



# Our response to the CMA's final report on its investigation into competition in the retail banking market

November 2016



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We have carried out this work in the context of the existing UK and EU regulatory framework. We will keep it under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework, including as a result of any negotiations following the UK's vote to leave the EU.

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## Abbreviations used in this paper

<b>BBA</b>	British Bankers Association
<b>BCA</b>	Business current account
<b>BEIS</b>	Department for Business, Energy and Industrial Strategy
<b>CASS</b>	Current Account Switch Service
<b>CCA</b>	Consumer Credit Act 1974
<b>CCD</b>	Consumer Credit Directive
<b>CMA</b>	Competition and Markets Authority
<b>FCA</b>	Financial Conduct Authority
<b>FIIC</b>	Free-If-In-Credit
<b>FSBRA</b>	Financial Services (Banking Reform) Act 2013
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>HMT</b>	Her Majesty's Treasury
<b>IRB</b>	internal ratings based model
<b>MMC</b>	Monthly maximum charge
<b>OFT</b>	Office of Fair Trading
<b>PAD</b>	Payment Accounts Directive
<b>PCA</b>	Personal current account
<b>PRA</b>	Prudential Regulation Authority
<b>PSD</b>	Payment Services Directive
<b>PSD2</b>	Second Payment Services Directive

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<b>PSR</b>	Payment Systems Regulator
<b>RCT</b>	Randomised Controlled Trial
<b>SBEEA</b>	Small Business, Enterprise and Employment Act 2015
<b>SME</b>	Small and medium-sized enterprise

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# 1. Overview

## Introduction

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- 1.1** On 9 August 2016, the Competition and Markets Authority (CMA) published its final report into the effectiveness of competition in the retail banking market.<sup>1</sup> The report sets out a package of remedies to address the problems it found. The CMA is taking forward many of these remedies itself. However, the CMA also makes recommendations to the Financial Conduct Authority (FCA) in relation to others.
- 1.2** As context, this response provides an overview of the retail banking market and ongoing changes that are likely to affect it. It then summarises the CMA's findings and remedies, including its recommendations to the FCA, and sets out the actions we propose to take as a result.<sup>2</sup> Lastly, it highlights broader areas where we intend to undertake further work, including high-cost credit and the wider retail banking competitive landscape.

## Overview of the retail banking market

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- 1.3** The FCA is the conduct regulator for financial services firms and markets in the UK, including retail banking. Banks provide important services to a significant proportion of UK consumers – both individuals and businesses. Notably, 97% of adults in the UK have a personal current account (PCA).<sup>3</sup>
- 1.4** The retail banking market is changing – a new wave of alternative providers is entering parts of the industry traditionally served by banks in areas such as payment services and lending. Consumers are interacting with their banking providers in new ways with particular growth in uptake of mobile and digital banking.
- 1.5** There are also a number of ongoing regulatory initiatives that have the potential to change the competitive dynamics of the sector. These include ring-fencing of retail banking functions, various European initiatives, other FCA market studies, and the work of the Payment Systems Regulator (PSR) and the Prudential Regulation Authority (PRA). An overview of the retail banking market is set out in Chapter 2.

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<sup>1</sup> The CMA's final report can be accessed here: <https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf>.

<sup>2</sup> To the extent that the recommendations in the CMA's final report constitute 'section 140B' advice within the meaning of section 140B of the Financial Services and Markets Act 2000 (FSMA), this response discharges our duty to publish a response to such advice within 90 days after the day on which we received it.

<sup>3</sup> See page iii of the CMA's final report.

## The CMA's retail banking investigation

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- 1.6** The CMA's market investigation into the supply of retail banking services was launched on 6 November 2014. The investigation considered the supply of PCAs, including overdrafts<sup>4</sup> and in relation to small and medium-sized enterprises (SMEs), business current accounts (BCAs) and lending products.<sup>5</sup>
- 1.7** In August 2016, the CMA published its final findings and remedies. It found that:
- 'The older and larger banks, which still account for the large majority of the retail banking market, do not have to work hard enough to win and retain customers and it is difficult for new and smaller providers to attract customers. These failings are having a pronounced effect on certain groups of customers, particularly overdraft users and smaller businesses.'*<sup>6</sup>
- 1.8** To address these problems, the CMA outlined a package of remedies that aim to promote more effective competition through increased consumer engagement and activity. The remedies include 'foundation measures', including the introduction of an Open Banking standard to share data, as well as other measures specifically directed to certain aspects of the market: current account switching, PCA overdrafts, and the needs of small businesses. The CMA intends to implement some remedies itself and makes recommendations to other bodies, including the FCA, to take others forward. An overview of the CMA's retail banking market investigation is set out in Chapter 3.

## The CMA's recommendations to the FCA: How we will act

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- 1.9** Our response reflects the fact that our statutory objectives, duties and regulatory initiatives give us a wider remit than the scope of the CMA's retail banking investigation.
- 1.10** In our work, we will act to advance our statutory objectives. We will apply our usual processes and apply the relevant tests and procedures in making any rules, such as undertaking consultation, ensuring proportionality and complying with the wider domestic and European legal framework. We will also take into account the implications and fit of this work with other ongoing related work, including the work of the CMA to implement other parts of their remedy package. Lastly, recognising that innovation and Open Banking may change the way that banks engage with their customers, we will maintain a forward looking approach across this work.
- 1.11** The action we intend to take as a result of the CMA's recommendations to us is summarised below. Full details are set out in Chapter 4.

### Promoting innovation

- The FCA has an existing focus on supporting innovative firms and approaches as a way of promoting competition in the interests of consumers. We welcome the introduction of the Open Banking standard, which we expect will directly support the rise of more innovative firms, products and services.

<sup>4</sup> PCA services, for the purposes of the CMA's investigation did not include: (a) an account in which money is held on deposit in a currency other than the official currency of the UK; or (b) a current account mortgage.

<sup>5</sup> Insurance, merchant acquiring, hedging and foreign exchange were all out of scope of the CMA's market investigation.

<sup>6</sup> See page 1 of the CMA's final report summary: [www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/544942/overview-of-the-banking-retail-market.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/544942/overview-of-the-banking-retail-market.pdf).



- As per the CMA's recommendation, we will act as an observer on the steering group of the Implementation Entity tasked with establishing the Open Banking standard.
- We will use our observer role in the group to clarify our expectation around the delivery of a solution that works for a broader set of accounts than current accounts, providing a way for firms to comply with the second Payment Services Directive (PSD2) and meet the expectations we set for such solutions in our credit card and cash savings market studies.

### Improving service

- We will take action in response to the CMA's recommendation to the FCA in relation to the publication of service quality information to consumers. Drawing attention to service quality could not only help consumers, but will also provide incentives to firms to improve their performance, products and service.
- The service quality information made available must be useful and meaningful to consumers and be communicated in a simple and engaging way. We expect intermediaries, including new innovative services, to have a key role to play.
- We will establish a temporary stakeholder expert group to inform our consideration of what service quality data and information could be made available; we will then test these measures with consumers using a variety of research techniques.
- We expect the first meeting of this group to take place this year and, if warranted, we would bring forward proposals for consultation by the end of 2017. At this point, we envisage that any rules would take effect at the same time as the CMA's order on the publication of core service quality data.

### Prompting increased customer engagement

- We will take action in response to the CMA's recommendation to us regarding prompts. We are supportive of research and testing to ensure the prompts meet their intended outcome.
- Prompts are dedicated messages sent to consumers and can be periodic or triggered by certain events. They encourage or 'prompt' changes in attitudes or behaviours specifically in relation to shopping around or reviewing their accounts.
- We will undertake research to design prompts that are effective in engaging consumers and prompting them to consider their banking arrangements. Such prompts may also increase transparency around the cost of current accounts, helping consumers understand their account usage, fees and charges.

- We are mindful that prompts are likely to be more effective once other elements of the CMA's remedy package are in place, in particular the Open Banking standard. We are considering how to take this into account in our research.
- Our research and testing will be taken forward through the course of 2017. It is unlikely that any proposals for consultation, if warranted, would be made before 2018.

