Citizens Advice Scotland

Scottish Association of Citizens Advice Bureaux

Personal Current Accounts

Consultation response to the OFT

By Keith Dryburgh, Policy and Public Affairs Co-ordinator

Citizens Advice Scotland and its 71 CAB offices form Scotland's largest independent advice network. CAB advice services are delivered through 199 service points throughout Scotland, from the islands to city centres.

The CAB service aims:

to ensure that individuals do not suffer through lack of knowledge of their rights and responsibilities, or of the services available to them, or through an inability to express their need effectively

and equally

to exercise a responsible influence on the development of social policies and services, both locally and nationally.

The CAB service is independent and provides free, confidential and impartial advice to everybody regardless of race, sex, disability or sexuality.

Citizens Advice Scotland
Spectrum House, 2 Powderhall Road
Edinburgh EH7 4GB
Telephone: 0131 550 1000
Fax: 0131 550 1001
Email: info@cas.org.uk
Web: www.cas.org.uk

The Scottish Association of Citizens Advice Bureaux - Citizens Advice Scotland (Scottish charity number SC016637)

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Introduction

1. Citizens Advice Scotland (CAS) is the umbrella organisation for Scotland's network of 71 Citizens Advice Bureau (CAB) offices. These bureaux deliver frontline advice services throughout nearly 200 service points across the country, from the city centres of Glasgow and Edinburgh to the Highlands, Islands and rural Borders communities.

2. Citizens Advice Scotland welcomes the opportunity to respond to the OFT market study on Personal Current Accounts in the UK. The response is based on the actual experiences of CAB clients, anonymised and presented as case evidence. This is made possible by the CAB service's social policy feedback mechanism. Bureaux throughout Scotland highlight the problems in their area by sending in specific case examples that are indicative of wider issues. This information is collated and analysed by CAS in conjunction with social policy statistics from each bureau.

3. In 2006/07, 91,475 new debt issues were brought to Scottish bureaux – an increase of 4% on the previous year. This represents more than 250 new debt issues brought to Scottish bureaux each day of the year. Consumer debt remains by far the most common single issue that clients bring to bureaux.

4. CAS is well placed to comment on the problems with the Personal Current Account market in the UK. Many of the debt issues that clients bring to bureaux concern the actions of banks and problems with their accounts. These issues comprise a variety of different client problems including bank charges, difficulty opening accounts, banks freezing or closing accounts, and third party involvement.

5. This consultation response examines the problems experienced by Scottish bureau clients in relation to personal current accounts. Our response also:-

    a. examines the remedies by which the UK banks can make their terms and conditions more transparent
    b. looks at ways of encouraging customers to become more informed and take control of their account, and
    c. looks at how the UK banks can make their insufficient funds charges more transparent and proportionate.

Context

6. UK banks made over £3 billion from insufficient funds charges on personal current accounts in 2006. This represented 38% of UK banks personal account revenue, and around 12% of total retail bank revenue. Insufficient funds charges are therefore a profitable aspect of the personal current account market.

7. However, these charges can have a significant negative effect on consumers, particularly those with low levels of income. Bank charges can push a manageable debt situation into an unmanageable one, making juggling finances impossible.

8. Scottish bureau evidence on current accounts suggests that low income consumers are not well served by the market. Multiple high charges, that are insensitive to level of income and level of overdraft infringement, inherently discriminate against low income consumers. These disproportionate charges hit low income consumers and fund an unfair cross subsidisation from low income to higher income consumers.

9. Despite many consumers incurring high overdraft charges, the level of awareness of the level and likelihood of incurring charges is consistently underestimated by consumers. This is in large part due to the opaque and inconsistent way in which banks communicate their terms and conditions. Consumers are led to believe that the UK has a ‘free’ banking system; in reality, it is the free part of current accounts that are well explained by banks, while the fees and charges of accounts remain hidden and difficult to understand – but not difficult to incur.

10. Based on the concerns noted in the OFT’s report on current accounts, and the problems experienced by Scottish bureau clients, it is clear that changes to the personal current account market in the UK are both desirable and necessary. There is a general consensus that insufficient funds charges, or overdraft fees, are disproportionately high compared to costs and there imposition is done in an opaque and unfair manner.

11. This consultation response will look at the problems that bureau clients experience in relation to their current accounts, and look at remedies that will improve the service that banks offer consumers.

Bureau evidence on Personal Current Accounts

12. Overdraft charges, or insufficient funds charges, has been a hugely significant issue for Scottish Bureau clients in the last five years. They are a contributory factor to the increase in the number of bureau clients seeking advice on debt, while bureau have been active in helping clients to reclaim unfair and disproportionate bank charges.

13. Our evidence shows that customers have little understanding of the level and likelihood of incurring overdraft charges. The system of overdraft charges is unclear and confusing for bureau clients who do not understand the charges until they start to incur them – and once charges are levied, they are so high that they do not offer clients much of a chance to learn from their mistake.

