21.03.16

TSB Bank plc

Response to supplemental notice of possible remedies

Introduction & overview

1. This response provides TSB's views on the CMA's supplemental notice of possible remedies (the "Supplemental Remedies") dated 7 March 2016, in respect of its investigation into the retail banking market.

2. TSB welcomes the CMA's focus on improving outcomes for overdraft users. As TSB noted in its response to the CMA's additional remedy suggestions (the "Additional Remedies") published on 18 December 2015 and in its notice of possible remedies (the "Remedies Notice") of 22 October 2015, TSB recognises that many overdraft users feel unable to switch, despite having the most to gain from switching their account. The CMA's own analysis suggests that average overdraft users could save up to £140 a year and heavy overdraft users could save up to £260 a year by moving to another provider.

3. TSB, however, would point out that the problems that overdraft users face are the symptoms of a more fundamental problem relating to the uncompetitive nature of the market as a whole and so tackling them should not be seen as sufficient in itself. In order to address the underlying problems with the banking market and improve outcomes for all consumers including overdraft users, it is therefore important that the CMA focuses its remedies on driving transparency and removing perceived barriers to switching across all areas of the banking market. Only then will customers be provided with the tools that they need to actively manage their banking services and be able to switch PCA provider freely.

4. As such, while it largely welcomes some of the additional thinking outlined by the CMA in the Supplemental Remedies, TSB contends that more needs to be done to ensure that customers are aware of the true cost of their banking and can fully participate in the Current Account Switching Service.

5. TSB maintains that the introduction of both a Monthly Bill – so that customers are fully aware of their cumulative monthly overdraft charges and its overall impact on their finances – and the introduction of a Credit Passport – either through a Credit Reference Agency or the work of the Open Banking Working Group – are essential to improving outcomes for overdraft users and driving transparency in the banking market.

6. Below, TSB first explains why in its view the Credit Passport (or at least enabling banks to share, prior to the customer choosing to switch, the transactional data that would be required to be included in the Credit Passport) should be considered a key feature of the CMA's package of reforms on improving outcomes for overdraft users and why it should be facilitated as quickly as possible. Then in the following sections of this submission TSB responds to each of the Supplemental Remedies outlined by the CMA .

The Credit Passport

7. TSB welcomes the CMA's focus on making customer-specific transaction data more easily available and usable, and notes the CMA's support of the work of the Open Banking Working Group as a means of implementing Remedy 3 (facilitating price comparisons by making transaction data more available) as outlined the in original Remedies Notice.

8. TSB believes that giving banks access to relevant and accurate historical transaction data prior to the customer choosing to switch, is essential for improving outcomes for overdrafts users, as it will increase the likelihood of banks being able to match a new customer's existing overdraft limit at the point of application or inquiry. This will address an underlying problem with the PCA market where many overdraft users feel "trapped" with their current provider, as they are unsure that their overdraft will be matched if they switch to a cheaper account; or they may have to wait three, six or even nine months (as transaction data builds up) before becoming eligible for a suitable overdraft. In order to address this perceived barrier to switching, TSB has advocated the creation of the Credit Passport.

9. While TSB recognises that the Credit Passport's objectives can be delivered through the Open Banking Working Group, TSB contends that this will take longer to deliver than through the Credit Reference Agencies, which already have secure channels for submitting customer data to banks. TSB notes that the Open Banking Standard is still being developed and it continues to face significant technical, legal and regulatory obstacles. The full scope of the Open Banking Standard is not due to be delivered for several years – at best by 2019. TSB is concerned that without proper regulatory oversight, the Open Banking Working Group will not be able to deliver much needed changes in the banking market for some time.

10. TSB also has concerns over the ownership of the data being sourced by the Open Banking Working Group. Given that all customer transaction data is being retained by the account holder's bank rather than being shared via an impartial third party (as with the Credit Passport), there is a risk that not all participants in the Open Banking Standard will be given full access to each bank's customer transaction data (so far as this is authorised by the customer) that is necessary to make the overdraft eligibility decisions mentioned above, particularly as banks are given the opportunity to redact information in certain circumstances.