### Improved transparency for overdraft users

- The CMA's recommendations to the FCA in relation to overdrafts form part of a wider package of measures that the CMA is itself putting in place, seeking to promote more effective competition for overdraft users.
- As part of this, we will undertake research and testing to design alerts that are effective in increasing personal banking customers' awareness of their overdraft usage and helping them manage it. Our previous research has demonstrated that such alerts can be effective in prompting consumers to take action to avoid fees and charges. This work will be carried out alongside the research into prompts (see above).
- The CMA will require firms to set and publicise the monthly maximum charge (MMC) consumers could incur from use of an unarranged overdraft. We will review the effectiveness of this measure once it has been in place long enough to measure its impact – expected to be late 2018 at the earliest. In order to help us do this, we will begin collecting baseline data in 2017.
- During the course of 2017, we will look at banks' account opening procedures to see whether improvements could be made to make consumers more aware of the features and costs of overdrafts.
- We will consider whether additional measures are required to increase the availability of overdraft eligibility tools following the introduction of the Open Banking standard. As part of this, we will also take into account cross-sector work currently underway to develop improved quotation search tools.<sup>7</sup>
- In addition and as noted in the next section, we will undertake additional work on high-cost credit beyond the scope of the CMA's recommendations to us.

### Delivering a competitive market for SMEs

- The FCA is committed to promoting competition in the interest of all consumers, including SMEs.
- The FCA's actions in relation to the publication of service quality information and prompts will cover both personal and business banking customers.

<sup>7</sup> See PS16/15 at [www.fca.org.uk/publication/policy/ps16-15.pdf](http://www.fca.org.uk/publication/policy/ps16-15.pdf).

- As recommended by the CMA, we will attend the British Bankers Association (BBA) convened industry group tasked with standardising BCA opening procedures as an observer.

### Potential future work for FCA

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- 1.12** The FCA's role and remit in relation to retail banking goes beyond that covered within the scope of the CMA's investigation. While we are mindful of the initiatives already underway in this space, and its changing nature<sup>8</sup>, the importance of this sector to both personal banking customers and businesses means it is vital we continue to take an active role in ensuring consumers are adequately protected and that competition works effectively in all areas of retail banking.
- 1.13** There are two areas where we consider that further work will be necessary to better understand the risks to our objectives we see in this sector: high-cost credit, and the wider retail banking competitive landscape.
- 1.14** As part of future work on high-cost credit, we intend to examine overdrafts (arranged and unarranged) in the context of the wider consumer credit market and in comparison to other products. We will invite views and evidence in a separate section of the Call for Input on the high-cost short-term credit (HCSTC) price cap review, which will be published later this month. We discuss this further in Chapter 5. The views and evidence we gather will help inform a decision about what work we should undertake in this area in future.
- 1.15** In relation to the wider retail banking competitive landscape, we recognise that its multi-faceted nature means there may be value in looking at this sector more holistically. In particular, we intend to undertake further work to better understand how firms' actions in one market may affect outcomes in another and how conduct and competition are affected by the links between different parts of the business model. Part of this will include considering the impact of Free-If-In-Credit (FIIC) banking more broadly than was within scope of the CMA's investigation. Relevant issues for the FCA also include the drivers of consumers holding multiple products with one provider and the impact of innovation in this sector, including the increasing role of non-banks.
- 1.16** Our Business Plan for the year ahead will indicate the substantive work that we decide to undertake. Further details are set out in Chapter 5.

### Next steps

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- 1.17** We will take forward the actions set out in this document. Those wishing to express an interest in participating in the research outlined should contact [retailbanking@fca.org.uk](mailto:retailbanking@fca.org.uk).

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<sup>8</sup> See paragraphs 2.5 onwards.

## 2. Overview of the retail banking market

In this chapter, we provide an overview of the retail banking market, including the FCA's role, the size and importance of the sector to consumers, and how it is changing – including initiatives that are underway and likely to affect it.

### The FCA's role and objectives

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- 2.1** The FCA is the conduct regulator for 56,000 financial services firms and financial markets in the UK, including retail banking. Our strategic objective is to make financial markets work well. We have three operational objectives:
- to secure an appropriate degree of protection for consumers<sup>9</sup>
  - to protect and enhance the integrity of the UK financial system, and
  - to promote effective competition in the interests of consumers
- 2.2** The FCA regulates the conduct of a wide range of financial services firms, including deposit-takers such as banks and building societies. It is also the conduct regulator for wider activities in the financial services sector, including consumer credit and mortgages and the regulator for payment institutions and e-money institutions. The FCA is also the prudential regulator for some financial services firms while the PRA is responsible for the prudential regulation of banks, building societies, credit unions, and major investment firms.

### The importance of retail banking

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- 2.3** Currently, banks provide important services to a significant proportion of UK consumers:
- 97% of adults in the UK have a PCA – this is often the first financial product a customer owns. There are around 70 million active PCAs in the UK and PCAs generated revenues of approximately £8.7 billion in 2014.

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<sup>9</sup> The term 'consumer' in our objectives refers to any person who uses, has used, or may use a regulated financial service. This includes individuals acting in a personal capacity, corporates acting for business purposes, and a range of other types of consumer. In this document, we use the term 'personal banking customers' to refer to consumers acting in a personal capacity, and 'business banking customers' to refer to those acting for business purposes.

- In addition, in 2014 there were over 5 million SMEs, accounting for 99.9% of all UK businesses. There were around 5.5 million BCAs in the same year, which generated approximately £2.7 billion in revenues.<sup>10</sup>

**2.4** Consumers also hold a variety of other financial services products, many of which are also provided by banks, and often alongside a current account. For example:

- In 2014, 48% of SMEs had credit cards, 43% had overdraft facilities, and 18% had held a loan. Around 90% of SMEs went to their main bank for overdrafts, general-purpose business loans and credit cards.<sup>11</sup>
- 93% of adults in the UK have a cash savings account; approximately £700bn is held in cash savings accounts.<sup>12</sup> The CMA found that 60% of instant access savings account customers have a PCA with the same bank.<sup>13</sup>
- There are currently around 30 million credit cardholders in the UK, meaning approximately 60% of the UK adult population owns at least one credit card.<sup>14</sup> The CMA found that 40% of credit card customers have a PCA with the same bank.<sup>15</sup>

### The changing face of retail banking

**2.5** The nature of banking is changing, with new alternative providers entering parts of the market traditionally served by banks.

**2.6** FinTechs and existing providers are offering new services that compete with the traditional retail banking business model. We have seen an increase in these services in the payments space, and the emergence of e-money accounts, and services which allow customers to see an aggregated view of their accounts at different banks. Competition in this sector is only likely to accelerate in the future with the changes brought by the CMA's Open Banking Remedy and PSD2, which will enable new and innovative ways of using the information available in customers' accounts and making payments from these accounts.

**2.7** There has also been a growth in alternative lending – in particular to small businesses, with the emergence of peer-to-peer lending firms.

**2.8** Consumers are also changing the way they interact with their banking providers. Whereas bank branches have traditionally been the main distribution channel, increasing numbers of consumers are now using digital banking – mobile in particular. A recent report found that internet banking logins fell last year, from 4.4 million a day in 2014 to 4.3 million in 2015. However, mobile device apps were used 11 million times a day in 2015, up from 7 million a day in 2014. There was an average of 71 branch visits per branch per day in 2016, a 32% fall

<sup>10</sup> All statistics from page iii of the CMA's final report: [assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf](https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf).

<sup>11</sup> See page xx-xxv of the CMA's final report: [assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf](https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf).

<sup>12</sup> See page 6 of the final findings from the FCA's cash savings market study: [www.fca.org.uk/publication/market-studies/cash-savings-market-study-final-findings.pdf](http://www.fca.org.uk/publication/market-studies/cash-savings-market-study-final-findings.pdf).

