Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Consumer and Competition Policy
1 Victoria Street
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Our ref: HMT/BIS CP

Dear Mr Lovitt

Managing Borrowing and dealing with debt: Consumer credit and personal insolvency review

This is the Financial Services Consumer Panel's response to the Department's call for evidence in support of the consumer credit and personal insolvency review. The Panel has addressed only question 8 in the paper, which deals with unarranged overdraft charges. This is because the remaining questions fall outside the Panel's specific remit.

Q8: Do you believe that the current voluntary, market-driven initiatives to address concerns about unarranged overdraft charges are delivering, or will deliver, sufficient improvements for consumers? If not, what would the wider implications of limiting bank charges be? Please provide evidence in support of your views.

In its 2008 Market Study of Personal Current Accounts in the UK[1] the OFT reported that there seemed to be a substantial cross subsidisation from those consumers who incurred insufficient funds charges to those who did not; and to a significant extent from 'vulnerable', low income and low saving consumers, to higher income, higher saving ones. Although the Panel has not undertaken specific research in this area, we do not think that there has been a marked change in the retail banking sector as a whole since then.

Based on Panel members' collective experience, we do not believe that voluntary market-driven initiatives will deliver sufficient improvements for consumers. There are only a small number of banks in the UK offering a branch network and transactional bank account service and as a consequence this sector of the market is dominated by a small number of players. There is a continuing lack of transparency about the real cost of banking services and it is difficult for consumers to help drive down the cost of unarranged overdrafts or other charges, whether explicit or hidden, by shopping around. The voluntary approach to dealing with unauthorised overdraft charges relies on banks improving themselves, yet they have

[1] At www.oft.gov.uk

patently failed to do this in other areas in the past – a key driver for the FSA taking over regulation of the deposit taking side of banking was to introduce an explicit and overarching requirement to treat customers fairly which had not been in the previous voluntary Banking Code.

Moves to impose mandatory limits on bank charges would, amongst other things, challenge current banking models and in particular the myth of “free banking”. Any profit lost as a result of limiting charges would almost inevitably result in banks seeking to recoup this in other areas of their business which would not be subject to such controls, such as by reducing the rate of interest payable on savings accounts. The Panel would welcome a public debate into whether consumers who remain in credit should pay a ‘fair’ fee for banking services and whether this would actually be to the advantage of the market as a whole.

In our evidence to the Independent Commission on Banking[2] we have set out a number of good consumer outcomes that we would like to see delivered by the banking sector. These include fair bank charges which are transparent and proportionate to the product or service provided. While we do not support the setting of maximum tariffs as such, we would like to see the financial services regulator putting measures in place to ensure that a bank should be able to break down a particular charge into the nature of component costs, including the element of profit that has been applied. Greater transparency will also help consumers to decide whether the products and services on offer meet their particular needs and also whether they represent value for money. In this context the Panel has concerns about packaged accounts, an area in which there has been a significant growth in recent years. Headlines from Mintel’s June 2010 research[3] showed around one in six current account holders have a fee charging packaged account and that twice as many would be prepared to pay a small fee for certain benefits. Yet earlier research[4] by Which? revealed that only 12% of its members with a packaged account said they used all the benefits it offered, while 78% used some and 10% none.

We also believe it would be worth exploring practical preventative solutions. For example, if financially vulnerable consumers locked into ongoing cycles of charges had access to a regulated mechanism with their bank whereby they could apply for repetitive charges to be stayed while they repaid the principal debt, this would help vulnerable consumers bring their overdraft back within arranged limits – we understand there may be a lending model or models with at least some of these characteristics already operating in the market. A preventative approach could eliminate the worst cases of consumer detriment from cyclical overdraft charges, and enable consumers to meet their financial responsibilities. This is a simple idea that the new Consumer Protection and Markets Authority could easily regulate, but with

[2] Financial Services Consumer Panel submission to the Independent Commission on Banking at www.fs-cp.org.uk
[3] Mintel at oxygenacademic.mintel.com
[4] www.which.co.uk

the onus on the consumers to engage in the process with their banks.

Yours sincerely

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