14. Despite the outcome of the High Court case between the OFT and the UK banks earlier in 2008, bureau clients continue to experience problems with their overdrafts and subsequent charges. This response will look at the problems under the following headlines:

- Disproportionate charging
- Direct debits/standing orders
- Item charges
- Multiple insufficient funds charges
- Unclear terms
- Responses to client requests

Disproportionate Charging

15. Scottish bureaux have seen a number of clients who have built up substantial charges for a very small overdraft. These clients often go into their overdraft without realising that they have done so, and find that they have incurred high overdraft charges at the end of the month.

16. These overdraft charges are often highly disproportionate to the level of overdraft infringement. This system inherently discriminates against low income customers, where the level of charges is insensitive to the level of infringement.

An East of Scotland CAB reports of a client with severe mental health problems who quickly built up substantial bank charges for an overdraft of £1.92. The client used her debit card for a purchase of £4.25, not realising that there was only £2.33 in her account. Over the next two months her overdraft of £1.92 grew to more than £180, solely as a result of interest and charges imposed by the bank. The client was very worried as to how she could possibly pay this from an income of £79 per week.

An East of Scotland CAB reports of a client who received excessive bank charges for a small overdraft. The client is a mature student who works part-time. The client went 60 pence into his overdraft and was charged £28 and then £38. Since then, the client has been unable to clear his overdraft. The client only earns £50 per week, and finds himself in an impossible situation.

A West of Scotland CAB reports of a disabled, lone parent who was given an overdraft charge after exceeding her overdraft limit for one day. The client stated that she regularly checks the status of her account using the telephone services and was at no time made aware of a problem with her account. The client exceeded the overdraft limit on her account for only one day and feels that the £28 charge is excessive and unfair.

An East of Scotland CAB reports of a pensioner who received excessive charges for exceeding her overdraft limit. The client recently exceeded her overdraft limit by £46.74, with her bank statement showing charges of £170 for exceeding the limit. The client lodged a complaint about the excessive charge, but despite being a pensioner found that the local manager was unsympathetic to her situation.

17. Overdraft charges can have a significant impact on clients whose only source of income is benefit payments. These clients can budget in pennies, then find that a slight overspend can mean that they owe up to £100 in charges. A standard overdraft charge of £25 is a daunting prospect for those living on benefit payments.

18. The consequence of this policy is that low income customers can very quickly be in a lot of debt to a bank due to a small overdraft. The customer's low income would then preclude any chance of getting out of the overdraft, thereby trapping the client in a cycle of debt.

19. The consequence of this cycle of debt is that clients begin to have their benefits – which are necessities for living - swallowed up by charges. Under the present system, benefits lose their identity when they reach the client's account, and are used by the banks for paying bank charges. This can leave clients with very little to live on.

An East of Scotland CAB reports of a client who has bank charges taken from her account each month even though her income consists entirely of benefits. The client gets about £40 per week, but this month's bank charge was £120, leaving the client with £10 a week to live on. The client is stuck in cycle of bank charges that her limited income will not allow her to escape from.

An East of Scotland CAB reports of a client who experienced significant financial and housing difficulties when his benefit payments were swallowed by bank charges. The client lost his job and was unable to continue his contractual obligations while on Job Seekers Allowance (JSA) and went into his overdraft. The client's housing benefit and JSA were paid directly into his account, but all monies going into the account were swallowed up by bank charges for unauthorised overdraft, failed direct debits and letters to the client. The client went into rent arrears and was evicted by the landlord. He is currently homeless and staying with a friend. The bureau arranged for the client's housing benefit to be paid directly to a landlord and another account opened for his JSA to be paid into.

Unpaid item charges

20. A common problem for bureau clients is high charges for unpaid items. This is particularly the case for missed direct debits and standing orders. These charges are for a high amount (commonly £35) and can be charged a number of times in the same month for a client with multiple direct debits. The impact of this is that a client who is not in overdraft can be dragged over their overdraft limit by a missed payment and consequently incur a number of charges.

21. For example, a client who has £34 in their account and has a £35 direct debit to be paid from the account on that day will be likely to incur a £35 missed payment charge and then a £25 charge for going over the overdraft limit. This would leave the client with a £26 overdraft and liable to receive future charges – including the missed direct debit.

22. A client may have set up multiple direct debits for the same day. If the balance is not as high as expected, this can have disastrous multiple charges for the client.

An East of Scotland CAB reports of a client who went into his overdraft and consequently was charged for missing nine direct debits. The client does not have guaranteed hours of work and already owed more than £15,000. The client's debt problems were aggravated by receiving £351 of bank charges for missed direct debits in a two week period. The charges are approximately the same as his monthly wage.

A West of Scotland CAB reports of a client who was charged twice for the non payment of a standing order. The client had insufficient funds for a standing order of £17 and received a charge of £38 for the 'unpaid item'. He put money into the account to cover both costs, but then received a letter from the bank advising him of an additional charge of £28 for an unauthorised overdraft relating to the same standing order. The customer feels that these charges are excessive and is being charged for the same thing twice.

