



## Remedies Proposed in UK Retail Banking Sector to Address Lack of Competition

The UK Competition and Markets Authority (“CMA”) has provisionally concluded there is a lack of effective competition in the UK retail banking market and has proposed a number of remedies to improve customers’ knowledge and awareness, encourage them to switch providers, and make it easier for them to do so. However, the CMA has refrained from imposing structural remedies, such as breaking up the UK’s largest retail banks or requiring banks to cease offering so-called “free-if-in-credit” (“FIIC”) banking services.

This is a key stage in the CMA’s market investigation of the sector, which is assessing whether competition is working effectively in the retail banking sector in the UK, in particular for personal current accounts (“PCAs”) and banking services to small and medium-sized enterprises (“SMEs”).

Market investigations involve in-depth reviews of markets as a whole to identify whether there are any features that have an adverse effect on competition. The CMA’s provisional findings set out its initial conclusions on the competition concerns it has identified and the range of possible remedies. These conclusions and remedies are subject to consultation before a final decision will be made before May 2016.

However, the provisional findings usually indicate the likely outcome of the investigation.

The PCA market has previously been reviewed by the UK competition authorities, and other consumer financial services markets have been or continue to be scrutinized in similar ways, including private motor insurance, payment protection insurance, general insurance add-on products, and home credit. The UK’s Financial Conduct Authority (“FCA”) recently launched a “call for inputs” on residential mortgages and has an ongoing market study of the wholesale market, including investment and corporate banking services.

### Scope of Investigation

The UK’s current account market is concentrated, with the four largest banks accounting for more than 70 percent of active PCAs and 80 percent of Business Current Accounts (“BCAs”). There have been longstanding concerns that this concentration has remained stable for many years and that customers are not switching providers. Some 57 percent of consumers have been with their current PCA provider for more than 10 years and 37 percent for more than 20 years. In 2014, only 3 percent of customers switched their PCA provider.

On the other hand, customer surveys have shown that a high proportion of customers are satisfied with their main current account provider. The investigation was undertaken following concerns expressed by politicians, new entrants (“challenger banks”), and consumer organizations.

The scope of the investigation has focused on three broad theories of harm:

**Customer Inertia and Lack of Switching.** The CMA investigated whether consumers face difficulties choosing or switching products or suppliers, and whether this means that banks are not sufficiently incentivized to compete for customers on price, quality, and innovation. Much of the focus has been on consumer inertia and lack of switching by consumers. The lack of engagement by consumers is not unique to the retail banking market in the UK but has also been a feature of other retail markets, including energy.

A particular feature of the CMA’s analysis, and the subject of much media attention, is the prevalence of the FIIC model of charging for banking services in the UK. This means that, if a customer’s account remains in credit, he will not be charged any direct fees for the daily operation of his personal current account but also will not be paid interest on the balance in the account and may also be subject to charges for nonstandard services such as overdrafts.

**Market Power of Four Largest Banks.** The CMA considered the extent to which the markets for the supply of the banking services are concentrated and confer market power on those banks and whether this leads to worse outcomes for consumers. The evidence showed that the market is concentrated in the UK’s personal current account market, mainly resulting from the low level of switching between current account providers by consumers, but not highly concentrated.

**Barriers to Entry.** The CMA also reviewed whether there are barriers to entry and expansion that lead to worse outcomes for consumers. The barriers to entry could arise from regulatory barriers (e.g., capital requirements, anti-money laundering requirements, and the authorization process), access to payment systems, IT and funding, and strategic and first mover advantages, which could favor the larger incumbent banks.

## Provisional Conclusions on Competition

The CMA concluded that competition in both the PCA and SME banking markets is negatively affected by low customer engagement, barriers to searching and switching, and linkages among the PCA, BCA, and SME loans markets. As was the case in its recent findings in the retail energy sector, the CMA considers that weak customer engagement when it comes to shopping around for better prices and switching suppliers inhibits effective competition. In particular, it results in a lack of switching, an absence of incentives for banks to innovate through better products and prices, and greater difficulty for new entrants to gain a foothold in the market.

Nevertheless, the CMA did not consider that the FIIC model distorted competition in the market. Some UK banks already offer accounts with bank charges and a system of rewards that compete with FIIC accounts. There was also evidence that FIIC accounts offer a reasonable deal to many consumers and no convincing evidence that they distort competition.