11. If, nevertheless, the CMA contends that it would be more proportionate or effective to deliver the Credit Passport's objectives through the Open Banking Working Group, TSB asks that the CMA consider the following terms for its final remedies in this area:

    I. Ensure that the Open Banking Standard facilitates the sharing of the type of data that the Credit Passport remedy would require (prior to the customer choosing to switch) as outlined in TSB’s submission on the Credit Passport of 20 November 2015 (e.g. by making sure that the transaction data required is classified as data which the customer is authorised to share via the Open Banking Standard). All banks should be required to deliver data to a minimum standard.

    II. Implement a mandatory timeframe for the Open Banking Working Group to deliver the Credit Passport's objectives so that overdrafts users are able to benefit from full access to the switching service as soon as possible.

    III. Ensure that challenger banks have a fair and equitable input into the designing of the Open Banking Standard.

    IV. Require the Open Banking Working Group to allow all banks equitable and secure access to customer transaction data. This may be facilitated via the governance structure which the Open Banking Working Group is planning to develop shortly.

<u>**Prompts and alerts to inform customers of imminent and actual overdraft usage and charges**</u>

12. TSB believes that overdraft alerts are an important tool for helping customers manage their money and contends that all banks should offer alerts to customers.

13. TSB believes that there is merit in the CMA exploring options for auto-enrolling customers into an alert that informs them when they have gone into, or are just about to go into, unplanned borrowing. For more complex or tailored alerts however, TSB believes that, on the whole, rather than being auto-enrolled, customers should be given the opportunity to pro-actively choose at account opening what information they do and do not want to receive from their bank.

14. TSB contends that giving customers an active choice in the alerts and number of alerts that they receive will result in customers becoming more engaged with their overdrafts and PCAs more broadly. It is also worth noting that auto-enrolment for some alerts may prove difficult since:

    a. Not all customers choose to share their mobile number or email address when they open a bank account.

b. some of the alerts would be difficult to administer without active customer input, e.g. the "High and Low Balance" alerts currently provided by TSB[1] which require the customer to set the levels that will determine when he/she is alerted of changes to his/her account balance. TSB's own experience is that customer preferences regarding when they would like to be alerted (e.g. how close to a zero balance) vary significantly.

15. TSB believes that the list of alert types outlined by the CMA are comprehensive and contends that, although SMS messages are the most effective way of communicating overdraft alerts to customers since they are likely to be accessed instantly, customers should be given the choice over the channel through which their bank communicates with them. The CMA should also give consideration to the pace of technological change in this area, as over time alternative alert forms (e.g. push notifications via mobile apps) may become more relevant.

16. In order to ensure take-up of the alerts, it is important that customers are made aware of alert services provided by their bank. Banks should be required to promote alert services during the account opening process and could look to remind customers about overdraft alerts when customers are notified of overdraft charges.

17. Alerts should provide customers with a “call to action” including advice on what customers can do to avoid charges – e.g. by reminding them of the grace and retry periods which they can take advantage of to avoid engaging in unplanned lending. As the options available to customers will vary depending on account type and circumstances, PCA providers should be given the flexibility to tailor the content of “calls to action” to individual customer needs. It should also be noted that the content of “calls to action” may be limited by functional constraints depending on the medium through which an alert is sent – i.e. how many characters can be used in sms alerts.

18. Communicating cumulative charges to customers on a monthly basis, could also be a helpful tool that enables customers to understand the broader impact of their overdraft on the overall cost of their current account.

19. Rather than only providing information to customers on cumulative charges through alerts, however, TSB contends that this information would be best delivered as a key component of a Monthly Bill. By displaying overdraft costs every month in a clear and succinct manner, customers will be able to form an accurate ongoing picture of how their pattern of account usage affects the cost of their account. These costs will also be displayed alongside the other benefits and costs of the customer's PCA usage (e.g. interest, account fees, cash-back, etc),

[1] Please see TSB's response to Question 1 of the CMA's information request on Personal Current Account ("PCA") overdrafts, dated 22 February 2016.

meaning that the customer can make an informed decision about the overall value of his account, based on his/her personal use.