A West of Scotland CAB reports of a client who returned from holiday to find that she had been charged for a missed direct debit as she was 2 pence short. The bank charged the client £35 for the missed direct debit. The client was extremely unhappy with the charge as she has been a customer with the bank for over 20 years.

23. This situation can also occur for reasons outwith the control of the client. For example, if a client has a direct debit set up without their knowledge, has a payment deducted before it is due, or has their wages paid late, this can have a huge impact on the finances of a client through no fault of their own. The client may have the error corrected, but are unlikely to have their overdraft charges cancelled.

A North of Scotland CAB reports of a client who incurred overdraft fees after receiving her pay later than promised. The client was due to be paid on the 28th of December, but did not get paid until the 5th of January. This resulted in the client going £3 over her overdraft limit. The client received a charge of £35 for missing a direct debit as a result, and received another charge after being overdrawn the next month as a result of the initial mistake.

A South of Scotland CAB reports of a client who received charges after a missing direct debit repayment that she had not authorised. The client maintains that she had not authorised a direct debit for a TV Licence, but a debit was presented against her bank account recently. The client's bank returned the direct debit unpaid due to insufficient funds and charged her each time this was done - £35 charges on three occasions. The application of these charges resulted in the client's overdraft being exceeded and additional charges levied – the total amount of charges was around £130. The client's benefit payments are now being used to pay for charges and the client has had to apply for a crisis loan.

24. Clients may be also charged for the number of items that they purchase while in overdraft. These charges can be significantly and disproportionately high for a client who does not realise that they are already in their overdraft. The charges are very difficult to predict, as it is difficult for a client to know at what point they will start to incur the charges. The charges are also insensitive to level of the purchase, often charging the same set fee for a £2.50 food item as luxury goods costing £1000.

25. For example, a client that enters into their overdraft while on a shopping trip could incur charges for every item paid for over the limit. A client who buys three items over the limit could expect a £25 overdraft charge and three charges of up to £30 for each item – a total of £115 worth of charges.

A North of Scotland CAB reports of a client who has received excessive charges on items paid for when in his unauthorised overdraft. The client has an authorised overdraft of £2,000, but has occasionally been over this limit in the last year. His bank charges £30 for every item paid for over the limit, with a maximum of three such charges per day. The client has paid a total of £1,135 in overdraft charges in five months, mainly due to the item fees.

Multiple Insufficient Funds Charges

26. The variety of different types of overdraft and similar charges – insufficient fund charges, missed payment charges, and item charges, among others - mean that clients can receive levels of charges that are massively disproportionate to the level of infringement. It is not inconceivable that a client could slip into their overdraft unknowingly by a few pounds, miss two direct debits, and buy three items while over the limit. Using the cases in the response so far, this could mean charges of nearly £200 for a small overdraft.

27. This is an example of a 'snowball' effect, in which a client enters their overdraft on one occasion and incurs multiple charges. This effect can cause severe detriment to clients and condemn them to an endless cycle of charges. Alternatively, clients may go in and out of their overdraft in the same month and incur a charge for each separate occasion.

28. Analysis by MoneyExpert.com found that the average total charges are £44.98 for an overdraft infringement and fees for an unauthorised overdraft can go much higher. Around 30 per cent of all current accounts charge a combined fee of £60 or more for straying beyond the borrowing limit.[1] By contrast, fees for defaulting on a credit card are a standard £12 after being effectively capped by a recent investigation by the Office of Fair Trading.

29. The upshot of the variety of charges that clients can incur has resulted in a substantial cross subsidisation from those who incur charges and those who do not. According to the OFT market study, and supported by our evidence, this cross subsidisation is from low income, low saving clients, to high income, higher saving consumers. Indeed, the revenue made from the customers who incur charges is actually keeping the cost of an account low for other higher income customers.

[1] http://www.moneyexpert.com/ContentArticle/None/Overdraft-mistake-costs-nearly-fourty-five-pounds-on-average/Article.aspx?articleID=237&productTypeID=0

Transparency and client awareness

30. A significant finding from the OFT market study is that consumers have a poor understanding of the consequences of going over their overdraft limit. Consumers often underestimate the likelihood of incurring fees and the cost of doing so. Nearly four fifths of consumers in the market study who had been charged in the previous twelve months had never heard of such charges, while only 7% of consumers knowingly went into their overdraft.

31. Evidence from Scottish bureau suggests that clients can have little idea of the likelihood and the cost of incurring overdraft charges. Unfortunately, this is a mistake that can have long-term negative effects for a client.

A South of Scotland CAB reports of a client who incurred bank charges after assuming that his card would be frozen after he ran out of funds. The client did not know about bank charges, thinking that he would be told when he had no money. The bureau asked for a refund of charges, but found it very difficult to find somebody who would talk about the client's situation.

32. Clients need to take responsibility for knowing how their current account works and the charges for its misuse. However, banks have a responsibility for ensuring that the terms and conditions of use for current accounts are clear and understandable. This is not always the case. The OFT market study raised concerns over a 'lack of transparency' over 'less visible' terms and conditions in current accounts. This is borne out in Scottish bureaux evidence.