<sup>13</sup> See B2 of the CMA's updated issues statement appendices: [assets.publishing.service.gov.uk/media/5576bdace5274a150e000015/Updated\\_issues\\_statement\\_appendices.pdf](https://assets.publishing.service.gov.uk/media/5576bdace5274a150e000015/Updated_issues_statement_appendices.pdf).

<sup>14</sup> See page 22 of the interim findings from the FCA's credit card market study: [www.fca.org.uk/publication/market-studies/ms14-6-2-ccms-interim-report.pdf](http://www.fca.org.uk/publication/market-studies/ms14-6-2-ccms-interim-report.pdf).

<sup>15</sup> See footnote 13.

since 2011.<sup>16</sup> In response to this trend, a number of online-only banks are planning to enter the market, or have recently joined.

### Initiatives already underway

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- 2.9** Competition in retail banking has been a longstanding concern and there is a significant amount of work underway which will affect providers of banking services and has the potential to change the competitive dynamics of the sector. Some of this has been initiated by the FCA, while other elements stem from the UK Government or European Union. This work is set out in the following paragraphs.
- 2.10 Ring-fencing of retail banking functions:** The Financial Services (Banking Reform) Act 2013 (FSBRA) will introduce a ring fence around 'core deposits' held by UK banks which have core deposits in excess of the threshold of £25 billion, with the aim of separating certain core banking services critical to individuals and SMEs, from other banking services. The PRA will play a key role in establishing the ring fence. In addition, the FCA will make rules relating to disclosure that entities which are not ring-fenced banks, but are part of a corporate group which includes a ring-fenced bank, should make to customers. The ring-fencing regime is scheduled to take effect from 1 January 2019.
- 2.11 European initiatives<sup>17</sup>:** We are working to implement the Payment Accounts Directive (PAD), under which we will finalise standardised terminology and definitions for certain features of PCAs and other payment accounts. This, along with clearer presentation of fees and charges to customers, should go some way in aiding transparency and comparability of account features in future. Likewise, the impact of a new right to a largely fee-free basic bank account has yet to be assessed. **PSD2** updates the current framework on payment services, extending its scope to payment services providers that were previously unregulated, and will improve the transparency and security of payment services. We also expect the Directive to have an important impact on competition for payment services and fostering innovation by allowing third parties access to customer account data (with consent) to provide information or initiate payments. This is an important factor in the work on an Open Banking standard. We expect Her Majesty's Treasury (HMT) to consult imminently on draft implementing regulations in order to ensure implementation by January 2018. Lastly, the Interchange Fee Regulation, which took effect from December 2015, imposes a cap on the level of interchange fees<sup>18</sup> for transactions based on consumer debit and credit cards of 0.2% and 0.3% respectively. It also bans the imposition of surcharges on transactions using these types of cards.
- 2.12 Other FCA market studies:** The FCA worked on a market study with the CMA on the provision of banking services to SMEs<sup>19</sup> and has undertaken work in relation to a number of other markets where banks operate. These include the cash savings market, the consumer credit market, the investment and corporate banking market, and the mortgage market. The **cash savings market study** was concluded in January 2015<sup>20</sup> and found that competition

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<sup>16</sup> All statistics taken from the BBA's The Way We Bank Now: Help at Hand report: [www.bba.org.uk/wp-content/uploads/2016/07/TWWBN3\\_WEB\\_Help-at-Hand-2016.pdf](http://www.bba.org.uk/wp-content/uploads/2016/07/TWWBN3_WEB_Help-at-Hand-2016.pdf).

<sup>17</sup> Firms must continue to abide by their obligations under UK law, including those derived from EU law, and continue with implementation plans for legislation that is still to come into effect.

<sup>18</sup> Interchange fees are fees paid by the merchant acquirer (the merchant's bank) to the card issuer (the cardholder's bank), as a percentage of each transaction made by the cardholder and form part of the package of fees that merchant acquirers charge to merchants.

<sup>19</sup> The joint FCA/CMA market study on SME banking can be accessed here: [assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report\\_final.pdf](https://assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report_final.pdf).

<sup>20</sup> The final findings from the FCA's cash savings market study can be accessed here: [www.fca.org.uk/publication/market-studies/cash-savings-market-study-final-findings.pdf](http://www.fca.org.uk/publication/market-studies/cash-savings-market-study-final-findings.pdf).

was not working well for many consumers. The FCA has confirmed several remedies and is considering further options to address the findings of this study. The final findings of the **credit card market study** were published in July 2016.<sup>21</sup> We found that competition is working fairly well for most consumers, though raised concerns about the scale of persistent debt, and consumers' control over their credit limits. The FCA is now taking forward policy interventions. These will address how firms should address large, persistent balances by ensuring consumers are taking control where possible, and are protected from excessive cost if they do not. We will publish a consultation paper in the next few months. We published the final findings and remedies from the **investment and corporate banking market study** in October 2016.<sup>22</sup> This found that while many clients feel well served by primary capital market services, there were also some areas where improvements could be made to improve competition. Later this year, we will launch a **mortgage market study** focused on consumers' ability to make effective choices, with a view to improving how competition works and delivers better outcomes for customers.

- 2.13 Ongoing work by the PSR:** In May 2015, the PSR launched two market reviews in relation to **the ownership and competitiveness of infrastructure provision in payment systems**<sup>23</sup> in the UK and in relation to **the supply of indirect access to payment systems**.<sup>24</sup> In relation to the former, the PSR published its final report in July 2016 and concluded that there is no effective competition for the provision of UK payments infrastructure for certain payment systems and is consulting on changes to remedy the current situation. The PSR found that the common ownership and control of payment systems and the infrastructure provider are likely to reduce the level of competition. In relation to the second, the PSR found that access to payment systems is improving and that competition in the supply of indirect access is generating increasingly positive results. We continue to act as an observer on the new **Payment Strategy Forum**<sup>25</sup>, and look forward to the publication of its final strategy later this month.
- 2.14 PRA work on capital requirements:** The PRA is conducting a review of its approach to internal ratings based (IRB) model approval for smaller firms. This is in response to the fact that firms that calculate residential mortgage risk weights using the IRB approach tend to have lower risk weights than firms which use the standardised approach, and this difference is exaggerated for lower loan to value mortgages. Furthermore, it is worth also noting that the risk weight calibration under the standardised approach is currently under review by the Basel Committee on Banking Supervision.
- 2.15 The New Bank Start-Up Unit:** This is a joint initiative from the FCA and PRA, giving information and support to newly authorised banks and those thinking of becoming a new bank in the United Kingdom. The Unit assists new banks to enter the market and through the early days of authorisation. It draws staff from the PRA and the FCA, with a standalone website, telephone number and email address. It provides new banks with the information and materials they need to navigate the process to become a new bank, as well as with focused supervisory resource during the early years of authorisation. The New Bank Start-up Unit provide named case officers for firms during the authorisation process at both the PRA and the FCA and a greater level of supervisory support during the new bank's early years after they have been authorised.

21 The final findings from the FCA's credit card market study can be accessed here: [www.fca.org.uk/publication/market-studies/ms14-6-3-credit-card-market-study-final-findings-report.pdf](http://www.fca.org.uk/publication/market-studies/ms14-6-3-credit-card-market-study-final-findings-report.pdf).

22 The final findings from the FCA's investment and corporate banking market study can be found here: [www.fca.org.uk/publication/market-studies/ms15-1-3-final-report.pdf](http://www.fca.org.uk/publication/market-studies/ms15-1-3-final-report.pdf)

23 For further information see [www.psr.org.uk/sites/default/files/media/PDF/MR1523-infrastructure-market-review-final-report.pdf](http://www.psr.org.uk/sites/default/files/media/PDF/MR1523-infrastructure-market-review-final-report.pdf).

24 For further information see [www.psr.org.uk/sites/default/files/media/PDF/MR1513-indirect-access-market-review-final-report.pdf](http://www.psr.org.uk/sites/default/files/media/PDF/MR1513-indirect-access-market-review-final-report.pdf).

