making and where you make it, so it is very important hence we did launch in the market, three years ago.

We are not on advanced so I can directly answer your second point. It is a barrier. Very sympathetic to the points Paul has been making, today and consistently, and we have been involving together at Treasury on this, but we have ended up, taking decisions about actually reducing lending and mortgages because of the capital relative to other opportunities we have on line now.

We would like to do more and serve more customers. We know it will probably resolve over a period of time, but it really feels like too long a wait when you are sitting running a business today. As Paul described in an SME space, you end up skewing the risk profile of your lending towards the higher end where there are perceived higher margins but through the cycle will there be? Would be a question.

So that is something we would prefer to not to have. We would probably prefer to have a better spread. Why there is no reflection of LTV in standardised risk ratings, I have no idea. In fact, the Treasury has no idea, to be fair.

On a third point, it does then affect your ability to compete on other things, because certainly for us, we are trying to invest and grow a number of different products lines at the same time, where there are large scale advantages the incumbents have.

To be fair we have pretty decent scale on things like personal loans, car insurance and credit cards, but you are not going to be wanting to skew your whole business to that sort of risk either. You want to try and get a better shape to the risk you are taking on.

It has been a serious consideration about whether we continue to lend or not or to what level of lending we are going to take on, because it gets to a stage where it becomes uneconomic to compete. Not just because of the capital but because of the funding costs, disadvantages you have against the incumbents. So I think it is consistent, Paul, with your SME and residential mortgage market. It has left us to take the decision to slow down the number of customers we lend to because of the economics.

A. (Mr Hemsley) I would echo those points in that we are on IRB as a result of the Northern Rock acquisition, but not in the same place as some of the more mature main lenders that we referred to earlier on.

There is no question that in the UK today, it is largely a price driven market, so when you factor the capital costs into your pricing models, it has an impact on your ability to compete. You combine that with the funding advantage that the main high street banks have got through paying nothing on their current account balances, and overall it has an impact on the economics and the parts of the market that you can play in.

A. (Mr Warrington) [✄] There is a series of things we can invest in, in a particular sort of order and this is further up the pecking order than current accounts even, though we would like to be in the current account market.

A. (Mr Hemsley) The ridiculousness of it is the fact that we could all lend to the same person for the same property on the same LTV and have to price it differently, purely because of capital. No difference in the risk whatsoever.

Q. I appreciate in asking you about the economics of your own operations we are treading on slightly delicate territory and I do not want to try to tempt you into saying things that you should not say in an open forum.

Let me put this in slightly more general terms. These issues, from what you said, affect the decisions about what shape of lending book different banks want to have. Does that effect the profitability of retail banking overall for banks that have the ability to do a lot of domestic mortgage lending business because of the IRB is going to do much better than one that has to focus its lending books somewhere else. Or, do you just say, "Oh well, I cannot do too much domestic mortgage lending, but there are plenty of other profitable lending opportunities". Is it an overall disadvantage to the overall commercial success of a retail bank if not having IRB status keeps you out of low loan to value domestic mortgages.

A. (Mr McCreadie) Also for your investor it could be at a lower return. There is a disadvantage in it. If you want a genuine return out of that business that you are having one hand behind your back, to an extent, then clearly there are other areas that you would be looking to invest in.

A. (Mr Lynam) Also talks of the sustainability of the business model. So, the UK mortgage market is £1.3 trillion or £1.7 trillion. Assuming you get the LTVs right, it is the lowest risk type of lending. Therefore, if you want to grow a scale business, you kind of need to be in mortgages and you need to have a decent spread of the mortgage risk spectrum. Otherwise, you run the risk and the situation that we find ourselves in, which is we are economically forced to write higher than average risks simply because we cannot write lower risk lending.

Short-term investors will be attracted to that because they can see short term profits but they will not be there when things get tough. Therefore, it does have huge implications, Alasdair, in terms of how a board sets a strategy to shape its business model.

We do not do regulated mortgages at the moment. We are ready willing and almost able to do that but I cannot do it right now because it is not economic for me to do that. The Regulations as well as the funding are stopping me from reducing the risk profile of Secure Trust as much as I would like. You then have a situation where the regulators look at us, as they do other banks and they say, "You guys are higher risk than average and therefore you have an additional capital overlay" which compounds the standardised effect, which goes back to where we need you guys to break the circle.

Q. As we said in our Provisional Findings, this is an issue that we are still working on. We did not come to a provisional conclusion on it because it is quite a complex issue.

I hope my questions have indicated the kinds of issues that we are interested in and if you have reflections on these questions particularly -- towards your own business and, for example, and I am not going to place you here on it but Starling is not the only new bank that have told us that they are not doing any domestic mortgage lending. If decisions like that are influenced by capital requirements issue, it is an issue we would like to know about, not necessarily here.

A. (<u>Ms William-Gardener</u>) We want to do one thing and one thing very well that being a PCA. Like other new entrants we have the pressures of capital requirements.

Q. The ones that you want to do well is current accounts.

A. (<u>Ms William-Gardener</u>) We will provide a current account which will have the ability for overdrafts and savings ... we do still have similar requirements on the capital requirements. We have no current plans to offer mortgages.

THE CHAIRMAN: But if you are doing current accounts you need to lend your money out somewhere but you are choosing not to lend out on the domestic mortgages?

A. (Ms Williams-Gardener) We will be lending to our client base, we believe our clients will want overdrafts and loans.

Q. Since several of you have mentioned the issue of the funding advantages of large banks let me just underline what we said in our provisional findings so that if you think we have got this wrong then you can either here or elsewhere bend our ears about it.