An East of Scotland CAB reports of a client who opened a student account upon starting her studies, and built up substantial charges without ever using the account. At some point, the client's account changed to a 'royalties account' which meant a charge of £6 per month for use of the account. Because there was a zero balance the £6 charge put the account into the red and a £28 per month bank charge plus interest began to be applied. By the time the client realised what had happened, she had a debt of over £300 and rising. The client maintains that she was not told that the unused account was going to be upgraded to the new fee-charging account nearly two years after she had initially opened the account. Whether the bank informed the client is unclear, but it is likely that if she was informed it was not in a clear and transparent fashion.

Switching

33. Low levels of switching are a distinctive feature of the personal current account market, especially when compared to other markets in the UK. The OFT market study found that the personal current account market has a very low level of switching, with only 13% of consumers having switched their account in the last five years. This compares poorly with the electricity (54%), gas (54%), and car insurance (61%) markets, as well as with other financial products, such as credit cards (31%) and savings accounts (20%).

34. The knock-on effect of low levels of switching is a lack of competition in the market, and clients are therefore unable to make the threat of switching to banks that provide a poor service. A lack of competition then manifests itself in poorer terms and conditions, as the main banks are not incentivised to offer better deals to win more customers.

35. Despite the lack of switching, it is clear that clients can benefit from moving to another bank. The OFT market study found that yearly savings from switching would range from £7.50 to £110, mostly through switching to an account offering a higher interest rate. Clients who persistently incur insufficient funds charges have potentially the most to benefit from switching their accounts.

36. Past and current problems with switching has lowered client confidence in switching their own account, with the OFT market study finding that almost half of consumers (45%) wouldn't be confident that the switching process would be smooth. These fears are borne out by the finding that over a quarter of clients who had switched their account had experienced problems.

A West of Scotland CAB reports of a client who experienced problems in switching her bank account. The client cleared her overdraft with her bank before changing to a different bank. Her new bank told the client that they would take care of transferring the direct debits to the new current account. However, a few months later the client received a letter from her original bank stating that she had gone over her overdraft limit of £1000. It transpires that the bank account was not closed and that direct debits have been going out of both accounts. The two banks are blaming each other for the mistake, while the client's original bank is threatening legal action to reclaim the overdraft debt. The bureau contacted both banks and has not received a response from either.

37. Many clients are disinclined to switch their account due to a negative past experience. However, the majority of clients who have not switched their account have never even considered doing so. This is because they do not understand the costs of their account, which they perceive to be free of charge, and therefore have little understanding of the benefits of switching to another account. Customers also display a misplaced loyalty to banks which they have been with for years, when they could be much better off with a different account. Bureau have seen clients who have experienced significant financial difficultly partly through refusing to open another current account.

An East of Scotland CAB reports of a client who experienced significant financial and housing difficulties when his benefit payments were swallowed by bank charges. The client lost his job and was unable to continue his contractual obligations while on Job Seekers Allowance (JSA) and went into his overdraft. The client's housing benefit and JSA were paid directly into his account, but all monies going into the account were swallowed up by bank charges for unauthorised overdraft, failed direct debits and letters to the client. The client went into rent arrears and was evicted by the landlord. He is currently homeless and staying with a friend. The bureau arranged for the client's housing benefit to be paid directly to a landlord and another account opened for his JSA to be paid into.

Responses to client requests

38. A significant problem for bureau clients is the attitude and actions that banks take when clients question or ask for reprieve from charges. The responses from banks to customer queries are unpredictable and erratic, and can adversely affect the customer.

39. Scottish bureaux have found that attempts to negotiate with banks over overdraft fees are often met with unhelpful attitudes and sometimes retaliatory action.

An East of Scotland CAB reports of a client who had her agreed bank overdraft removed after sending the bank a letter requesting repayment of bank charges she felt were unfair. Upon receiving the letter, the bank removed her agreed overdraft, leaving her liable to charges once again, and gave the client a week to repay the overdraft (£600). The bureau feels that the bank's actions are retaliatory, and advised the client to report the matter to the Financial Ombudsman.

An East of Scotland CAB reports of a client whose account was frozen after he sought advice on clearing his overdraft. The client had financial problems that had pushed his account over his authorised overdraft limit. At this point, the client sought advice from the bureau to help him stay out of his overdraft and avoid charges. The bureau wrote to the bank asking them to consider reimbursing some of the charges to help stabilise his position while he worked out repayments to the bank and his creditors. The bank responded by freezing the client's account, leaving the client with no access to funds, even though he was within his authorised overdraft at that time. The bureau requested an explanation and was told that the account had been frozen as the accounts were "at risk". The client feels he is being punished for trying to be responsible with his money and repay his debts.

40. Another common response from banks is to pressure clients to take out new products while they are stuck in their overdraft. This can include consolidation loans, re-financing loans, and other products. Clients feel under pressure to agree to these requests as overdraft charges mount up. It is also common for banks to ask for high rates of repayment of overdraft arrears and to be unresponsive to other offers of repayment.