20. The regularity of the Monthly Bill will also mean that customers are continually kept abreast of what their PCA lending is costing them. Alongside the other prompts and grace/retry periods discussed further below, it will give customers the opportunity to change their behaviour going forward so as to avoid incurring these costs in the first place. TSB would note that the format of Monthly Bill can be easily amended to contain the 'calls to action' advocated by the CMA at paragraph 56 of the Supplemental Remedies notice.

21. Therefore, TSB contends that, while prompts on cumulative charges may prevent customers from incurring fees in the short-term, the richer and regular information provided via the Monthly Bill will foster more meaningful customer engagement, encouraging customers to assess and change their behaviour on a longer-term basis. (TSB notes that the effectiveness of a customer bill or statement provided on an annual basis has been questioned, but one of the points about its remedies proposal is that, rather than being annual, it is monthly or otherwise sufficiently regular in order to promote genuine and sustained customer engagement.)

22. TSB notes that the CMA is considering prohibiting PCA providers from including arranged overdrafts within the definition of 'available funds' based on the premise that this can lead to customer confusion about what funds are available to use without incurring overdraft charges. TSB believes that that bank already makes it clear to customers what funds are available to them without incurring a charge but would be open to further consideration of the CMA's proposal if the regulator has received customer feedback indicating that more needs to be done to make this definition clearer.

<u>Offering customers the opportunity to "opt-out" of unplanned overdrafts</u>

23. While unplanned overdrafts should not be used for regular borrowing, they do provide a valuable safety net by which the bank covers important payments when the customer is in unexpected financial need – such as authorising a payment for a utility bill that is paid for by direct debit, where if it fails a customer would run the risk of being cut off from the utility service. It is also notable that, as recognised by the CMA, "customers perceive that they use unarranged overdrafts less often than they actually do, as well as perceiving that they do not use it at all when actually they do".[2] This is why TSB believes it is important to offer an unplanned overdraft as a default position when opening a new account (subject to the customer meeting eligibility and affordability checks). Otherwise, there is a risk that a

[2] See Appendix C, paragraph 5 of the CMA Working Paper: Actual and perceived behaviour of personal current account customers (revised) , revised on 18 August 2015.

significant number of customers will not expect to use and not opt into an unplanned overdraft, with the result that they subsequently miss critical payments on the handful occasions when they unexpectedly need an emergency, temporary facility for a few days.

24. However, TSB recognises that having an unplanned overdraft facility on a PCA is not right for all customers. Therefore, provided that the potential adverse effects of opting out of unplanned overdrafts are clearly articulated to customers, TSB considers that all customers should be given the opportunity to opt out of unplanned borrowing at account opening. TSB also contends that banks should give customers the option of opting out of future unplanned borrowing when they are notified of unarranged overdraft fees being applied to their account.

25. TSB supports giving customers more control over unplanned overdrafts and is open to exploring whether it can still provide protection to customers from missing particularly important payments (e.g. specific utility or rental payments) – even in the event that they opt-out from using an unplanned overdraft for the majority of payments. However, TSB does not believe the CMA should mandate how the banks should make customers' unplanned overdraft customisable (e.g. applicable to only certain transactions). Efforts to tailor unplanned overdrafts to each specific customer are likely to face practical and technical challenges (as explained further in the following paragraph). TSB believes that in this area PCA customers are better served by leaving banks free to compete for customers by improving their overdraft offering to meet each customer's bespoke needs most effectively. By contrast, if the CMA obliges all banks to provide, for example, an unplanned overdraft opt-out for specific transaction types, this will remove the incentive for banks to innovate their overdraft offering in order to capture customers. Instead, the CMA's mandated product features will become the standard which all banks follow.