Let us take it for granted that large banks do have funding advantages. If you have a large current account or savings account business, then you have a source of cheap funds. That seems to be a statement of the way regional banking works. That is the way of the world and let us suppose that gives existing banks an advantage. Our take on that was that any entrant going into retail banking will build up that advantage as it builds up its deposit-taking activities and therefore the advantage of the large deposit taker, which is an advantage that can be competed away if entrants can come in and grow fast in the deposit taking business. You then become big deposit takers.

So our take on it is that is fundamentally an issue about whether there are barriers to entry into deposit-taking business. Is that a reasonable way to look at it?

A. (Mr Lynam) I think you have to look at the other side of the picture. If the only reason you want more and more depositors is because you can do more and more lending, which takes us back to the capital ...

Q. The capital requirement issue is one thing. We are keen to hear more about it, but the funding advantages issue is a separate, second element and you said, Richard, you are an IRB but you face the cost of funds issue, but as you grow your deposit taking activity you become a large deposit taker, no?

A. (Mr Hemsley) You have to break that retail savings market into two macro chunks. There is more than that, but we can talk about it in terms of two macro chunks. The vast majority of that savings market is what you might call the primary market, which is about personal current accounts and the savings that most consumers leave in their personal current account and it has proven to be massively rate insensitive from that perspective.

So most of us, I suspect, around this table are playing in the secondary market, which is significantly more expensive. From the consumer point of view, more positive, but from our point of view, significantly more expensive and that is where we grow our funding from. So, yet again, the very fact that you have got free-if-in-credit current accounts that hold the material chunk of retail savings in the UK, both directly and through the tax savings accounts, puts the challengers at a significant disadvantage from a cost of funding point of view, to the incumbents.

Q. We will come on to talk about free-if-in-credit banking, I promise you, but the statement you have just made, surely, is true only if you are at a disadvantage in growing in the free-if-in-credit market. If free-if-in-credit bank accounts have this tremendous funding advantage then you should be growing your free-if-in-credit current account business.

A. (Mr Hemsley) But that is reliant on the cross subsidisation.

A. (Mr McCreadie) It is only true if you are not growing. I mean, if you have the heritage and history, having the large current accounts and associated savings account and you are rate insensitive, that is fine. When you are competing to grow you are lending deposits. The reality is if somebody can show me where all the customers are that do not want any return on their savings then tell me where they are, but the reality is you have to compete in a competitive market and your marginal rate of funding is much more expensive than the incumbents'.

Q. We think we recognise all of those arguments.

A. (<u>Mr McCreadie</u>) It is probably the expense. I think with you are saying is over time you can get to a scale position. I do not think you can, economically.

A. (<u>Mr Warrington</u>) You can be held at arm's length by the incumbents who can invest in the incentives to switch, which we established is currently the only reason.

Q. When we look at what we could do to make this market work better the answer seems to be that the barrier to levelling the playing field in respect of the cost of funding is whatever barriers there are to growing retail deposit-taking business, ie the high cost of customer acquisition because the customers are sticking. So in relation to things that we could look at in relation to remedies, things that would make it easier for new banks, banks with exciting new propositions for customers to recruit, to acquire customers quickly are the things that would level the playing field. Is that wrong?

A. (<u>Mr Warrington</u>) I agree with that but I do not think you can only look at the pace of acquisition on the challenger side. I think you have to look at the incumbents and the advantage it gives the incumbents, and the ability of the incumbents, whatever tools you give the challengers to grow, the ability of the incumbents to slow that down because of the advantage.

A. (<u>Mr Lynam</u>) But the advantages go beyond simply the back book of deposit customers and the free-if-in-credit current accounts. If they have free-if-in-credit current accounts, it is clearly a massive benefit and that would become

hugely important as base rates rise and that is the single biggest thing.
The second thing is they have the back book of low LTV customers on the mortgage side who they can borrow against on wholesale markets, because it is low risk and therefore it is low cost.
Thirdly, they have the too big to fail status which will remain, notwithstanding your comments. Underneath that scenario those big banks will not be allowed to fail whatever whilst they have the market shares that they have.
The fourth area is they can abuse their back book customers safe in the knowledge that most of them are not walking away. So NatWest wrote to me last week slashing my interest rate on my ISA accounts to 0.25 per cent. A number of my other providers did exactly the same thing. So if I wanted to move, all of the large providers are offering broadly the same price.
Q. Offering a tax-free quarter of a per cent.
A. (Mr Lynam) That actually makes a mockery of the bloody tax incentive in the first place because you can get more by not having savings in a tax efficient product.
Those four advantages are the reasons why. Over time, you are right, theoretically over time the price will converge, but that requires a huge growth in the small banks to eat away at the massive market share of the big guys and until we have something that enables us to kick start our growth, which will be some form of equalised funding scheme which the small banks would pay for, so there is no cost to the taxpayer or to the Exchequer, we would pay that. So we would basically borrow against the UK credit rating in the same way as the too big to fail banks are implicitly borrowing, and therefore that reduces the marginal cost at no cost to the Treasury, at no risk because we

can collateralise it and then that could be an initiative that would kick start the faster rate of lending which then grows the competition, which is your question: "How do you stimulate competition?"