An East of Scotland CAB reports of a client who has an overdraft with a bank who is pressuring her to take out other products as part of a repayment agreement. The client is trying to repay an overdraft she incurred while at university. The client has since changed her account for financial reasons. The bank has sent correspondence stating that the client must re-open an account with them, take out a credit card, and are asking for £260 per month. The client cannot afford to pay this amount, and has tried repeatedly to contact her branch to negotiate. Meanwhile, her account continues to incur overdraft charges.

An East of Scotland CAB reports of clients who were offered a consolidation loan after advising their bank that they were experiencing difficulties repaying their overdraft. The clients had an overdraft of £3,546 which they felt unable to repay. At the time, both clients were under considerable stress and did not fully understand the nature of the agreement. The loan including insurance cover of £1,281 which was not required as neither of the clients are able to work, which the branch manager was aware of. The clients now have a debt of £8,600, an increase of £3,000 on the original debt.

A South of Scotland CAB reports of a client who was pressurised to take a consolidation loan to repay his overdraft. The client is currently unemployed and living on Job Seekers Allowance. The client noticed that the interest on the consolidation loan was greater than he was currently paying on his overdraft. His income is only £42.70 per week and he is not in a position to take on a loan.

41. Citizens Advice Bureaux in Scotland have reported frequent problems when dealing with banks concerning personal current accounts. This can include difficulties in finding the right department to speak to concerning a client’s account, difficulty in getting a bank to accept that the bureau is acting on behalf of the client, and recently problems with banks freezing clients’ accounts when a client seeks advice at a bureau.

42. Scottish bureau have reported banks who have refused or delayed recognising a bureau as representing a client. The consequence of this is that the bureau cannot act on the behalf of the client while banks continue to request payments from them.

A West of Scotland CAB reports of a case in which a major bank refused to recognise a Citizens Advice Bureau as representing a client. The client had asked the bureau for help to re-claim bank charges on his account. The bureau contacted the bank on the 8th of March 2007 by letter with a signed mandate from the client. The response stated that the bank ‘is under no statutory obligation to record this information and therefore I am unable to assist further with your request'. The bureau contacted the bank again to request information relating to the bank charges, and were asked to forward another signed mandate from the client. The bureau received no reply, so sent the letter and mandate again, but were told on the phone that the bank had not received a mandate. The bureau received a letter from the bank dated 10.9.07, six months after first sending a letter, advising that 'with effect from 23 April 2007 it became an offence to provide claims management services without authorisation.' It further reads that after checks they were 'unable to confirm your company have the required authorisation.' The letter went on to say that the bank would deal directly with the client. This correspondence took place over a period of over six months without the bank accepting that the bureau was representing the client.

An East of Scotland CAB reports of a retired client with a loan who was upset by the harassment she felt she was receiving on the telephone while she was trying to negotiate a solution to her debt problems. The client had approached the bureau for help, but the bureau found that creditors were taking a long time to respond to their letters while continuing to contact the client directly. The client was then told on the phone that the bank does not deal with third parties, including the citizens advice bureaux. The bureau contacted the head office of the bank who advised that this was not the case and that the original offer of repayment would now be accepted.

43. A recent trend reported by bureau has been banks freezing clients' accounts after a citizens advice bureau has made contact on behalf of a client. The reasoning behind this action is that the banks are protecting their own funds in case the client gets further into debt. This seems highly counterintuitive, especially as many UK banks encourage customers to visit a bureau if they are in financial trouble in their correspondence to clients. The effect of this policy is to place clients in short-term strife and long-term debt problems.

A North of Scotland CAB reports of a client who had her current account closed after making a reduced offer on her loan repayments. The client was in financial difficulty and the bureau made a reduced offer of repayment and sent her financial statement to the bank. The bank responded by immediately closing the client's bank account, which caused the client to lose her State Retirement Pension of £380 which was due to be paid in that day. The bureau called the bank who were unhelpful and would not return calls. The client was left with no money whatsoever.

An East of Scotland CAB reports of a client who had her current account frozen after a bureau contacted the bank with an offer of payment on behalf of the client. The client had been coping with her debts until her husband had had an accident at work. She decided to do the sensible thing and deal with her debts before they got unmanageable. The bureau sent out letters to the client's creditors offering repayments, but received no reply from the client's bank. On approaching her branch, the bank informed the client that the account was 'frozen' and she could not withdraw any money. The client had £461 in her account, and was therefore not in her overdraft. The branch informed her that because she had involved the CAB, it was their policy to automatically freeze the account. The branch further told the client that she should have come to them for help, and not the CAB. The client duly informed them that she had approached them and asked for a loan to tide her over until her husband went back to work, which they had refused. The client then asked what help they could offer her, receiving the reply that as she had involved CAB, there was no further help they could give her. The client left the branch with no money, and two children under 10 to feed over the weekend.

Remedies

44. Based on the concerns noted in the OFT's report on current accounts, and the problems experienced by Scottish bureau clients, it is clear that changes to the current account market in the UK are both desirable and necessary.

