

# **CMA CONSULTATION: PERSONAL CURRENT ACCOUNTS AND BANKING SERVICES TO SMALL AND MEDIUM-SIZED ENTERPRISES**

## **A RESPONSE FROM YORKSHIRE BUILDING SOCIETY**

### **1. Introduction**

- 1.1. Yorkshire Building Society (YBS) Group welcomes the opportunity to respond to the CMA consultation on personal current accounts (PCAs) and banking services to small and medium-sized enterprises, published in July 2014.
- 1.2. YBS is owned and governed by our members and is Britain's second biggest building society with over 3.4 million customers. Our primary business areas are deposit-taking activities, mortgage sales and administration and mortgage related insurances. We operate via a number of distribution channels including telesales, postal and the internet. Our primary distribution channel is, however, via our network of 231 branches across the YBS network and the other brands we trade under – Barnsley Building Society, Chelsea Building Society and Norwich & Peterborough Building Society. YBS also has a wholly owned subsidiary, Accord Mortgages Limited, which handles intermediary mortgage business.
- 1.3. In terms of the personal current accounts market, YBS offers current account services through its Norwich and Peterborough Building Society (N&P) brand. This service from N&P has been a longstanding proposition with a base of around 100,000 customers, 86% of which are from within the N&P heartland of East Anglia and Lincolnshire. YBS has a stated intention to introduce a new current account service across its network and brands for the benefit of its own members and as a 'mutual alternative' to challenge the dominant providers of the market. YBS believes that a competitive and well-functioning PCA market should provide a climate for new entrants and challenger institutions, across a variety of models – including consumer-owned mutuals – to be in a position to make a significant impact on the sector (which remains highly concentrated and therefore not operating in the best interests of customers). YBS believes that this would represent a significant step in facilitating a diverse, dynamic and innovative banking market in the best interest of consumers.
- 1.4. YBS does offer a limited SME banking service through its N&P brand, though YBS is, relatively speaking, a small player in this market. YBS does not, at present, have plans to expand this service across its network, but will keep this under review. As with the PCA market, YBS believes that a competitive and well-functioning SME banking market should provide a climate for new entrants and challenger institutions, across a variety of models to make a significant impact on the sector. For the purposes of this consultation, however, YBS intends to focus on the PCA market, given its importance to YBS's current and future operations.

### **2. Response to key consultation questions**

- 2.1. YBS welcomes the CMA's provisional decision that a market investigation reference (MIR) is made in relation to both PCAs and retail banking for SMEs. YBS has held longstanding concerns about the functioning of these sectors and believes that a MIR is an appropriate course of action. Furthermore, it is clear that previous market investigations in the PCA sector have not led to any material shifts in the structure of the market. Therefore, more assertive and effective regulatory intervention is needed to establish a more competitive and dynamic market that ultimately generates better customer outcomes. YBS has set out below its views in relation

to the CMA's consultation questions and has outlined its own proposed remedies to the PCA market, which include:

- A structural review of the PCA sector (with potential further divestitures to tackle high levels of market concentration that would otherwise take too long to achieve through natural competitive forces)
- Require an overhaul of overdraft pricing – one of the main commercial enablers of the 'free in credit' model
- Mandate account number portability – to help unlock inertia (given that account switching has only grown modestly since the launch of the Current Account Switching Service in 2013)
- Mandate free ATM access for all customers with a UK debit card to all bank-owned or bank-controlled ATMs. YBS and its members have a long stated concern on this issue, campaigning against the proposed wholesale removal of free withdrawals from other banks when it was last attempted. Mandated free access would help establish a 'level playing field' and prevent large incumbent players exploiting their dominant distribution positions.

***Do you consider that the CMA's analysis of the suspected features of concern in the market for PCAs is correct?***

2.2. YBS agrees with much of the CMA's analysis of the PCA market, as set out in paragraph 3.6 of the consultation document. YBS believes that the main structural issues facing the PCA market are related to an inter-connected relationship of: (1) high levels of market concentration; (2) low levels of switching and high inertia; (3) low levels of innovation and differentiation; and (4) the dominant free-in-credit banking model that relies on cross-subsidisation.

2.3. YBS also agrees with the CMA on its analysis and conclusions (both in the consultation paper and Chapter 3 of the PCA Market Study Update) with regards to the issue of a lack of transparency in charging structures. Many of the dominant providers use overdraft fees and charges – which are not readily transparent or understandable, and are not a key factor in the decision making process for customers selecting a current account provider – as a key source of revenue and use this revenue to effectively cross-subsidise other products and services in the market. Some of these fees and charges are significant and there is a risk they could represent poor value for customers. They are potentially also incurred by those customers who are least able to afford them. In some cases, the costs of overdraft fees are greater than interest charged by payday lenders. Not only does this practice risk acting against the best interest of customers, it also distorts the market and acts as a barrier to competition and new market entrants. YBS has suggested some potential remedies to this practice below.