A. (Mr McCreadie) I think also it does take us back to the core issue around transparency and comparability. I guess we are here putting forward as a hypothesis that you can invest and grow. We just feel that to be very expensive. Actually, we would not to invest as much to attract new customers, say on credit and interest in current accounts, if the market operated effectively, if there was transparency and they were getting zero where they are today. So, eight out of ten customers getting zero per cent on their current account deposit and you are providing them with the right information to allow them to make a choice. I guess we have spoken a lot here about lots of little incremental potential remedies, but unless it is something with stronger bite on the large incumbents, even from our opening discussion today, it is probably going to be helpful, it will not be unhelpful, but it will not change the market.

We need to actually have something that is much more about transparency, informing customers to make a better choice and then they can actually scan the market and see where to move to. That will speed up the rate of growth of smaller businesses trying to grow.

Q. I think we agree with that. You want to see a significant change in the market. Having more customer engagement, choice and switching is good not just because it is good for the customer, but because that is a vehicle for having much more dynamic competition between incumbents and between incumbents and incomers than we currently have.

A. (Mr Lynam) Rigorous competition is a much better policeman of conduct and consumer protection standards than any amount of regulation. So all the time the consumer knows that if someone abuses me, like a petrol station, I can drive down the road and go somewhere else. Well, oddly enough, those businesses will behave themselves. It is not necessarily the case all across the spectrum in retail banking.

Q. I want to move on to the remedies we are not pursuing and have an opportunity to talk. We have reflected quite a bit on aspects of free-if-in-credit banking, but we have an opportunity to have a discussion about whether we should look more directly at tackling free-if-in-credit banking, but before we move on to that we will perhaps grab some lunch as well.

I would like to ask about one other issue that we did not pronounce on in the PFs but we do want to look at in our final report, [✂], which is the change in the bank tax. That is not, conventionally speaking, something that we would normally look at as adversely affecting competition; governments change various taxes up and down in ways that they affect people. I think the relevance of it for us is that if everyone is for a general policy push - for reasons which we have been discussing in our report and have been discussing here - to make entry into banking easier because that is where we see the real competition is going to come from. If taxation policy is changing in a way that is going to make that significantly more difficult then that is something that we might be tempted to say something about in our final report.

So I would like your perspective on how the change in the bank tax is going to affect the banking business and the extent to which it is a significant change or just a small change, but we all complain about tax changes even if they are small changes. Any reflections on that?

A. (<u>Mr McCreadie</u>) I mean, I think this will be consistent with what we have said in other forums, but it is not helpful when you are trying to invest and trying to grow a business where you serve customers well that a percentage of it is taken away that you cannot then reinvest.

It also has led to observations by, certainly ourselves and others, that actually there are lots of things we have in the banking entity that do not need to be in the banking entity. The reality is you would have structured yourself very differently if you knew that this tax was potentially coming. So an insurance business, a brokers business does not need to be in the banking entity. An ATM business does not need be a banking entity. I am sure money will flow around in different ways, but when you are trying to be very consumer focused and invest, and you have got to compete on pricing to try and attract new business to grow your own banking business, it is just not helpful.

A. (<u>Mr Lynam</u>) If you think back to when the banking levy was introduced it was done so on the premise that the big banks have, and continue to enjoy, the too big to fail implicit government guarantee, which reduces their funding costs, so therefore there is a financial benefit to them and therefore the levy was one way in which they were paying for that. Now what we have is a situation where the tax take has been broadened to include the vast majority of banks which were not subject to the levy and that will be used to pay for, over time, the removal of the levy. We still do not have the benefits that the big banks get, so you have a bizarre situation where the too big to fail banks are subsidised by the government and we challengers are now going to be subsidising the reduction in the bank levy for them. A brilliant idea.

A. (Mr Warrington) I will talk for mutuals generally, if I can. Again, it is not helpful. Mutuals tend to invest in savings rates in branches in a different business model, so it just continues to erode areas that the business can invest in. It is going to make it harder to get a current account business up and running.

One of the things that we were disappointed in not seeing in the report was just some acknowledgement of the landscape of different business models in the market and how we could move from a system of generally banks and profit-seeking organisations to one which had a more equitable landscape of profitable organisations, mutuals, not for profits. I think things like the levy will make it difficult for mutuals, credit unions, et cetera to come into the market and compete when they already have a branch footprint, local presence.

I would be asking why we are not seeing more of those types of providers coming into the market and that would be one of the reasons I throw at you.

A. (Ms Williams-Gardener) I think the other thing that I would add here, it is certainly something that we have seen, we are not in the position where we will subject to it as we are not yet launched or making those profits, but obviously the aim will be to get there, what we have actually seen is the reaction of investors. So, to your point, there are people wanting to invest in this space and they are looking at those that will be subject to the surcharge and they are looking at the Fin Tech providers who will not. So there is a massive issue that I think, like everybody else, hits us really hard.

Q. Okay, any others comments on anything? Well, as I said this is an issue that we will be looking at for our final report, so any further reflections that you have to feed in to our deliberations?

A. (Mr Lynam) The challenger bank panel, which includes some of the guys around the room, have written to the Chancellor and we have made clear that we have no objection whatsoever to being on the tax footing as everybody else provided we are on same competitive footing. So we are not looking for any advantages we just do not want to disadvantaged.

Q. Okay. Shall we break and grab some lunch, but I would suggest to make best use of time we just bring our lunch back to here and rather than make small talk standing around for 15 minutes we continue with big talk sitting around a table.