45. While banks can make revenue from providing customers with banking services, the key point is that this revenue should be achieved in a transparent and fair fashion from consumers in a market in which the banks that provide the best service and are the most innovative are rewarded.

46. There are a number of potential remedies that could create a more fair and transparent service for customers. These remedies are based on data from the OFT market study on personal current accounts and address the concerns already detailed in this response.

47. Most of these remedies are already in use in the UK banking market, but often only sporadically. If they were to be used more widely, they could lower disproportionate and unfair charges while promoting competition in the market. This response will look at proposed remedies under the following headings:

- Transparent terms and conditions
- Encouraging switching
- Changes to insufficient funds charges

48. The aim of these remedies is to make the terms and conditions of insufficient funds charges more transparent, and at the same time to make clients more informed of the circumstances in which they will incur these charges. The remedies also aim to curb the practice of charging low income clients high charges for having small overdrafts, which will help to stop the cross-subsidisation that currently exists in the market.

Transparent terms and conditions

49. The OFT market study outlined concerns about low levels of transparency on the fees that make up a substantial proportion of the payment that consumers make for current account services. The result of this is that consumers face a complex set of information when predicting when they will incur charges.

50. Imperfect information in the market has led to low levels of switching and a lack of consumer awareness, which has given banks little incentive to make their charges transparent to customers, much less to offer better deals on charges and interest. A clearer and transparent method of explaining charges to customers would allow for more perfect information and better consumer awareness, and possibly kick-start competition in the market.

51. The Competition Commission investigation into personal current accounts in Northern Ireland, which concluded in 2007, found that consumer awareness of charges was a distinct barrier to competition and fairness in the market, and recommended a number of remedies to increase consumer awareness, including:

- Easy-to-understand terminology and descriptions of PCA services
- Easy-to-understand explanations of the levels of charges and interest rates and how and when they are applied
- Information on statements
- Breakdown of charges and interest on statements
- Advance notice of charges incurred

52. The UK and Northern Ireland personal current account markets are similar and experience the same types of problems with transparency. The UK market may benefit from the types of remedies that were recommended for the Northern Ireland market.

53. The problem for bureau clients isn't necessarily that they don't know that they can incur charges, but more that they underestimate the level and number of charges that they can incur in various situations. Any remedy that outlines the terms and conditions of charges and when they occur will help client awareness and help them to avoid these situations.

54. Possible remedies that will help to make charges more comprehensible to customers include:

- **A standard set of account features to be published by each bank** – all banks to provide account information in the same format to allow easy comparison between accounts and to encourage switching. This information should include insufficient funds charges, so that clients begin to take this into account when switching.

- **Charges booklets** – a simple explanation in Plain English outlining the situations in which clients can incur charges, to be sent to all customers or those who have incurred a charge. Customers could be sent the booklet after they first enter their overdraft with a warning that these charges will be applied to their account unless they clear their overdraft.

- **A simplification of charges** – each bank has its own set of insufficient funds charges, ancillary charges, interest rates, missed payment charges, item charges, and overdraft terms and conditions. These terms and charges are complex and opaque, and can be changed regularly by banks. It would help clients to understand charges if they were more uniform in their names and descriptions, and were published in a similar fashion.

- **Monthly/yearly breakdown of charges incurred** – an itemised breakdown and explanation of the charges a customer incurred, and how the client can avoid them in the future.

- **Advance notice of charges to be levied** – to allow clients to know when charges are to be debited from their account and to allow them to budget against incurring further charges as a result of the debit.

Encouraging switching

55. The OFT market study found that the personal current account market has a very low level of switching, with only 13% of consumers having switched their account in the last five years. As mentioned previously, this compares poorly with other markets.

56. The reasons for the lack of switching are three-fold: Firstly, clients are put off by the problems experienced by others who have tried to switch accounts, such as missed direct debts. Secondly, clients often hold a misplaced sense of loyalty to their bank. This loyalty is misplaced, because banks offer better terms to new customers than to those who have banked with them for years.

57. Finally, and perhaps most importantly for bureau clients, they do not see or understand the benefits of switching their accounts, often due to the common perception that current accounts are 'free' and that they are therefore unlikely to receive a better deal elsewhere. However, the best accounts on the market are paying between 5% and 6% interest, while the four main banks offer around 0.1%. Switching to the accounts that pay interest will incentivise the main banks to offer a better deal to all their customers and increase competition in the market.

58. A remedy to the lack of switching in the market could therefore be to provide clients with the information they need to make an informed choice of the best bank account for their circumstances. This could take the form of:

- **A standard set of account features to be published by every bank** - all banks to provide account information in the same format to allow easy comparison between accounts and to encourage switching. This information should include insufficient funds charges, so that clients begin to take this into account when switching.

- **A booklet on the advantages of switching and how to go about it** – information on the key features of a personal current account to look for and the savings that could be made. The booklet could also explain the process of switching and how to go about it. This could be made available on the internet or be sent out yearly by banks to their customers.

- **A media campaign to inform consumers of their options** – there have been successful media campaigns on financial literacy and inclusion run in the recent past, and a campaign focused on getting clients to consider the account that they hold and take control of their finances could be influential.