26. Aside from the broader concern of inadvertently stifling competition and innovation, there is also a risk that the CMA will oblige banks to adopt product features which would face significant unforeseen practical or technical obstacles. TSB believes that it would not necessarily be useful to give customers the opportunity to "opt-out" of unplanned borrowing depending on "transaction type". The relative importance of a particular payment to a customer does not bear close relation to whether it is made via debit card payments, direct-debit, standing order or cheque (etc). Therefore, defining an unplanned opt-out by the type of transaction that is taking place, is unlikely to be meaningful for customers. For example, while a customer may be willing to go into an unplanned overdraft to pay a standing order for a rental or utility payment, other standing orders may be deemed less important, such as gym membership or contact lens subscriptions – despite all these transactions being defined as the same "transaction type". In view of its complexity this intervention may be difficult to deliver at an industry level.

27. TSB notes that the CMA recognises that banks may levy a charge or remove account benefits if customers choose to opt-out of unplanned borrowing. TSB contends that, since the charging structures of PCAs vary depending on a bank's risk appetite (as the charges for providing unplanned overdrafts take account of the credit risk undertaken from providing the service), banks should be given the flexibility to manage pricing independently, and set and apply set their own charges for an opt-out service. So long as the CMA also implements the transparency and customer engagement remedies suggested, the price of opting out of unplanned lending would become another area of competition.

<u>Introduction of suspension periods for unarranged overdrafts</u>

28. Grace periods and retry periods are useful safety nets to help customers avoid charges on their PCA products, which is why TSB is committed to promoting and providing this service for customers.

29. However, grace periods and retry periods are linked to payments processing times (e.g. for cheques, standing orders, and direct debits). Therefore, it may not be practical for the CMA to explore options to increase suspension periods as the CMA would need to ensure that a corresponding change is made to industry-wide payments processing times, which would require the input of payment system operators and their numerous participants.

30. Moreover, increasing suspension periods too far may have unintended consequences for the customer. Unplanned overdrafts should be used only in the event of emergency when the customer unexpectedly exceeds his/her planned overdraft. They are a line of credit of last resort intended to protect the customer from missing critical payments in a time of need for a brief period of time. However, if the suspension period was significantly extended, customers may start to use grace periods and retry periods on a regular basis as an extension of their regular planned overdraft. Given that unplanned overdrafts fulfil a fundamentally different need, TSB is concerned that this could result in customers taking on debt that they cannot necessarily afford on a sustained basis.

31. TSB does, however, believe that banks should be able to define their own "buffers" beyond the grace period – but believes that this should be decided by each bank on an individual level. This will enable banks to compete with each other on the size of additional buffer that they offer.

<u>Introduction of a maximum monthly charge (MMC) for unarranged overdrafts</u>

32. TSB does not set a total £ cap on the amount charged for use of an unarranged overdraft, but it does put a cap on the number of charges (excluding interest) a customer could incur in

a billing period.[3] TSB believes that, by providing customers certainty regarding the maximum level of fees they will incur in a billing period, customers will be better able to control their borrowing and plan their finances better.

33. TSB therefore agrees that it is in the interests of both customers and PCA providers that banks apply an appropriate cap on the charges incurred by customers for using their unarranged overdraft. Any cap should be applied monthly, as customers typically run their finances on a monthly cycle (given that key payments like rent and utilities are debited monthly). Although TSB currently has separate monthly caps for overdraft charges and returned item fees, TSB is open to exploring the adoption of a single overall MMC, provided that each bank has the ability to set its own levels for that directly.

34. While agreeing that all PCAs having an MMC would be beneficial, TSB would not, however, support the introduction of a regulated upper limit for MMCs and contends that forcing one pricing model on the market is unlikely to work in the best interests of all customers or market competition. Instead, the level of the MMC should be a matter for each bank to determine for each PCA product or otherwise agree with customers – and then communicate this clearly to them.