The first thing I would like to raise is one that has been touched on several times, which is free-if-in-credit banking. Now, I will not rehearse the reasons that we gave in our provisional report for the provisional view that we do not want to deliberately do away with free-if-in-credit banking, but let me just say it is not that we somehow want to preserve the free-if-in-credit model. If there were much more competition for customers with overdrafts and much more competition for customers with high credit balances, and there is a bit more of that latterly, then the economics of the current model might be called into question and free-if-in-credit banking might disappear. We are not trying to stop that happening, it is simply that we were not attracted to remedies such as requiring the payment of interest on current accounts, which I think is a line that Virgin would be keen to pursue.

Richard, do you want to say something about why you think it would be a good idea to require the payment of interest on current accounts?

A. (Mr Hemsley) I think from our perspective it is really driven by our assessment of, and confidence in, the remedies that have been put forward and, going back to the earlier statement, to what degree we think those factors will have a material impact on the marketplace. I think our assessment, both before the remedies came out and now, is that to drive material change in the marketplace - both in terms of transparency and benefit from a consumer point of view, but also for competition in the marketplace - more material steps need to be considered to drive that activity.

From our perspective we, certainly, believe that if there are steps which are open, and are taken, that will push some of those factors, such as paying interest on current account balances - following the previous conversation just before lunch - we feel that that would trigger greater levels of interest and activity among consumers about the options that are out there and available to them.

The summary from our perspective would be a desire and intent to drive material change in the market over a shorter period than I think some of the elongated timescales that are likely to come from some of the remedies put forward.

Q. You think that would prompt bank customers to be better consumers, to be more engaged consumers?

A. (Mr Hemsley) Well, as we sit here today, I think for many of the reasons we have covered this morning, from a consumer point of view you have got low engagement in the current account marketplace and therefore low switching rates, and therefore low competition, and a lack of many aspects of marketplace innovation. We should be looking for mechanisms to stimulate that initial engagement from a consumer point of view, because the other things will follow off the back of that.

Q. (<u>Ms Bon</u>) What would prevent a bank or yourself from doing that? If you think that that is going to attract customers and promote more engagement why does it need to be forced?

A. (<u>Mr Hemsley</u>) We already have offered a current account which pays an attractive rate of interest, but you are still not stimulating the knowledge and the awareness of the incumbents' practices. We have many, many millions of PCA customers with those four or five largest incumbent banks, very few of them paying attractive rates of interest, keeping back the funding benefit and the cross-subsidisation, often not paying that. By pushing the problem of credit interest into that sector, you will stimulate awareness of the value that actually sits in those balances.

Q. (<u>Ms Bon</u>) I guess what I am trying to understand, and perhaps you have some research with the consumers, how would that stimulate them to move rather than now? So incumbent banks' customers now get interest on their balances, which is great for them, so why would they be encouraged to actually move around?

A. (<u>Mr Hemsley</u>) I think from our perspective we have suggested that as part of a package of measures that would create greater transparency and understanding of what the individual constituent elements of the cost of a current account with the consumer were - one of which is that there is value in their credit balances, so therefore they could be remunerated for those credit balances. It has to come as part of a package.

A. (<u>Mr Emuss</u>) On the opposite side, one of the converse things is why the incumbents are not moving themselves. One of the things we were interested in and one of the things we have been looking at is the recent study on competition in the mortgage market. One of the things they talk about there is the tacit coordination, looking at whether there is tacit coordination in amongst the incumbents.

You are talking a lot about what the challengers would do, but I do not think and certainly I did not come away from reading the report understanding why the incumbents are not changing and with a better understanding of what the current competitive landscape of the current account market is.

I know one of the things that was picked up in the Treasury Select Committee was around profitability and trying to assess individual bank profitability and obviously there were challenges on that. Looking at it from the other side it is just trying to get a better understanding of the competitive landscape from the challengers' point of view.

THE CHAIRMAN: I certainly would not want to represent the views of what you call the incumbent banks. My impression is that they have differing views, but I do not think that they necessarily feel that free-if-in-credit banking is a terribly good model. But no one incumbent would feel able to offer it alone.

One of the things I am struggling a little bit to understand is it might well be that the large banks would like to get away from free-if-in-credit banking as well, it is not that it is somehow held in place by tacit collusion. On the contrary, if tacit collusion were possible they might tacitly collude to start charging monthly fees on all their current accounts, but they cannot do that because competitive measures stop them doing it.

Q. (<u>Ms May</u>) I know Paul Lynam said there is only one Paul Lynam, but just looking at some of his arguments today I would have thought that if you mandated paying credit interest on current accounts and there was a charge following Paul's line of argument the advantages that the incumbents to be able to lure people to more attractive packages, I cannot see why, in that set of circumstances they might not actually pay the highest rate of interest and the lowest charges so it might not actually unlock that opportunity for challengers that you are referring to.

A. (Mr Hemsley) Well, as I say, from our perspective we think it is a right step but not a singular right step. From our perspective, to come back to the same point, it is about the transparency that is there if we are clear with consumers what the value of their credit balances is. At the moment those incumbent banks - what is it - £8.7 billion a year, they are making from PCAs, a significant chunk of which is the value of those credit balances. If we actually put in place a few measures that start to break that, then they have to come forward with clarity about the value of the credit balances, that actually the real value of the services that are provided are charged and open to the customers, and the real value of overdrafts and the administration of overdrafts and unauthorised borrowing behaviour is charged to the customer appropriately. It is a set of mechanisms that force the transparency. I do agree with your point, a single act, it would not drive that.

Q. (Ms May) It is really about transparency. It is about the customer, picking up your earlier point at the very start, knowing what he is paying.