59. Another avenue that could be explored is that of informing customers of how much they pay for their 'free' account, and therefore dispelling the myth of the free banking system. The majority of UK customers do not pay a fee for their account, but pay for their account in less obvious ways, such as interest

forgone, ancillary charges, insufficient funds charges, interest payments, and so on. In fact, UK banks make far more money per account from free if in credit accounts than from packaged accounts. The result is that most people have no idea of how much they pay for their personal current account.

- Therefore, **a mechanism that lets clients know how much they pay for their account** would help fuel comparison and switching between accounts. This could be done through a calculation page on a website that allowed customers to input information from their statements and find out their total cost. The calculation page could also be used to show whether the client would have saved money with a different account.

- Alternatively, banks could send a yearly statement to customers outlining the total cost to them of various charges and the interest foregone. This would allow clients to know an accurate cost of their account and to have a better idea of how the terms and conditions of another account would benefit them.

60. Other remedies could focus on improving the switching process for clients:

- **Improving the switching process** – the OFT should work with the UK banks and BACS to ensure an event-free switching process in the vast majority of cases. This will improve client confidence in the switching process. The average time for switching a bank account is currently about 8 weeks[2] - this is far longer than other services, and needs to be shortened.

61. The potential advantages of this approach would be to help inform clients of the important terms of their account and the advantages of switching, and therefore encourage clients to take charge of the management of their money. This would increase the levels of switching, and, in turn, encourage banks to offer more competitive terms and conditions.

[2] This is Money - http://www.thisismoney.co.uk/help-and-advice/advice-banks/article.html

Changes to insufficient funds charges

‘Opt-in’ Overdrafts

62. The OFT market study found that only 7% of consumers knowingly went into overdraft. There is therefore scope to suggest that a high proportion of the remaining 93% may not have entered their overdrafts if given the choice.

63. A potential remedy for this situation is for customers to have a choice of whether they want to go into an unarranged overdraft. Customers could indicate when they open an account whether they would prefer to go into an unarranged overdraft or be stopped from doing so if their account had no funds. Alternatively, a customer could be informed when making a cash withdrawal that doing so would take the customer into their overdraft, and asking if the customer still wished to take the withdrawal.

64. The benefit of this option is that customers who do not want to go into their overdraft cannot do so accidentally. Those that are prepared to go into their overdraft will at least be aware of the consequences of doing so. This remedy would also ensure that all clients are at least aware of overdraft charges when they begin to use their account.

65. The drawback of this option is that when customers run out of funds, they may be unable to find additional funds for essential expenditure on food or utilities. However, this option is voluntary for the customer so would put them in the position where they know that they cannot spend past their resources and are therefore less likely to spend unwisely. Customers could also be able to have the option of contacting the bank to ask for a temporary overdraft facility.

Warning Systems

66. The OFT market study found that many consumers are unaware of overdraft charges or underestimated the likelihood of incurring an overdraft charge. Nearly four fifths of consumers who had been charged in the previous twelve months had never heard of such charges, while only 7% of consumers knowingly went into their overdraft.

67. These findings suggest that there is scope for both warning clients that they are close to their overdraft and informing them of the consequences of doing so.

68. Some banks in the UK, are trialling the use of mobile phone texts to warn customers that they are close to entering their overdrafts and then again when they have entered the overdraft. Clients then have till the end of the day to get out of the overdraft until charges are applied.

69. This is a positive step towards informing customers of their financial position in real time, rather than sending them a letter after the event. Given the number of customers that unknowingly enter their overdraft, this should help to lower the number of people incurring charges. These texts could also include information on the level of charges that would be applied. The effect would be to make charges more transparent and clients better informed.

70. For those without mobile phones, there could be an option of phoning or emailing a client to inform them. This shouldn't be an opt-in service, but rather an opt-out service, in which all clients receive the service unless they ask not to.

71. However, the period in which clients have grace to clear their overdraft after receiving the text, often the working day, is too short for many customers. A customer will often have good reasons, such as work or transport problems, not to be able to reach a bank branch. It would therefore be beneficial if customers received a longer period of time to clear their overdraft, such as three days.

Buffer zones

72. A complementary remedy for disproportional charges is allowing customers to have a small buffer zone in their overdraft in which they have a certain number of days to clear their debt before they incur charges. This system would ensure that clients aren't hit with high charges for very small infringements into their overdraft, and allows for extra leeway for affording cheques and direct debit payments.

73. Some bank customers have a buffer beyond their agreed overdraft limit, for which they are charged a flat fee of £22 every time they run into it. As long as customers get back into the black within five working days, there are no extra fees and interest charges. The £22 fee is still too high – but the principle is a move in the right direction.

74. An alternative remedy would be to allow customers to have three chances at staying out of their overdraft before they incur charges. This would allow customers to learn from their mistakes, rather than being put into unserviceable debt the first time they enter their overdraft.