25 For further information, see [www.psr.org.uk/psr-focus/payments-strategy-forum](http://www.psr.org.uk/psr-focus/payments-strategy-forum).

## 3. The CMA's retail banking investigation

In this chapter, we provide a summary of the CMA's investigation into the effectiveness of competition in retail banking, including its remedies and recommendations to us.

### The CMA's investigation

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- 3.1** In November 2014, the CMA launched a market investigation into the supply of retail banking services to PCA customers and to SMEs in the UK. This followed an update carried out by the CMA of a previous market study undertaken by the Office of Fair Trading (OFT) into the effectiveness of competition in the PCA market<sup>26</sup> and a joint FCA and OFT market study into the supply of banking services to SMEs.<sup>27</sup>
- 3.2** Within scope of the CMA's market investigation was the supply of PCAs, including overdrafts. In relation to SMEs, the CMA's scope included BCAs and lending products.
- 3.3** At the outset, the CMA set out three broad areas in which it had concerns that retail banking may not be working well for customers. The CMA considered:
- whether there is a weak customer response due to lack of engagement, and/or whether barriers to searching and switching are reducing incentives for banks to innovate or to compete on price or quality
  - whether there are barriers to entry and expansion constraining the ability of banks to enter or expand, and
  - whether the level of concentration is having an adverse effect on customers

### The CMA's findings

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- 3.4** The CMA published the final report arising from its market investigation in August 2016. In its report, it set out that it had found many positive developments in the market, including the entry of new banks, the adoption of new business models, specialist product offerings, and opportunities created by new technologies (such as digital only banks). The CMA also commented on the wide adoption and growth of mobile banking, as well as the availability of new types of payment services.

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<sup>26</sup> The CMA's final report can be accessed here: [assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf](https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf).

<sup>27</sup> The joint FCA/CMA market study on SME banking can be accessed here: [assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report\\_final.pdf](https://assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report_final.pdf).



**3.5** However, despite these developments the CMA concluded that:

*'Older and larger banks, which still account for the large majority of the retail banking market, do not have to work hard enough to win and retain customers and it is difficult for new and smaller providers to attract customers. These failings are having a pronounced effect on certain groups of customers, particularly overdraft users and smaller businesses.'*<sup>28</sup>

**3.6** In particular, the CMA highlighted the following main issues:

- Personal and business current accounts have complex charging structures and customers generally do not know much about the service quality and charges provided by other banks. It is therefore difficult for consumers to know if they can get better value and services from another product or provider.
- Personal and business current accounts are open-ended and there are no regular trigger points to prompt consumers to consider whether there are better current account deals elsewhere.
- The Current Account Switch Service (CASS) makes current account switching easy; however, the service is not well known, and consumer confidence in it could be improved. The processes for small businesses opening an account can also be onerous and lengthy.
- Overdraft charging structures are complicated, making comparisons between providers difficult. Consumers are also concerned about not getting the same overdraft from their new bank if they switch. The CMA also found that consumers often underestimate their overdraft use.
- Over half of start-up businesses open their current account with the same provider as the business owner has their personal account. The CMA reported that '90% of small businesses get their business loans from their main bank' and it is hard for small businesses to determine the best lender for them.
- The CMA also looked at whether the FIIC banking model makes it less likely that consumers will switch and did not find this to be the case. They also looked at whether it was low-income customers who were paying more under the FIIC model and, again, found that this was not the case.

### The CMA's remedies

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**3.7** To address the problems it found, the CMA outlined a set of remedies. These remedies build on those introduced in past reviews and on recent positive developments in the market (such as those outlined at paragraph 2.9). The CMA sets out that these remedies will:

*'help customers to find and access better value services and enable them to take more control of their finances. This will also enable new entrants and smaller providers to compete on a more level playing field and increase the opportunities for new business models to develop.'*<sup>29</sup>

<sup>28</sup> See page 1 of the CMA's final report summary: [www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/544942/overview-of-the-banking-retail-market.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/544942/overview-of-the-banking-retail-market.pdf).

<sup>29</sup> See footnote 25.

**3.8** The CMA's remedies package is grouped into four elements:

- 'Foundation remedies' to make PCA and SME banking markets work better for customers – these remedies comprise the introduction of an Open Banking standard to share data, the publication of service quality data, and the introduction of prompts for customers to consider their banking arrangements.
- A current account switching package, which sets out proposed measures to improve the process of switching current accounts and promote greater customer awareness of and confidence in the process.
- Additional remedies targeted at PCA overdraft customers, which include further measures to help customers understand and manage their overdrafts better and to reduce the detriment arising from overdraft usage.
- Additional SME remedies, including measures to make it easier for SMEs to shop around and compare products with increased transparency of prices and eligibility of lending products, as well as improvements to BCA opening procedures.

**3.9** The CMA will implement some remedies itself, using orders and seeking undertakings. However, it also makes recommendations to other bodies, including the FCA, to take forward implementation of others.

### The CMA's recommendations to the FCA

**3.10** The CMA's recommendations to the FCA are set out in the table below:

<b>Innovation</b>	The CMA suggests that the FCA has, at least, observer status on the steering group of the Implementation Entity responsible for delivering the Open Banking standard, for the benefit of both personal banking customers and SMEs.
<b>Service quality</b>	The CMA recommends that the FCA requires PCA and BCA providers to publish and make available to others, including as open data, additional <sup>31</sup> objective measures of service performance encompassing their PCA, BCA and SME lending products, and principal sales/delivery channels.
<b>Prompts</b>	The CMA recommends that the FCA: <ul style="list-style-type: none"> <li>• undertake a research programme, including randomised control trials (RCTs), in conjunction with a selection of PCA and BCA providers to identify those prompts most likely to increase customer awareness of the potential benefits of switching and prompt customers to consider their banking arrangements</li> <li>• use its rule-making powers (subject to the results of the research programme) to implement a series of prompts to be communicated to customers</li> <li>• consider the extent to which the content and presentation of the prompts should be standardised in order that a consistent message is delivered to customers by all providers; and</li> <li>• monitor the effectiveness of these prompts, and, as and when necessary, redesign the prompts to reflect market and regulatory developments</li> </ul>

<sup>30</sup> These objective measures of service performance are additional to those subjective measures that the CMA will require firms to publish (using its order-making powers).

<p><b>Overdrafts</b></p>	<p><b>Overdraft alerts:</b> The CMA recommends that the FCA identifies, researches, tests and implements (as appropriate) measures to increase customers' engagement with their overdraft usage and charges. As part of this programme of work, the CMA recommends that the FCA consider the following:</p> <ul style="list-style-type: none"> <li>• How providers may be able to enhance the effectiveness of overdraft alerts: for example, by changing the type, medium, content, timeliness and frequency of the alerts offered, and/or their auto-enrolment policies.</li> <li>• The grace periods operated by providers and the timings communicated in alerts.</li> <li>• The set of alerts customers should be automatically enrolled into by providers</li> <li>• How to articulate the concept of available funds to customers: in particular, whether this is inclusive or exclusive of an arranged overdraft.</li> </ul>
	<p><b>Assessing the effectiveness of the MMC:</b> The CMA recommends that the FCA undertakes work to assess the ongoing effectiveness of the MMC and considers whether measures (such as the introduction of rules if appropriate) could be taken to further enhance its effectiveness.</p>
	<p><b>Account opening procedures:</b> The CMA recommends that the FCA looks at ways for providers to engage customers more, during the account opening process, in considering overdraft features and their potential relevance and impact.</p>
	<p><b>Overdraft eligibility tools:</b> The CMA recommends that, following the introduction of the Open Banking standard, the FCA considers requiring providers to offer online tools that indicate whether a prospective customer may be eligible for an overdraft.</p>
<p><b>SMEs</b></p>	<p>The CMA recommends that the BBA-convened industry group tasked with standardising opening procedures for BCAs invite the FCA to attend its meetings as an observer and recommends that the FCA attends such meetings.</p>

## 4.

# The CMA's recommendations to the FCA: how we will act

In this section, we set out the action we will take in response to the CMA's recommendations to us.