A. (Mr McCreadie) I feel we all have different views on the tools to get there, but we certainly have common views in terms of what we are trying to achieve. We would be reticent to want to have pricing regulation. We would rather find a way to stimulate the market to have effective competition. It does not sound like it is a route that is going to be followed up on anyway, but I think it does take you back to the core issues around the transparency, comparability and engagement with customers.

THE CHAIRMAN: I think it is probably fair to say that the CMA like any competition agency would also be reticent about intervening in the customer relationship between a supplier and a customer. It does not say you may not have certain kinds of price schedules. It is a very interventionist line which I think we would need, based on persuasion, that would be taken.

I am interested in how you would differentiate this proposal from a proposal which TSB has made publicly which is not that interest be charged, but that customers get a statement of foregone interest. It is almost as you are offering the same justification, that giving consumers a statement of their foregone interest might be as effective as actually paying them the interest.

A. (Mr Hemsley) I think our perspective would be - it comes back to the conversation earlier - giving customers information and data would be a step forward from where we are today, but I do not believe that we will see that provide a substantive step up in levels of switching activity. It is like a number of the remedies in here, helpful, certainly not destructive, but would not drive a fundamental change in the market. You are not, at the end of the day, actually altering the financial dynamics of the business itself that sits underneath it.

Q. You are saying to a high balance customer, “Do you realise that the bank is making 20 quid a month off you?” Well, on the face of it that might prompt some of them say, “Oh, there are some banks that will pay me this”.

A. (Mr Hemsley) It definitely will prompt some of them. I think it is the scale of impact that it has.

Q. (Mr Garland) Just following from that if you require all the banks to pay the interest, so £20 a month as an example, does that then not take away the stimulus to move because you are being compensated for the balance that you are holding? I am just struggling with how forcing the banks to pay the interest on the credit balances stimulates people to switch their account if it is reducing the competitive differential.

A. (Mr Hemsley) Again, it comes back to the point of it being a measure in a set of measures which was how we meant to position that. If the consumer has complete transparency of the costs of the services that they are consuming that enables competition to develop more effectively. At the moment we are in a position where for a number of years it is significantly financially penal, from the challenger banks' perspective, to grow our customer base in the current marketplace. If we can get the transparency on charging, it gives us the opportunity to innovate about how we can build products and services that actually customers are then prepared to pay for.

Q. (Mr Garland) Yes, I understand that but I think that the next step is then going beyond transparency and forcing the banks to pay the interest, not just revealing what the interest would be.

A. (Mr Hemsley) Yes, that is our perception. That would be our suggestion. That is our perception about how you trigger that at a greater scale. I think transparency in its own right - and we may disagree - I think is helpful and a step forward, but I do not think it will drive material change in the marketplace.

A. (Mr Emuss) It is coming back to the point that the Chairman made about the incumbents viewing free-if-in-credit as not necessarily a great thing, but having no incentive to move. So this would be a coordinated approach against the whole market rather than challenging the challengers to come up with a solution.

Q. (Mr Whitcombe) You mentioned earlier that introducing this system where banks had to offer interest to their customers, you said that would change the financial dynamic of how a bank operates its business. Could you just talk us through what you would expect the bank to do in terms it is giving money back to the customers, how is the bank now going to try and get that money back? What sort of charges or things would you do differently?

A. (Mr Hemsley) Well, I think there are many models you could look to around the globe that have in some way, shape or form, come up with solutions around that in terms of how basic banking services are funded and paid for. We know that those services cost customers, and we know that they are cross-subsided by either the fees charged around overdrafts or the credit balances. So effectively, as I say, it is one of a number of steps that would be required to drive that transparency, and then there are many routes open to the organisations about how they can price on the other services to compensate for that.

Q. (Mr Whitcombe) And these changes that you would be making to these other services, I am curious to know whether this is part of the story in terms of getting customers more engaged to actually compare facts. I do not want to put words in your mouth, but are you saying that it is easier for customers to compare and engage with these other prices that you are charging as opposed to interest rates?

A. (Mr Hemsley) Customers, broadly speaking, and I know there are examples where this is easier to understand than others, but broadly speaking on a PCA today the customers do not understand the scale of costs or foregone interest that are related to their current account. So I work from the general principle that says the greater transparency they have of that, the greater competition that can come off the back of that, the more innovation in terms of products and services that would then flow through.

A. (Mr Warrington) I agree with the transparency point. For me I would be reticent to see price intervention. I think that is best left to competition.

The other thing is, going back to the earlier conversation, in doing some form of price intervention we are making it all about price as well and I think it is important to just remember the earlier points around service. I think for the vast majority of people it is going to be £1.10 foregone credit interest and no other charges in a month and not really material to them and they would not then think, "Oh, well, that means that the bank is making billions of pounds out of everybody". It would just be simply associated with their own personal view of it.

I think a bigger intervention which would force action, but I am not a fan of this either, would just be the imposition of a fee. If everybody had to pay £10 then that would cause everybody to suddenly look around and go, "Well, actually, it is now much more important that I get value for money for my £10", but I think, again, it is hard for me to conceive how that would be a good thing for the majority of consumers in the market really.

Q. (Ms Bon) The UK is unique in this model, the free-if-in-credit. Other markets where the fees are being charged for current accounts, the switching levels are comparable, so it does not immediately imply that charging consumers would immediately force them to look around.

THE CHAIRMAN: And obviously the CMA is not in the business of seeking easy popularity. We are in the business of finding out the right thing to do for the markets, but I have to say that it would quite a hard sell to say we are in favour in competition, we want to promote competition and we are going to impose a price floor on this market and require everyone to pay a minimum price for their monthly bank account. I think we would all see that as quite hard, and for good reason.