The CMA also acknowledged some positive developments—including new entrants, innovative products, the rise of digital banking, and new data and price comparison tools—to address the customer engagement problem and stimulate greater competition. The CMA also noted existing tools and initiatives in the market aimed at facilitating switching, such as the Current Account Switch Service. However, the CMA concluded that these by themselves were insufficient to address its current concerns.

The CMA believes that incumbent banks have market power over their existing customers that enables them to charge higher prices, but it did not find evidence of coordinated behavior among banks. Nor did it consider that the current level of concentration among the four largest banks by itself is harming competition or customers.

However, the CMA suggested that any increased consolidation among the largest four banks would cause concern, although merger activity involving smaller banks would not have the same impact and could be procompetitive.

## Proposed Remedies

The CMA has a wide range of options to remedy adverse competition effects, including price caps and even breaking up companies, as it has done in a number of cases, notably in the UK airport and cement sectors. There were calls by politicians, challenger banks, and consumer organizations for the CMA to impose stronger remedies in this investigation. In particular, there were calls for breakup of the large retail banks in the UK and a ban on FICC banking (arguably a form of price control). The CMA considered these options but concluded these remedies would not be justified or proportionate in the circumstances and would not necessarily help resolve the competition concerns identified.

Instead, the CMA focused on measures aimed at empowering consumers by providing them with better information about how to switch providers, the options available, and how to compare them.

Specific remedies include:

- Requiring banks to prompt customers to review the service they receive from their bank through individual messages at certain “trigger points,” for example when a customer has incurred charges as a result of an unauthorized overdraft, when there has been a local bank branch closure, or when there has been a breakdown of service due to IT glitches.
- Making it easier for customers to compare bank products by improving or putting in place new price comparison website tools, as well as giving customers easy access to their banking history to use to shop around.
- Requiring banks to raise public awareness of switching bank accounts including through advertising.
- Requiring better sharing of information with credit reference agencies, banks, and financial advisers to make it easier for SMEs to shop around for loans.

The CMA's preferred solution to consumer inertia therefore involves “nudging” customers into making more rational choices. This policy strategy is consistent with the increased use of behavioral economics by UK competition authorities and regulators in assessing and promoting competition in such consumer-facing markets.

## Conclusions

The CMA's report provides a further indication of how the UK competition authority can use market investigations to examine and redress markets it believes may not be functioning well, as the [CMA also recently did in the energy sector](#).

It is likely that the banks will welcome the proposed remedies as being less intrusive and radical than they could have been. But this is unlikely to be the end of the matter. The retail banking market will continue to be scrutinized. In the near term, the CMA will consult on its provisional findings and proposed remedies to give all interested parties the opportunity to respond.

The precise detail of the remedies, and how they will be implemented, now will be carefully argued. For some of the proposed remedies, such as the “prompt” messages to consumers, there will be practical difficulties in prescribing and monitoring them in practice. The banks will wish to have certainty on the extent of their obligations and narrow their scope, while the challenger banks and consumer organizations are likely to seek to push the CMA to broaden them.

## Next Steps

The final report and decision on the market investigation and remedies must be issued by 5 May 2016. There will then follow a remedies implementation period and ongoing reporting to and monitoring by the competition authorities. It is likely that the FCA, the main regulator of financial services in the UK, will have a key role.

Given the nature of the market and the remedies, we would expect a formal detailed review to be undertaken after two or three years, to understand whether the remedies and other market developments have been effective in addressing the competition concerns; if not, the possibility of a further formal investigation and stronger remedies cannot be ruled out. Market investigations are costly, intrusive and disruptive, and it is likely that the banks will be incentivized to implement the remedies effectively and seek proactively to promote switching, to avoid a further review.

## Further Reading

To read more on this topic, we encourage you to click on the following links:

The [CMA's press release concerning the report](#)

A [summary of the report and possible remedies](#)

The [notice of provisional findings](#)

The [notice of proposed remedies](#)

The full provisional findings report will be available shortly on the [CMA's website](#)

## Lawyer Contacts

For further information, please contact your principal Firm representative or one of the lawyers listed below. General email messages may be sent using our "Contact Us" form, which can be found at [www.jonesday.com/contactus/](http://www.jonesday.com/contactus/).

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