### Overview: how we will act

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- 4.1** The actions we propose to take in response to the CMA's recommendations to us are set out later in this section. Here we set out some broad principles of our approach, which apply to all the recommendations.
- 4.2** Our response reflects the fact that our statutory objectives, duties and regulatory initiatives give us a wider remit than the scope of the CMA's retail banking investigation.
- 4.3** In our work, we will act to advance our statutory objectives – in particular, our consumer protection and competition objectives. We will apply our usual processes, including obtaining and assessing evidence<sup>31</sup>, applying the relevant tests and procedures in making any rules, such as undertaking consultation, and complying with the domestic and European legal framework.
- 4.4** We will also take into account the implications and fit of this work with other ongoing related work. This includes the work of the CMA to implement other parts of their remedy package, in particular Open Banking, and our own work to improve competition in the cash savings market; implementation of PSD2 and the PAD; the review of the Consumer Credit Act 1974 (CCA) provisions retained when consumer credit regulation was transferred to the FCA in April 2016<sup>32</sup>; the Innovation Hub and Sandbox work on innovative products and services; and access for vulnerable customers.
- 4.5** Lastly, recognising that innovation and Open Banking may change the way that banks engage with their customers, we will maintain a forward looking approach across this work. For example, when shaping our plans to research new prompts and alerts and our work on establishing a set of service quality indicators, we will need to consider the emergence of new intermediaries and new methods of comparison to future-proof our proposals.
- 4.6** We are keen to hear from and work with innovators to ensure we do not create barriers to future innovation in this sector and, where possible, enable it.

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<sup>31</sup> To the extent that it is possible, we will seek to make use of evidence already gathered by the CMA.

<sup>32</sup> Full details at [www.fca.org.uk/publication/call-for-input/call-for-input-review-retained-provisions-consumer-credit-act.pdf](http://www.fca.org.uk/publication/call-for-input/call-for-input-review-retained-provisions-consumer-credit-act.pdf).

## Promoting innovation

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**4.7** The FCA has a focus on supporting innovative firms and approaches as a way of promoting competition in the interests of consumers. Through Project Innovate<sup>33</sup>, we assist businesses in developing and testing innovative products, services, business models and delivery mechanisms. In the retail banking market, we have supported firms that want to help people access bank accounts and manage their savings more effectively. Retail banking services can also be found in our Regulatory Sandbox<sup>34</sup>: a safe space for firms to test new ideas without immediately incurring all of the normal regulatory consequences of engaging in the activities in question.

**4.8** Alongside many other participants and commentators, we see potential for the CMA's remedies package to promote innovation from banks and third parties, increasing competition in the interests of consumers. In particular, we expect that the increased access to data provided by the CMA's open banking foundation remedy (with measures due for completion in March 2017 and January 2018) will directly support the rise of more innovative firms, products and services.

### *Our approach*

**4.9** As suggested by the CMA, we will act as an observer on the steering group of the Implementation Entity tasked with establishing the Open Banking standard. The FCA previously attended the Open Banking Working Group, brought together by HMT, to explore how data could be used to help people transact, save, borrow, lend and invest their money.

**4.10** There are many similarities between the 'read and write functionality', which the CMA will require under the Open Banking Remedy, and the obligations under PSD2 to allow third parties to access account information and initiate payments on users' behalf (with consent). We will therefore use our observer role in the steering group to emphasise the need for the Open Banking standard to be consistent with the requirements of PSD2 if firms intend to use it to meet these obligations.

**4.11** In addition, we will also use our role to encourage the Implementation Entity to deliver a solution that works for a broader set of accounts than those covered by the CMA's remedy. PSD2's requirements in relation to third-party access extend beyond the CMA's focus on current accounts. In our view, they can apply to e-money accounts, flexible savings accounts, credit card accounts and current account mortgages.<sup>35</sup> We have conveyed similar views already in our credit card and cash savings market studies, as well as in relation to initiatives in other sectors. We see the introduction of the Open Banking standard as an opportunity for industry to provide a single way of accessing the full range of these accounts. A unitary standard for all products would reduce the risk that fragmentation could undermine the creation of a true Open Banking framework, and would achieve the full potential of PSD2, supporting third parties in offering a broad range of services across a wider range of products, for the benefit of all consumers.

**4.12** Given the FCA's broader objectives to promote market integrity, consumer protection and competition in the interests of consumers, we will also use our observer role in the steering group to emphasise the following:

- Our support for the Implementation Entity's focus, to date, on being transparent and inclusive for interested stakeholders, including 'challenger' banks, technology firms and representatives of consumers.

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<sup>33</sup> For further information, see: [www.fca.org.uk/firms/project-innovate-innovation-hub](http://www.fca.org.uk/firms/project-innovate-innovation-hub).

<sup>34</sup> For further information see: [www.fca.org.uk/firms/project-innovate-innovation-hub/regulatory-sandbox](http://www.fca.org.uk/firms/project-innovate-innovation-hub/regulatory-sandbox).

<sup>35</sup> See Q16 of Chapter 15 of the FCA's Perimeter Guidance Manual [www.handbook.fca.org.uk/handbook/PERG/](http://www.handbook.fca.org.uk/handbook/PERG/).

- The importance of security and safeguards to mitigate the risk that cyber attacks and fraud could affect consumers and the financial markets.
- The need for the final product to be accessible to third parties, to meet their needs and to evolve as these needs change. The Implementation Entity should understand how third parties might use their access, and ensure that they are able to do so. This is imperative if consumers are to be able to benefit from innovative services.

### Improving service

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- 4.13** We will take action in response to the CMA's recommendation to the FCA on the publication of service quality information to consumers. We recognise that transparency remedies, such as this, can be an effective regulatory tool. We already publish data on complaints handling<sup>36</sup> and are currently running a trial in relation to the publication of interest rate information on certain cash savings accounts.<sup>37</sup> We will also be piloting the publication of a scorecard on the value of a small number of retail general insurance products.<sup>38</sup> It is important that firms compete to offer high-quality products and good customer service, as well as competing on price, and drawing attention to this information can provide firms with incentives to act to improve their performance and the products and service they offer.
- 4.14** Our aim, in taking action in relation to the publication of service quality information, is that the information given facilitates consumer choice on the basis of service – a product feature that can often be difficult to judge. We recognise that comparable and easily accessible data on the service and value offered by providers should help consumers be better informed when making decisions about which current account best meets their needs. To this end, in taking action in response to this recommendation, we would be advancing our competition objective.
- 4.15** We also expect that publication of this information could actively engage consumers. In particular, we expect that intermediaries are likely to play a pivotal role in delivering service quality information to consumers in an engaging way. We are keen to encourage the development of new services offering innovative ways of engaging consumers with the value and service offered by current account providers, and which are able to recommend accounts based on an individual's preferences and account usage, going beyond current price comparison websites and media commentary.
- 4.16** Lastly, publication of this information should encourage banks to consider and improve their own standards, by understanding how they compare to others in the market. Publication of this additional consistent information could give providers incentives to compete actively to offer a good service to both existing and new customers, as well as competing on price.
- 4.17** For the reasons given above, we propose to take the actions set out in the following section in response to this recommendation.
- 4.18** The CMA has recommended that we require additional service information to be published for both personal and business current accounts. We will use a similar approach to develop proposals for both customer groups. However, we recognise that the information needed is likely to be different for the different users of these accounts.

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36 For further information, see: [www.fca.org.uk/firms/complaints-data](http://www.fca.org.uk/firms/complaints-data).

37 For further information, see: [www.fca.org.uk/publication/data/sunlight-april-2016.pdf](http://www.fca.org.uk/publication/data/sunlight-april-2016.pdf).

38 For further information, see: [www.fca.org.uk/publication/feedback/fs16-01.pdf](http://www.fca.org.uk/publication/feedback/fs16-01.pdf).