A. (Mr Hemsley) There are a number of drop-off points between those (overspeaking) ...

Q. Absolutely. Yes, and I appreciate your proposal is mandatory interest not the monthly fees, or some other charge would flow from it through competition.

A. (Mr Hemsley) Yes, and I would also, behind that, say clearly that whatever the charges and/or interest it should be reflective of the true value, not a falsely calculated figure.

Q. Incidentally, there are also distributional issues to think about that if we have the move to having a mandated level of interest, as for example a commercial monthly fee, the gainers would be customers with large balances and the losers would be customers with low balances.

A. (Mr Emuss) Which is why we have also suggested price control on overdraft fees as well.

Q. As I said earlier the customer with unarranged overdrafts, on our evidence, are a pretty representative slice of the banking population.

A. (Mr Emuss) But there would still be a segment of the socially disadvantaged.

Q. Yes, but there would also be a segment of the socially disadvantaged who do not have overdrafts because they are not allowed to have overdrafts, who have low balance, lots of ATM use for small sums of money and I think they would probably lose out from the disappearance of free-if-in-credit banking, would they not? It is not a killer, but it is something that we would need to think about.
A. (Mr Hemsley) We are all producing basic bank accounts as well though. So again there are ways and means of working through that.
Q. So people with busy bank accounts would not get interest?
A. (Mr Hemsley) Offering options.
Q. Okay.
Q. (Mr Whitcombe) Let us just play out the scenario where we introduce this interest rate that we have to charge and, let us say for argument's sake, as a result lots of banks start charging monthly fees. If we were to, let us say, believe that story what we would be looking for would be evidence that this monthly fee gets customers more engaged and makes them more likely to hunt around and find a good deal on the monthly fee, and not just that, but also the whole package that the banks are offering. Any kind of comments that you can give us on that?
A. (Mr Warrington) I will say one thing, I think it would get customers more engaged. It is a very specific thing which would drive ...
THE CHAIRMAN: [✄]
A. (Mr Warrington) I think it would be universally unpopular and I think for the vast majority of people it leads to worse customer outcomes which is why you would not do it, but I think it is an intervention which would drive. It would.

A. (<u>Mr Hemsley</u>) It is not a perfect answer to your question, but the most successful PCA over the last few years has been one that both pays interest and charges a monthly fee.

A. (<u>Mr McCreadie</u>) And has the highest overdraft charges.

Q. And many people would see that as the mark of why do we need a mandatory pricing model when banks are able to introduce this pricing model if they wish and some seem to be doing reasonably well.

A. (<u>Mr Hemsley</u>) Because of the economics that it takes to get to that point.

A. (<u>Mr Emuss</u>) And it should be clear, we are not proposing a monthly fee. I mean, the things we have been proposing are price control on unarranged overdrafts and minimum interest rate, as a way of breaking the free-if-in-credit.

Q. Yes, but we have to recognise that if we have a minimum interest rate then the economics of the personal current account are such that monthly fees would follow, would they?

A. (<u>Ms Cattanach</u>) Or some kind of charge.

Q. Yes, some kind of charges, yes, you are quite right. Okay, well, let us not speculate what kind of charges we would make. It would be even less popular than other kinds of charges, I think. A history of free banking would make it very hard for people to be relaxed about incurring a charge every time they stick a plastic card into an ATM.

A. (<u>Mr McCreadie</u>) Yes, because of lack of transparency there has not been uproar about large daily and monthly overdraft fees.

A. (<u>Mr Hemsley</u>) I guess the macro level question, to bring it right back up, is do we think that free-if-in-credit banking is distorting competition in the UK market?

Q. And to answer your question honestly I think our current view, having looked at it in a variety of ways, is that free-if-in-credit per se is not the main source of distortion. It is the general difficulty of engaging consumers and especially consumers making comparisons about where they will get best value. If I have a free-if-in-credit current account that does not, in itself, stop me working out whether somebody can give me a better deal, or make me reluctant to do it. I can call up Santander and see what Santander will offer instead.

A. (Mr Hemsley) It is very, very hard to effectively compare.

Q. I think our view is that the reasons why it is very hard to effectively compare bank accounts are to do with the difficulty of a situation where you need to put a complex bank charging schedule, maybe no monthly fee, maybe no interest, but some charges, against the complicated details of an individual's bank account and the individual who has occasional overdraft or occasional foreign exchange transactions, 25 uses of their debit card and so on, that number of direct debits, putting that against the offer of different banks and working out which one is better for you. That is what is complicated and there are price comparison tools like Midata. That is why that is at the heart of what we are looking at because that is where we see the real barrier to competitive switching, that banking is inherently a very difficult product to work out value for money.

A. (Mr McCreadie) On the basis that most people do not pay for individual transactions like direct debits, it does take us back to seeing the feedback from customers on something at least gives me an indication on the value and cost I pay today without a labelling system. At least it prompts me to get more engaged and think about. I mean some of the quotes from customers, that could be really negative for the bank you are with today. It might prompt me to think about changing. It is an extra reminder that you are getting crap deal. I mean, people were staggered when we put in front of them the overdraft they were paying today and how it compared to what was available to them elsewhere. You need to give some level of comparability on a simple basis. It may not be complete, but then tools such as Midata et cetera could follow on from that, prompting higher levels of engagement.