Proportional charging

75. The current banking system hands customers the same charges for small overdrafts as for large overdrafts. This system inherently discriminates against low income customers who can very quickly be in a lot of debt to a bank due to an overdraft of only £1 or £2. The customer's low income would then preclude any chance of getting out of the overdraft, thereby trapping the customer in a cycle of debt. This situation can then be made worse by multiple charges.

76. A remedy to this problem would be to charge customers proportionately for their infringement into their overdraft. An overdraft of £1 shouldn't be met with a charge that can be 30 times the amount – this isn't proportionate to the cost for the bank or fair to the client. It also gives little chance to customers on low incomes to clear their overdraft.

77. CAS therefore proposes that charges should be proportionate to the level of infringement, including low levels of charges for low levels of overdrafts. For example, a flat charge of £5 could be levied for any infringements of less than £30 in an overdraft. Clients would then be exempt from other charges provided they clear their overdraft within a certain limit.

78. In addition, clients should not be charged for going in and out of their overdraft during a month. For example, in the current system, clients who go into their overdraft three times in the month, even if this is only by pennies each time, will receive three sets of charges.

79. It is mutually beneficial, or should be, for banks and customers if the customer is financially stable. By charging low income customers high charges for small overdrafts, banks are taking away the chance of financial stability for many clients. Overdraft charges shouldn't be aimed at this end; they should allow customers to repay small overdrafts and proportionate charges and to reach a even financial footing.

Conclusion and recommendations

80. Personal current accounts, particularly in relation to overdraft charges, remain a key area of concern for bureau clients. The remedies to the UK bank system will have a significant impact on Scottish bureau clients.

81. Despite the outcome of the High Court case between the OFT and the UK banks, clients still struggle with disproportionate and punitive overdraft fees. Examples of problems that clients experience include:

- **Disproportionate fees** – paying high or multiple charges for small overdrafts

- **Swallowing of benefit payments** – overdraft charges can take away much needed benefit payments from clients

- **Direct debits/standing orders** – clients can receive multiple charges for being short of funds for a direct debit

- **Item charges** – clients who unknowingly go into their overdraft can receive multiple charges for buying further items

- **Unclear terms** – clients don't have a clear understanding of the terms of their overdraft and the consequences of overspending; the way that these terms and conditions are applied by banks doesn't encourage client understanding

- **Responses to client requests** – Banks are often unpredictable and unhelpful towards clients who actively try to make an agreement to repay overdraft debts

82. Scottish bureau clients are experiencing problems with other aspects of their current accounts. A client who is declared bankrupt, which is especially prevalent in Scotland in 2008 with the start of Low Income Low Assets (LILA) route to bankruptcy, is likely to have their bank account frozen and then closed. The effect is that clients are denied access to the funds in their account and struggle to have an account to have their pay or benefits paid into.

83. Other problems for bureau clients include a bank's policy/attitude towards citizens advice bureaux that are representing a client, which has included freezing a client's account for third party involvement.

84. Based on the concerns noted in the OFT's report on current accounts, and the problems experienced by Scottish bureau clients, it is clear that changes to the current account market in the UK are both desirable and necessary. There is a general consensus that insufficient funds charges, or overdraft fees, are disproportionately high compared to costs and that they are made through an opaque and unfair manner. It is therefore likely that the way in which banks impose charges will evolve in the near future.

85. Citizens Advice Scotland have a number of proposed remedies of how the banking model could be reformed to allow a more fair and transparent service for customers. These remedies include:

- **Transparent terms and conditions** – Simplifying charges and ensuring that clients are aware of and understand the terms and conditions of their account
- **Encouraging switching** – informing clients of the benefits of switching so that they are more likely to change accounts, thereby encouraging banks to offer better terms and conditions in a more competitive market
- **Opt-in overdrafts** – giving customers the option of not going into their overdraft when they have run out of funds
- **Warning systems** – warning clients, through mobile phone messages, when they are close to or into their overdrafts and giving a time period to repay
- **Buffer zones** – allowing a small amount that customers can go into their overdraft in which they can repay without charges within a time limit
- **Proportional charging** – charging clients on a scale according to how much they owe on their overdraft. Those in their overdraft by small amounts should receive small charges

86. These remedies would make the way that banks impose charges fairer and more proportionate to a client's situation. It would also decrease the level of charges and number of customers incurring these charges.

87. The effect of these remedies is of course a reduction in the amount of revenue the banks make from unauthorised overdraft charges. This is positive in the sense that this revenue is made from unclear charges from low income clients who can barely afford them.

88. The UK personal current account market isn't working for clients. The myth of free banking, alongside hidden terms and conditions, has lead to a low client understanding of current accounts and low levels of switching. This situation has proved profitable for UK banks, and there is therefore little incentive for banks to address the problems in the market and to offer better deals on their accounts.

89. The task for the OFT and the banks is to provide remedies that will empower clients to take control of their current accounts. This needs to be done by making terms and conditions more transparent, by encouraging switching, and making insufficient charges fairer and more proportionate. The effect would be to kickstart competition in the market on the hidden terms that currently adversely affect clients, and therefore encourage banks to make their revenue from better deals for clients, rather than from low income clients who can ill afford it.