***Do you consider that the CMA's provisional analysis with respect to the exercise of its discretion to refer the PCA market is correct?***

2.4. Yes. YBS has noted some positive developments in the market, including the growth in competitive rivalry among market players, certain improvements with respect to pricing transparency and the introduction of a new account switching service, which should go some way in addressing the issues noted by the CMA. YBS recognises, however, that there are a number of deep-seated issues in the PCA market and the long list of prior market inquiries and investigations by competition and regulatory authorities – with their associated recommendations and remedies - is testament to the difficulty of achieving material reform in this market. YBS therefore, supports the MIR referral.

***Do you consider that the features which the CMA has identified that may prevent, restrict or distort competition, are capable of being effectively and comprehensively remedied by UIIs (undertakings in lieu of an MIR) given by the banks?***

2.5. No. YBS does not believe that the main structural issues facing the PCA market are capable of being remedied by the major banks, in lieu of an MIR, as many of the changes required are fundamentally not in their interest and would take too long to resolve through natural market forces – both on the supply and demand side.

***Do you consider that a potential solution to any competition concerns identified may need to consider alterations to the structure of the markets in addition to (or in place of) remedies focused on increasing customer engagement?***

2.6. YBS has a number of proposed remedies, which it believes are required to address the fundamental structural issues in the PCA market.

- **A structural review of the banking sector:** YBS believes that serious consideration should be given to significant market interventions in banking sector to create pre-conditions for effective competition. This may be judged to require further forced divestitures of the 'Big 5' (the Big 4 plus Santander). It should be noted that Lloyds Banking Group still has a PCA market share of over 25 per cent, despite the TSB divestment. YBS holds the view that the Big 5 continue to hold an overly dominant market position, with younger customers effectively "sleepwalking" into opening an account with the Big 5 and, as the CMA has identified, customer satisfaction towards these banks is low. YBS notes such structural changes would have a positive impact on consumers and would highlight the way TSB is gaining share from the incumbents by providing better value and a decent service proposition. Further measures of this type should be seriously considered.
- **Require an overhaul of overdraft pricing:** As set out above, this is an area where YBS believes customers risk not getting good value from their account and the issue of cross-subsidisation by major banks is of concern. Potential remedies could include mandating that overdraft pricing must be based on interest only and not fees, avoiding a small number of customers providing the greater proportion of the revenue for providers. An alternative would be to force banks to show a very visible APR for planned and unplanned overdraft lending (to include fees) which currently they do not do. This would bring PCAs into line with other forms of consumer credit regulation. In the meantime, YBS Group is reviewing its own charging model for the product offered under the N&P brand currently to ensure we adopt these principles to provide best value to customers on a voluntary basis. We believe this is preferable to waiting for the outcomes of the MIR, which we hope will in time bring the fundamental reform of fees and charges which is necessary across the banking sector.
- **Mandate account number portability:** Such a measure would reduce the risk to customers of switching (which is often acts a significant behavioural barrier to switching) and reduce the dead cost to industry of moving customers' payment instructions from one bank to another. YBS notes that the market has not seen a material uplift in switching since the introduction of the Current Account Switch Service (CASS), and a proportion of the uplift that was evident in the early days is likely to be due to customers switching between Lloyds and TSB as a result of the sort-code-

based approach of the TSB separation which led to a number of customers being separated from their local branch. CASS was proposed and implemented after the plc banks which dominate the current account market made the case it would give a more predictable switch, but there are outstanding problems. Forwarding of payments only lasts a year, after which time they are bounced. A significant emerging issue is growth of online based services linked to account number, which unlike standing orders and direct debits dealt with by the switching process, require the customer to manually amend these details. These obstacles to customers are substantial, and it is why the half-way house of a switching service is clearly sub-optimal when compared to the introduction of account number portability. Portability reduced barriers to switch considerably in the mobile phone industry and there's every reason to think it could do the same for banking, quickening the pace of changes in pricing model which will underlie a more competitive market.

- **Mandate free ATM access for all customers with a UK debit card to all bank-owned or bank-controlled ATMs:** This would both (a) support those customers who are financially disadvantaged and (b) remove barriers to entry. From YBS's perspective this removes the longer-term risk that banks use ATMs as a way to increase the cost of access to banking for smaller competitors who do not have a large, established ATM network. Through the LINK system the banks earn their costs back anyway so this would simply remove a future barrier to competition.

### 3. Conclusion

- 3.1. YBS welcomes the CMA's provisional decision that a market investigation reference (MIR) is made in relation to both PCAs and retail banking for SMEs. YBS looks forward to engaging with the CMA during the consultation process and the potential future MIR.