Q. I take the message that given that overdraft charges are one of the areas where switching is particularly difficult, or people are reluctant to engage, or they are perhaps people who have overdrafts because they have lots of other things going on in their lives that matter more than whether they are paying overdraft charges. But that might be an area where actually quite simple, robust tools to encourage people to shop around might be something worth more attention.

A. (Mr McCreadie) And then the lost value credit interest as well.

Q. I would not want us to go away today without having had some discussion of the biggest thing which we did not do, which is propose that the big banks be broken up. As we said in our report there is a two-fold reason for that of which the main one is we do not see the size of banks per se as being at the heart of the incumbency advantage. It is the incumbency advantage, rather than size advantage. There is some evidence that size does have an effect, but we saw the central problem as incumbency advantage. To put it crudely, having ten established banks with incumbency advantages would not create a much more competitive market than having five banks with incumbency advantages; coupled with the evidence of the huge cost and disruption to customers of the divestments that we are seeing post-2010 with the TSB divestment and the Williams & Glyn divestment persuaded us that breaking up banks was not an avenue we wanted to pursue, but tell us we were wrong and that we have been lily-livered and pusillanimous in not doing this. Anyone want to argue that we should have done more?

A. (Mr McCreadie) Listen, it would have been nice to have gained from some of the divestments but, you know, that is life, from a selfish perspective, but from an overall market perspective then we would agree with that.

Q. I mean I suppose you could still buy Williams & Glyn if you want.

A. (Mr Emuss) I suppose from our perspective it is just really understanding what other structural remedies you would consider, because obviously divestment is not the only one. I mean, obviously, earlier on we talked about some of the things that you thought were more probably the remit of the Payment Systems Regulator in terms of other structural changes. Did you not consider things like that in that context because you thought they were the remit of the Payment Systems Regulator?

Q. Yes. If the Payment Systems Regulator did not exist then the future of the payment system would have been at the heart of our enquiry, the big issue, but as I have already explained we thought it did not make sense for us to pursue that, given the PRS is there.

A. (Mr Emuss) And did you consider any other structural changes?

Q. I cannot think of anything else that we might have considered.

Q. (Miss Bon) What do you have in mind?

A. (Mr Emuss) I do not. I just wanted to know what you considered. And in terms of the remedies you are not pursuing, maybe the clue is in the title, is that the end of it now from your perspective? I mean, I know you said at the beginning, you had provisionally decided not to pursue it?

THE CHAIRMAN: Well, realistically, if someone has come along in the consultation period and has produced compelling arguments for a large scale divestment programme that could not be done within the timescale of this existing inquiry. So, as a practical point, as a practical matter, revisiting a divestment remedy would be very hard indeed, but other than that, no. I mean, if people make strong arguments to us on free-if-in-credit banking and persuaded us that we really needed to look at that again, then the provisional decision on remedies - I am absolutely not promising you anything - if we were really persuaded by paying interest on current accounts then that could be in the PDR. At the moment I think it is fair to say you are hearing voices that suggest we require a lot of persuasion, but our minds are open on it and nothing would stop us putting a proposal like that into the PDR if we thought it was right.

Q. (Ms Bon) The legal constraint is that there is a possibility to increase by six months the statutory deadline if there is sufficient reason to do so.

A. (Mr McCreadie) I think just to mark up the point on divestments, the key thing is not having more people acting the same way, the key thing is actually driving different behaviour. We have heard a few examples today of what TSB are suggesting, but they have not done any of them and they are operating exactly the same as an incumbent. So I do think you are spot on. It would not actually drive change without cultural change and behaviour change, having more banks, if all that happens is more banks act in the same way.

A. (<u>Mr Warrington</u>) More mutuals, that is what is needed.

THE CHAIRMAN: Is there anything that we have not covered today that you came along dying to raise and you have not had an opportunity, that has not come up in the discussion?

A. (<u>Mr McCreadie</u>) I am going to mention traffic lights just to really disappoint you, but just really an open invitation. We would love to come in and talk you through in more detail the customer research insights we gained rather than going through some of the high level things again today. Some of the customer insights if that was of any help to you.

Q. Well, thanks very much for that offer. We will be looking very carefully at the traffic lights proposal and I hope that the things that have been said about it in relation to our overall approach to the importance of effective, prompt and useable information mean that we will want to look very carefully at what you have suggested, and thanks very much for the offer.

A. (<u>Mr Warrington</u>) What has been proposed, I think they are all good, but they are like creeping improvements. I think that is the way I would describe it. So it sounds like the core view of the CMA is that consumers can be convinced with the right information to take action themselves and therefore you have discounted anything which forces consumers to do anything, which would bring putting a fee on the account into place or making it a fixed-term contract, or introducing some sort of intermediary market or something altogether more radical. Is the view that the consumer can be convinced?

Q. Yes, I think that is right, that we thought that somehow if consumers could not be cajoled and convinced into being more active then we would need to think about whether more interventionist remedies would be justified, would be proportionate given the scale of the issues. We are thinking about both things. I do not think anybody looking at the banking market would be hugely optimistic about a radical change is somehow just about to happen, although technological change may bring about some radical change in behaviour. Worthwhile changes can, we believe, be brought about and more interventionist remedies would be hard to sell as being proportionate to the scale of the problem.

Q. (Ms May) [✂]

THE CHAIRMAN: I think in some ways the harder question of that nature is in relation to business banking where the incumbency advantage is not customer stickiness as such, or rather the fact that the customer stays stuck to the same bank through a series of different transactions so you stick with your business bank even when you lose your free banking, you go to your own bank when you are looking for loan finance. Especially that latter step, with a very strong tendency for business customers to get their loans from their existing bank. The market would be more competitive if that link was not there, but that link is there for understandable business reasons.