### ***Our approach***

- 4.19** The CMA will itself require firms to publish core service quality indicators (measured by an independent survey on terms agreed with the CMA) and has recommended that the FCA consider and then require firms to publish additional information on service quality. We will follow up on the CMA's recommendation to require banks to publish data that includes the availability of core services (e.g. interruptions to digital channels, card payments etc.)
- 4.20** Research in behavioural economics tells us that consumers can find multiple indicators difficult to compute.<sup>39</sup> Therefore, the additional information made available to consumers needs to be useful and meaningful, and communicated in a simple and engaging way. As set out earlier, we expect that commentators and comparison services, including innovative services accessing data via the Open Banking standard, are likely to play a key role.
- 4.21** We are aware that there are many individuals and organisations with knowledge of and views on what consumers value in products and providers, and we will form a temporary stakeholder expert group on service quality information for personal banking customers. This group will provide views to the FCA on the information that could be made available to these customers in order to help them evaluate the service they are likely to receive. It will also provide views on whether the information needs to be collected and presented in a consistent way to be usefully compared. In our view, forming this stakeholder expert group is the best and most efficient way to utilise this valuable experience and help inform our work.
- 4.22** The stakeholder expert group will build on the widespread existing evidence on this subject, including that collected by the CMA, and will consider information and data on aspects of service that is already collected and, in some cases, published.
- 4.23** Our approach for business banking customers will be similar, but will require us to establish a subset of the temporary stakeholder expert group with members that have particular knowledge of the SME market, reflecting their different needs compared to personal banking customers.
- 4.24** We envisage that the group will include a range of commentators, comparison service providers, FinTech firms, consumer and public and private sector organisations with expertise in consumer service. We will also engage with individual firms (banks and non-banks) that offer current accounts, as well as with relevant trade associations.
- 4.25** The initial output from the stakeholder expert group and engagement with firms and trade associations will inform our consideration of what service quality data and information could be provided to consumers and therefore included in the second strand of our work.
- 4.26** This second strand of our work will test these measures of service quality with consumers using a variety of research techniques. As well as traditional focus groups, we are also interested in engaging with providers, comparison websites, applications and innovative providers to consider whether there might be value in undertaking some 'live trials' or 'mock-ups' to better understand how intermediaries could use the additional information to provide consumers with engaging and holistic comparison information and/or recommendations on current accounts that meet their needs.

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<sup>39</sup> See, for example, 'Price Lab: An investigation of consumers' capabilities with complex products', which can be accessed here: [www.esri.ie/pubs/BKMNEXT306.pdf](http://www.esri.ie/pubs/BKMNEXT306.pdf).

### ***Timelines and indicative next steps***

- 4.27** We expect the stakeholder expert group to be set up by the end of 2016. We plan to complete the second phase of our research during the first half of 2017. If our research supports our making rules and issuing guidance in relation to service quality indicators, we aim to bring forward proposals for consultation by the end of 2017. At this stage, we envisage any rules that might result would come into effect at the same time as the CMA's order on core service quality data, expected in Q3 2018.

### **Prompting increased customer engagement**

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- 4.28** Over the past few years, the FCA has developed its understanding of behavioural biases and gained experience in using them to design interventions. We provided evidence in this regard to the CMA's investigation and, in particular, its proposals for 'prompts'.
- 4.29** Prompts are dedicated messages sent to consumers and can be periodic or triggered by certain events. They encourage or 'prompt' changes in attitudes or behaviours specifically in relation to shopping around or reviewing their accounts. Such prompts may also increase transparency around the cost of current accounts, helping consumers understand their account usage, fees and charges.
- 4.30** We will take action in response to the CMA's recommendation to the FCA regarding prompts (as set out in section 3). In particular, we are supportive of undertaking research to help ensure prompts meet their intended outcome.
- 4.31** Our work on behavioural biases and smarter consumer communications has clearly shown that communications can overwhelm, confuse, distract or even deter people from making effective choices if presented in a way with which people struggle to engage. In addition, it shows that one-size-fits-all information can often be insufficient to empower consumers to make informed decisions and that, in order to be effective, communications should be designed to meet the needs of their target audience.<sup>40</sup>
- 4.32** However, when done well, disclosure can drive better consumer outcomes, especially when crafted in a way that means consumers pay attention to it, have the capacity to interpret it, and are willing to incorporate it into their decision-making. For example, we found that putting the old price next to the new price on insurance renewal letters for home and motor insurance increased switching.<sup>41</sup>
- 4.33** We therefore believe there is benefit in research and testing to identify and design prompts. Our primary aim in taking forward this work is to engage consumers and prompt them to actively consider their banking arrangements. For example, the prompt could provide a quick and easy way to compare providers using their own transaction data and the newly available service quality information. In addition, we recognise that, over time, information provided to customers through prompts could also lead to broader changes in their attitudes and behaviours: for example, by increasing awareness of their account usage, the charges they incur and the benefits they may gain from switching. This could encourage more active account management and increased switching. In taking action in response to this recommendation, we would be advancing our competition and consumer protection objectives. For this reason, we propose to take the actions described in the following paragraphs.

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<sup>40</sup> See FCA DP15/5: Smarter consumer communications at [www.fca.org.uk/publication/discussion/dp15-05-smarter-consumer-communications.pdf](http://www.fca.org.uk/publication/discussion/dp15-05-smarter-consumer-communications.pdf).

<sup>41</sup> See OP12 Encouraging consumers to act at renewal at [www.fca.org.uk/publication/occasional-papers/occasional-paper-12.pdf](http://www.fca.org.uk/publication/occasional-papers/occasional-paper-12.pdf).



**4.34** Our approach will incorporate lessons we have learnt from previous work on communications intended to change customer behaviour: in particular, that simpler processes for switching, comparison and account management would likely maximise the effectiveness of such communications. It will also have regard to the potential for prompts to be more effective once other elements of the CMA's remedy package are in place: in particular, the Open Banking standard. Lastly, it will take account of the fact that some of the more longer-term changes we expect to result from this remedy may be difficult to measure in the relatively short time period over which we will undertake our research.

**4.35** The CMA has recommended that we research prompts that are effective for both personal banking customers and for SMEs. Our approach will be the same; however, due to the fact that different types of customer may respond to different prompts in different ways, we will consider the most effective prompts for different types of customers separately.

***Our approach***

**4.36** We will undertake a programme of work in order to identify those communications that are most effective in engaging customers and prompting them to consider their banking arrangements.

**4.37** The first stage of work, which is already underway, is focused on gathering information on firms' practices in this area, and collecting existing research and evidence on the sorts of prompts that are likely to be effective.

**4.38** The CMA has put forward several suggestions for prompts to research and test. These include periodic prompts, such as annual summaries and event-based prompts, which, for example, follow a material change in a key product feature or the closure of a customer's branch. We agree that many of the prompts the CMA chose not to recommend are unlikely to be effective or practical to implement.

**4.39** We have started to engage with a range of external stakeholders in order to inform our thinking. We will also take into account evidence from past research and trials we have undertaken and the academic literature. Where possible, we will rely on evidence that firms have already provided to the CMA, rather than requesting the same information from firms.

**4.40** As part of our thinking, we will consider how prompts could fit with the existing requirements and limitations set out in European legislation – in particular, PSD2, PAD and the Consumer Credit Directive (CCD), and the restrictions that the maximum harmonising provisions of the legislation impose.

**4.41** In the second stage of our work, we will take the set of prompts that we identify forward for further research and testing. This is likely to include consumer research and RCTs, as well as broader research and testing. We intend to use consumer research (for example, focus groups) to help us refine the prompts before they are tested. Although focus groups (and other consumer research methods) do not simulate a real-life environment, they can prove useful in gathering early evidence on how consumers might react to or interpret the information being communicated. RCTs and other research methods will then allow us to assess certain aspects of the effectiveness of a potential prompt in practice, providing direct evidence of their effects on consumer choices and decision making in a real-life environment.