35. As explained above, TSB contends that banks should be left to compete on how to best meet customers' varying needs by innovating their overdraft product offering. Similarly, TSB believes that it should be free to set the price by which they cover the costs of this innovation and their wider PCA product offering. Any prescribed MMC risks having the unintended consequences of stifling innovation and competition for overdraft users, rather than promoting it.

36. A prescribed MMC would also fail to take into account each bank's different risk appetite and credit risk management strategies. TSB's own analysis has revealed that expected losses from unplanned lending are over [redacted] times higher than for planned lending, and it believes it should be given the opportunity to price unplanned overdrafts in accordance with this risk profile. If a regulated cap was placed on unplanned lending which did not reflect the risk or cost to a bank a likely outcome would be that banks would simply cease offering this important service to customers as it would be uneconomic to do so.

[3] The maximum number of Unplanned Daily Fees that can be incurred on a customer's account is 8 per monthly billing period (set at a maximum £10 per day). An additional £6 Monthly Overdraft Usage Fee is charged (unless this has already been paid when the customer uses their planned overdraft). So the maximum monthly total is £86 plus debit interest. The maximum number of Returned Item Fees a customer can occur (£10 per item) is three charges per day. For further details please see TSB's response to Question 1 of the CMA's addendum to January 2016 information request on Personal Current Account (PCA) overdrafts (dated 22 February).

37. TSB also notes that imposing a prescribed MMC is unlikely to increase customer engagement with overdrafts or encourage switching. Rather, the upper-limit of the prescribed MMC will likely become the standard charge levied by all banks. By making overdraft services and charges more homogenous, the CMA's remedy may in fact discourage switching.

38. Finally, it is worth nothing that a prescribed MMC would take no account of the different benefits and charges that customer receives/pays for the other services they use via their PCA. Different PCAs have different price points, and if customers were provided with full transparency of what their banking is costing them on a regular basis, through a Monthly Bill, this should incentivise banks to compete on different levers: some may choose to compete more strongly on overdraft pricing (including through a lower MMC) to attract the sorts of customers who find that most important, while others may choose to compete on other aspects of the overall PCA offering.

Conclusion

39. TSB welcomes the CMA's further efforts to increase customer awareness of and engagement with their overdraft usage and charges, to help customers manage their overdraft usage and to reduce barriers to switching PCAs. Therefore, TSB sees merit in mandating that all banks adopt some consistent standards relating to the disclosure of account information (e.g. relating to the cumulative cost of their overdraft usage) and processes to help ensure customers are given the opportunity to avoid incurring fees in the first place.

40. Linked to this, TSB maintains that the most effective way to protect customers is to ensure that they understand how their behaviour affects how much their account costs, to give them the opportunities and tools to effectively manage and (where possible) reduce their costs, to encourage them to consider alternatives, and to ensure that they have tools to compare accounts and switch with confidence. This is why TSB continues to advocate the Monthly Bill and the Credit Passport.

41. However TSB would also point out that, if the CMA focuses on obliging banks to adopt certain overdraft product features or if it imposes price controls, this could have the perverse outcome of stifling innovation and, in fact, may result in overdraft customers becoming more disengaged with their PCA offering, given the risk that all banks will likely adopt the same product features for the same price.

42. TSB is fully open to the CMA using existing industry initiatives to boost transparency and engagement of overdraft users – e.g. regarding the adoption of Open APIs (the Open Banking Standard) via the Open Banking Working Group. However, if the CMA does this, TSB would ask that it ensures that these vehicles are given a clear mandate and specific

timeframe for delivery, so that they can focus on achieving the CMA's objectives as quickly as possible.

43. Moreover, TSB believes it is clear that the difficulties affecting overdraft users are symptomatic of the wider problems resulting from an uncompetitive banking market. Outcomes for overdraft users will only truly be improved when the banking market is made more dynamic as a whole and TSB would urge the CMA to ensure that its overall package of remedies focuses more broadly on driving transparency, prompting customers to review their account regularly and removing barriers to switching.

* * *