In some ways our remedies in SME banking are more incremental than in PCA banking where Midata offers the opportunity of there being a real change, whereas in SME banking we were looking at chipping away at a quite deep-seated problem which is deep-seated for good reasons. I personally find it hard to be optimistic about making a big change in SME banking, but that is not because we are timid, it is because that is the world. We have to work in the world that we live in, not the world we would like to.

A. (Ms Cattanach) If we do not anticipate in retail banking that you will

substantially move the dial, there are quite a number of proposals of iterative changes which will have quite a cost associated with them, they will be felt disproportionately by smaller players because they obviously have a smaller base to soak that cost up from. Some of the plea is to say pick a few instead of a lot of very tiny incremental changes because you will end up with a cost burden that will actually disadvantage challengers. If your own anticipation is it not going to really move the dial then do not do a lot of small things that are not going to move the dial.
Q. (Ms Bon) I was hoping that it will move the dial.
THE CHAIRMAN: Yes, indeed.
Q. (Ms Bon) Yes, but in a proportionate way, absolutely.
Q. (Mr Hoehn) In response to what you said about the customer focus. I think it would be wrong to just see our remedy proposals as being customer-focused and focused on customer behaviour. It is also on bank behaviour. So if there was a price or quality comparison website or some way of making more transparent what the banks charge and how, or what rewards they give, then it would also, in my view, affect the behaviour of banks and, certainly, competition, just the interplay between demand and supply.
Q. (Mr Whitcombe) We have said we are interested in some more ideas in terms of what things we can do to get customers engaged. I guess maybe one way of rephrasing the question is say we set banks a target. Say, there are some indicators that we can measure in terms of how engaged customers are, for example are they searching? If we were to set the banks targets and there was a system in terms of incentivising banks to hit those targets, what type of things do you think banks might come up with to get customers engaged?

You mentioned traffic lights.

A. (Mr McCreadie) I think on all these things you just have to be very careful about what you are measuring, why you are measuring, what outcome are you trying to get to and what is the most effective way of getting there. I would be quite concerned about setting targets for clarity of purpose. It might just drive the wrong behaviour to achieve the target and nothing changes. So, I guess the unintended outcomes of any action or proposal like that would just need to be thought through.

Q. (Ms May) Just picking up on Julia's point about the cost burden of some of the remedies, potentially. Given that this is proposed currently, potentially, as a package, so inevitably the incremental pieces will add up to something more substantive, I imagine it would be helpful if you have got thoughts on any of the things we have discussed today as to what would be, to your mind, proportionally expensive to implement. That would be interesting information for us so that we can weigh it all up.

A. (Mr McCreadie) Account number portability.

Q. (Ms May) Account number portability.

A. (Mr McCreadie) Switching was a big expense, so account number portability would be many times worse.

Q. (Ms May) I know that one, but there might be others which I am less familiar with the costs.

Q. (Mr Whitcombe) It is a diverse market, is it not?

A. (Mr McCreadie) I do not think the issue is in this room, to be fair.

A. (Ms Cattanach) The devil will be in the detail. So the concept of Midata, it depends the way you do it, what the impact is.

A. (Mr McCreadie) If that was ten events it is very, very complex. Lots of processes, how do you deliver it to the customer, how do you know they have read it? So it seems sensible. You want to have some level of prompting, but make it impactful on a few.

THE CHAIRMAN: Well, we are certainly very committed to looking before we finalise the package of remedies. We are doing a lot of behaviour review and related research with consumers to make sure that if we do impose costs on you that the costs have a return. The worst possible thing to do would be to have a remedy, whether it is very costly or only a little bit costly that has no effect.

We know that the past history of interventions in financial markets is that lots of plausible looking remedies do not actually have any impact on the market and that is most definitely not worth doing and we are going to try and avoid doing that.

A. (Mr McCreadie) I think also just recognising that whatever the remedies and the cost of them are, again, large scale operators always have an advantage of how they can recover that cost relative to smaller players, meaning not very much to every individual customer.

Q. Okay. Well, thank you very much indeed for coming today. It has been a very useful and wide-ranging discussion for us and to those of you who have made formal submissions to the PFs, on those remedies, thank you very much. We look forward to further engagements with you in due course. Joanna is there anything else we want to say?

Q. (Ms Benison) The only thing I can say is a reminder that the transcript will be available to yourselves to check for accuracy and then we will publish it. We have just started our response hearings and roundtables. We will hear from consumers and SME customers and hopefully that will also give us a lot of food for thought in terms of what the effectiveness of the remedy package might be and the milestones I mentioned at the beginning. So a provisional decision on remedies in February. That is, again, just provisional decisions so there will be consultation afterwards as well with the view to finalise the enquiry at the beginning of May. Thank you very much.

Key to punctuation used in transcript

--	Double dashes are used at the end of a line to indicate that the person's speech was cut off by someone else speaking
…	Ellipsis is used at the end of a line to indicate that the person tailed off their speech and didn't finish the sentence.
- xx xx xx -	A pair of single dashes are used to separate strong interruptions from the rest of the sentence e.g. An honest politician – if such a creature exists – would never agree to such a plan. These are unlike commas, which only separate off a weak interruption.
-	Single dashes are used when the strong interruption comes at the end of the sentence, e.g. There was no other way – or was there?