**4.42** There is significant innovation underway within retail banking, particularly in how consumers engage with and manage their accounts. The introduction of the Open Banking standard, together with PSD2, is only likely to accelerate these changes. We are aware that the prompts we design and test must be 'future-proofed' and must work with, and make the best use

of, this new technology. As part of our research, we are also considering ways in which we can simulate and model how such prompts could work in the future, as well as exploring whether there are other more innovative ways of influencing consumer behaviour to encourage engagement and switching.

- 4.43** The CMA intends to make an Order requiring firms to cooperate with us in this research programme. Following discussions with firms, we will select the providers to participate. At this stage, we invite expressions of interest from firms who want to work with us, including those with ideas or proposals for how to forecast and anticipate future changes in the market as part of our research programme. We are also keen to engage with practitioners, in particular those working more broadly in FinTech, who can contribute to our thinking.
- 4.44** Again, our approach for SMEs follows the same principles, but will require us to design separate tailored research, reflecting the different needs of SMEs compared to personal banking customers.

#### ***Timelines and indicative next steps***

- 4.45** We have begun the first stage of our work and expect to complete our evidence gathering by the end of this year. We expect to take research and testing on prompts forward through the course of 2017. If supported by our research and testing, we will bring forward proposals for consultation; however, we are unlikely to do this before 2018.

#### **Improved transparency for overdraft users**

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- 4.46** The CMA's recommendations to the FCA in relation to overdrafts (as set out at the beginning of section 3) form part of a wider package of measures that the CMA itself is putting in place, seeking to promote more effective competition for overdraft users. Our proposed approach to the CMA's recommendations to us in relation to overdrafts is set out in the section below.
- 4.47** As we have set out, we have a broader set of objectives and remit than the CMA; we have an objective to protect consumers and our remit is much broader than current accounts and overdrafts. Given this, in addition to taking action in response to the CMA's recommendations to us, we will undertake additional work in relation to high-cost credit. Further details of this are set out in Chapter 5.

#### ***Our approach*** **Overdraft alerts**

- 4.48** Alerts are dedicated messages sent to consumers that communicate overdraft usage, triggered by overdraft-related events and provided in enough time to take action to avoid fees and charges. Existing alerts provided by firms include low balance and overdraft usage text message alerts.
- 4.49** We will take action in relation to the CMA's recommendations to us on overdraft alerts. Our aim in taking action in response to this recommendation is to research and identify alerts that increase personal banking customers' awareness of their overdraft usage and help them manage it. We would expect this to help these consumers save money by avoiding unnecessary overdraft charges, and, by increasing awareness of and responsiveness to overdraft fees and charges, should also put downward pressure on these charges. Taking forward this work would therefore advance both our consumer protection and competition objectives.

- 4.50** Our previous research has demonstrated that overdraft alerts can be effective in prompting consumers to take action to avoid fees and charges. In OP10<sup>42</sup>, we found that signing up to text alerts or mobile banking apps reduces the amount of unarranged overdraft charges incurred by 5% to 8%, and signing up to both services has an additional effect, resulting in a total reduction of 24%. This additional impact shows the benefit of combining a call to action (the alert) with the ability to take action quickly and easily (via the mobile banking app).
- 4.51** We propose to undertake a programme of research and testing to design effective alerts covering both arranged and unarranged overdrafts. This research and testing programme will follow the same steps as the research and testing programme for our prompts work (outlined at paragraph 4.28). It is therefore most efficient to take this work forward together as one programme.
- 4.52** As with prompts, the research will consider the timing, types, variations, combinations, channels and formats of overdraft alerts that are most effective and likely to encourage personal banking customers to engage with their overdrafts and help them make active choices about their usage. For alerts specifically, disclosure of grace periods and available funds will also be considered. Lastly, our research will consider the European Union law context and the constraints that it brings. The work will follow a similar timeline.
- 4.53** At the same time as making their recommendation to us in relation to overdraft alerts, the CMA will itself require firms to enrol all their personal banking customers automatically into an unarranged overdraft alert. They will also require firms to alert these customers to the opportunity to benefit from grace periods, during which they can take action to avoid or reduce all charges resulting from unarranged overdraft use. We are conscious of the need to use our resources efficiently, and also of the need to avoid imposing identical or parallel requirements on firms that are already subject to the CMA order.
- 4.54** If, following our research, we were to propose to implement our own requirements on firms in relation to overdraft alerts and grace periods, the CMA has indicated that it could revoke the requirements of its order. We will liaise with the CMA to ensure that we are not undertaking work unnecessarily and that, if we do propose to make rules in this area, the CMA will revoke their order at the same time.
- Review of the maximum monthly charge**
- 4.55** The CMA will implement the MMC remedy itself by making an order under the Enterprise Act 2002. The CMA report recommends that the FCA undertake work to assess the ongoing effectiveness of the MMC and consider whether measures (such as the introduction of rules if appropriate) could be taken to further enhance its effectiveness.
- 4.56** The CMA will itself keep the effectiveness of its Enterprise Act orders under review and will monitor compliance with them, including the order that will implement the MMC. The purpose of our review is to consider, once the MMC has been implemented, whether additional measures need to be taken to improve the MMC's effectiveness – in particular, in how it is communicated to consumers, and whether we should make rules in this area. An effective MMC should help consumers compare the cost of overdrafts and choose an account which meets their needs. Taking forward this work therefore primarily advances our competition objective.
- 4.57** For these reasons, we therefore propose to take action in response to this recommendation. In order to review the MMC and consider whether to make FCA rules in this area, we will need to collect baseline data. This will need to include data that covers the period before the

<sup>42</sup> See OP10: [www.fca.org.uk/publications/occasional-papers/occasional-paper-no-10-message-received-impact-annual-summaries-text](http://www.fca.org.uk/publications/occasional-papers/occasional-paper-no-10-message-received-impact-annual-summaries-text).

CMA's order comes into effect, as well as data once the MMC has been in effect for long enough to measure its impact. We expect the information we gather to include information on firms' current pricing structures and customers' current overdraft usage (so that we can better understand how the MMC has influenced charges and customer usage).

- 4.58** As above, we intend to review the MMC as soon as it has been in effect long enough to measure its impact. Given the CMA's Order is unlikely to take effect much before Q3 2017, our review is unlikely to take place until late 2018 at the earliest. However, evidence we gather as part of our wider work – for example, on high-cost credit products (see Chapter 5) – may result in us acting sooner.

#### **Account opening procedures**

- 4.59** The CMA recommends that the FCA looks at ways for providers to increase customer engagement during the account opening process with regard to considering overdraft features and their potential relevance and impact. This work aligns with our competition and our consumer protection objectives.

- 4.60** Over the course of 2017, we will look at current practice to establish how overdraft features are highlighted and to identify with industry and consumer representatives how effective improvements could be made. If needed, we would test any improvements with qualitative focused consumer research.

#### **Overdraft eligibility checkers**

- 4.61** We have previously committed to looking at promoting and facilitating the use of quotation search tools across all consumer credit markets.<sup>43</sup> These tools allow a consumer to see an indication of their eligibility and/or the potential price of a product before undertaking a full application for credit. We believe there is a real benefit in consumers being able to get an indication of their eligibility for specific products and the price they are likely to be offered if they apply (as well as other terms where these may vary). Sole reliance on eligibility or price can risk consumers being misled or applying for inappropriate products.

- 4.62** We will consider the CMA's recommendation on overdraft eligibility checkers following the introduction of the Open Banking standard (also expected to be in 2018) and in the light of the outcome of cross-sector work being undertaken by the industry to developing improved quotation search tools (announced in PS16/15<sup>44</sup> and the Credit Card Market Study Final Report<sup>45</sup>).

- 4.63** We consider that the Open Banking standard should facilitate shopping around and switching, particularly for overdraft users whom the CMA found faced additional barriers to switching due to the uncertainty surrounding acceptance and timing of an overdraft approval. Our work on prompts and alerts will also be looking at ways to encourage overdraft customers to shop around (among other objectives as set out above).

### **Delivering a more competitive market for SMEs**

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- 4.64** The CMA has outlined a package of remedies to improve competition in banking services for SMEs. The CMA's recommendations to the FCA on the publication of service quality information

<sup>43</sup> See CP15/33: [www.fca.org.uk/publication/consultation/cp-15-33-cma-remedies.pdf](http://www.fca.org.uk/publication/consultation/cp-15-33-cma-remedies.pdf).

<sup>44</sup> See PS16/15: [www.fca.org.uk/publications/policy-statements/ps16-15-feedback-cp15-33-consumer-credit-proposals-response-cma](http://www.fca.org.uk/publications/policy-statements/ps16-15-feedback-cp15-33-consumer-credit-proposals-response-cma).

<sup>45</sup> See MS14/6.3: [www.fca.org.uk/publication/market-studies/ms14-6-3-credit-card-market-study-final-findings-report.pdf](http://www.fca.org.uk/publication/market-studies/ms14-6-3-credit-card-market-study-final-findings-report.pdf).

and prompts cover both personal and business banking customers. These recommendations sit alongside the recommendation to participate in an industry initiative on BCA opening procedures. Together, these recommendations to the FCA put a focus on delivering a more competitive market for SMEs.

**4.65** Our competition objective is premised on the fact that competition can improve outcomes for SMEs, both independently and by complementing regulation. However, the FCA's understanding of SMEs as customers of financial services firms is not as well developed as for personal banking customers. This reflects our limited regulatory remit for some banking and lending activities in relation to SMEs.<sup>46</sup>

**4.66** The joint market study we undertook with the CMA on the SME banking market has helped develop our knowledge of SMEs.<sup>47</sup> In addition, we have seen recent evidence of poor outcomes experienced by SMEs. Our discussion paper<sup>48</sup> explored the suitability of our protections for SMEs, including the coverage provided by the Financial Ombudsman Service. We will publish feedback on this paper later this year.

**4.67** However, gaps in our knowledge remain and, as part of the action we take in response to the CMA's recommendations, we will look to improve understanding of the needs of SMEs, drawing on external expertise as necessary.

#### ***Our approach***

**4.68** As set out above, the CMA's recommendations to the FCA on the publication of service quality information and prompts cover both personal and business banking customers. The action we intend to take in response to these recommendations is set out at paragraph 4.13 onwards. In both cases, our research approach to developing proposals is similar for both personal and business customers. However, we recognise that these two groups of customers are different and will take account of this in our research.

**4.69** In addition to this work, we will attend the BBA-convened industry group tasked with standardising opening procedures for BCAs as an observer.

**4.70** We will also engage periodically with NESTA, the independent charity tasked by the CMA with the 'challenge prize' to enable the development and delivery of comparison services for SME lending.

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<sup>46</sup> For a detailed description of how our Handbook applies to SMEs, see Annex 4 of Our approach to SMEs as users of financial services, FCA, November 2015: [www.fca.org.uk/publications/discussion-papers/dp15-7-our-approach-smes-users-financial-services](http://www.fca.org.uk/publications/discussion-papers/dp15-7-our-approach-smes-users-financial-services).

<sup>47</sup> The joint FCA/CMA market study on SME banking can be accessed here: [assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report\\_final.pdf](https://assets.publishing.service.gov.uk/media/53eb6b73ed915d188800000c/SME-report_final.pdf).

<sup>48</sup> Our approach to SMEs as users of financial services, FCA, November 2015: [www.fca.org.uk/publications/discussion-papers/dp15-7-our-approach-smes-users-financial-services](http://www.fca.org.uk/publications/discussion-papers/dp15-7-our-approach-smes-users-financial-services).

## 5. Potential future work for FCA

### Beyond the scope of the CMA's investigation

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- 5.1** The FCA's role and remit in relation to retail banking goes beyond that covered within the scope of the CMA's investigation. We are mindful of the initiatives already underway in this space, and its changing nature.<sup>49</sup> However, the importance of this sector to both personal banking customers and businesses means it is vital we continue to take an active role in ensuring consumers are adequately protected and that competition works effectively in all areas of retail banking. The treatment of long-standing customers was identified as a priority for the FCA in our 2016/17 Business Plan.<sup>50</sup>
- 5.2** There are two areas in particular where we consider that further work will be necessary to better understand the risks to our objectives we see in this sector: high-cost credit; and in relation to the wider retail banking competitive landscape.

### Our approach to high-cost credit

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- 5.3** As described earlier, we will take action in relation to the CMA's recommendations to us on overdrafts, which form part of a wider package of measures that the CMA is putting in place seeking to promote more effective competition for overdraft users.
- 5.4** We recognise, however, that the subject of overdrafts, and specifically transparency and charges, is contentious. During the CMA's investigation, a number of stakeholders expressed concern regarding the cost of unarranged overdrafts. Some have also called for further steps to be taken to address the cost of unarranged overdrafts – for example, by imposing a cap. Others are of the view that unarranged overdraft charges should be set at the same level as arranged overdraft charges, and that we should review overdrafts in the context of other forms of 'emergency' credit.
- 5.5** We will undertake work in the area of overdrafts to help ensure that markets work well for all users and that these customers are appropriately protected. We will therefore take action in response to the CMA's overdraft recommendations to us, including reviewing the effectiveness of the MMC as soon as it has been in effect for a sufficiently long period.
- 5.6** It is important to note that the FCA has a broader set of statutory objectives, duties, powers and tools than the CMA, which requires us to consider interventions from a consumer protection perspective as well as a competition perspective. Given the importance of these issues, the range of views on possible solutions and their potential benefits and impact (including unintended

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<sup>49</sup> See paragraph 2.5 onwards.

<sup>50</sup> See FCA 2016/17 Business Plan: [www.fca.org.uk/publication/corporate/business-plan-2016-17.pdf](http://www.fca.org.uk/publication/corporate/business-plan-2016-17.pdf).

consequences), we consider it appropriate to examine overdrafts in the context of the wider consumer credit market and, in particular, in comparison to other forms of high-cost credit.

- 5.7** Therefore, we intend to invite views and evidence on the issue of overdrafts in a separate section of the Call for Input on the HCSTC price cap review, which will be published later this month. This will ask questions on wider issues relating to high-cost credit. For example, the potential consequences ('waterbed' effect) of taking action on specific high-cost credit products, particularly on firm behaviour and consumer welfare. The views and evidence we gather will help inform a decision about what work we should undertake in this area in future. Depending on the evidence we receive, we may decide we are able to take action sooner than the conclusion of our work on reviewing the effectiveness of the MMC.

### **Further work in relation to the wider retail banking competitive landscape**

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- 5.8** We recognise that there are wider questions for the FCA in relation to the retail banking competitive landscape: in particular, the multi-faceted nature of retail banking means we need to look more holistically. Many of these were beyond the scope of the CMA's investigation. Relevant issues for the FCA include the following:
- **The implications of the retail banking business model** – The retail banking business model spans multiple product lines and the actions of firms in one market can affect consumers in another. The FCA has undertaken several market studies focusing on particular markets, but has not, to date, looked at market outcomes holistically across the broader retail banking sector. We intend to undertake further work in this area, looking at how conduct and competition are affected by the links between different parts of the business model. Part of this work will include considering the impact of FICC banking more broadly than was within scope of the CMA's investigation. We will issue a further communication on the scoping of this work.
  - **Consumer demand for convenience in retail banking products** – A finding common across many of the market studies that we have undertaken is the value many consumers place in holding multiple products with one provider. Many of our market study remedies focus on trying to encourage consumers to shop around and switch and these remedies could be undermined by such consumer behaviour. We are considering whether there is value in undertaking further work to better understand the drivers of this preference.
  - **The impact of innovation in retail banking and the increasing role of non-banks** – We believe that innovative services – both those originating from third parties and those originating from banks themselves – have the potential to drive competition and improve the customer experience in retail banking. Throughout our work, we will aim to encourage and support this consumer-friendly and competition-friendly innovation. However, we also need to consider the implications for those who stay with more traditional providers.
- 5.9** Our Business Plan for the year ahead will indicate the substantive work that we decide to undertake.

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