

# **CRACKING THE CODES FOR BANKING CUSTOMERS**

**Banking Services Consumer Codes Review Group  
May 2001**



# FOREWORD

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30 May 2001

I enclose the report of our Review Group on Banking Service Consumer Codes, which you set up last November as part of the Government's response to the Cruickshank report on competition in UK banking. You asked us to examine whether the voluntary codes for banking and mortgages were delivering sufficiently strong benefits to consumers, and to recommend changes, if necessary, in the codes' content or in the process for revising them.

In addressing this remit, we felt it was important to consider codes in their wider context. First, codes are only one instrument among the many legal and market pressures that determine the service standards of banks. We think the voluntary codes we examined generally have been effective at raising standards and spreading best practice, but they cannot be expected to prevent or solve all customer complaints. For some, better consumer education is the answer; for others, statutory regulation.

Second, both the regulatory and the competitive environment in which banks operate are changing rapidly in the UK at the moment. The internet has brought in new providers, especially for savings products and mortgages. The Financial Services and Markets Act 2000 will bring extensive reform of the statutory framework, including that for mortgages. An investigation is underway by the Competition Commission into the provision of banking services to small businesses. Many of the key bodies in this field – including the Financial Services Authority, the Financial Ombudsman Service and the two compliance monitoring boards – are new institutions which are still defining their own processes and establishing their credibility.

In such a complex and rapidly evolving system, we felt it was both unrealistic and unwise to aim to define the optimal code for financial services or the optimal set of regulatory interventions. Instead, the approach we took was to identify where changes can be made to shift the incentives facing consumers, banks and monitoring bodies in ways that would foster more effective competition and provide greater consumer benefits. Then these new incentives need to be left in place long enough to allow the system to respond to them and adapt accordingly.

The Group's overall assessment is that the voluntary consumer codes for banking and mortgages have delivered benefits to consumers. They should continue to be updated to deal with new concerns as the competitive and regulatory environment changes. The Banking Code, now in its fifth version, is something of an exemplar in this respect. However, the hiatus in code development that has arisen for the Mortgage Code and the proposed Business Banking Code due to potentially cross-cutting activities by the Financial Services Authority and the Competition Commission is regrettable. Gaps in consumer protection persist, especially for mortgage advice and for dealing with the concerns of small businesses. We recommend that an interim update of the Mortgage Code be introduced by November 2001 and the first Business Banking Code be introduced by March 2002.

The Group identified four areas where the codes relating to banking services for consumers should be improved. While we were not able to carry out a full cost-benefit evaluation of these recommendations, we have tailored the details of our proposals to minimise their costs to providers, subject to achieving the benefits for consumers. Our seven main recommendations are set out to deliver benefits in these four areas:

- Easier account switching
  - a new '5 day start – 5 week finish' standard for switching accounts
  - a portable credit history
- Better customer information
  - a new Customer Annual Summary Statement (CASS)
  - 3 code formats
- Clearer code review processes
  - biennial code reviews led by an independent Reviewer
- More information on code compliance
  - early publication of aggregate compliance data
  - eventual publication of individual compliance data

We believe these recommendations would help the market for banking services work more effectively and thereby deliver greater consumer benefits.

Our recommendations were developed after an extensive consultation process from which we benefited greatly. Our thanks go to all those organisations and individuals who contributed their ideas. We also particularly wish to thank our efficient and hard-working secretariat from HM Treasury, David Fairbrother, and his supervisors, Paula Diggle and Dilwyn Griffiths. Without their exceptional efforts, and those of my secretary at the Bank of England, Elaine Kalli, we could never have completed this task in the time available.

Finally, my personal thanks go to all the members of the Review Group (listed below) for the substantial time and unstinting dedication they have brought to this task over the past six months. We have spent a lot of time together, probably more than they bargained for when they agreed to serve. I have benefited enormously from their wide-ranging expertise and diversity of perspectives on consumer banking.

Each Group member served in his/her personal capacity, not as representatives of the organisations for which they work. The recommendations in this report reflect the majority view of the Group. But not every member can be expected to agree with every detail of those recommendations, nor should it be assumed that their organisations will endorse them. All Group members, however, have been equally committed to our common objective of making codes work better for bank and building society customers.

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Michelle Childs	(Consumers' Association)
Adrian Coles	(Building Societies Association)
Janet Connor	(Abbey National)
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# EXECUTIVE SUMMARY

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Banking services play a major, and ever increasing, role in our lives. Over ninety per cent of UK adults have some kind of bank or building society account<sup>1</sup>, and there are over eleven million mortgages in the UK<sup>2</sup>. These services provide crucial benefits, ranging from the day-to-day ease of paying bills, to enabling people to buy their own homes. Problems in the delivery of these services therefore have the potential to cause significant disadvantage to consumers.

The background to the establishment of our Review Group was the Cruickshank report<sup>3</sup> and the perception of widespread public discontent with the standards of banking services in the UK. Our Group did not find strong evidence of the latter. We did find evidence of consumer detriment in some well known areas, but this needs to be placed in the context of the large number of transactions that take place in these markets, the vast majority of which are conducted smoothly and satisfactorily.

We believe that the banking market is becoming more competitive and that service standards in banking can be effectively dealt with by voluntary regulation through consumer codes of conduct. The Banking Code, and the compliance monitoring that supports it, have delivered consumer benefits, and our recommendations in that area would strengthen them. Progress with a Business Banking Code has been slow, delayed in part by the Competition Commission inquiry into business banking. We recommend that the work underway on the Code be completed forthwith. For mortgages, we are convinced that the areas of detriment would be best addressed through statutory regulation. We believe the proposed statutory framework for mortgages will leave several regulatory gaps in consumer protection, and consequently the Mortgage Code should be updated and continue beyond N3<sup>4</sup> to cover these areas.

## RECOMMENDATIONS

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The Group's main recommendations are focused on four areas where we believe the voluntary codes relating to banking services for consumers can be improved without creating excessive costs or red tape for banks and building societies<sup>5</sup>.

We believe these recommendations, if implemented in full, would change the incentives for both customers and providers of banking services in ways that would make the market work more efficiently and deliver greater consumer benefits.

### Easier account switching

The current account is the foundation, for most consumers, of their banking service relationships. Therefore, effective competition amongst current account providers is uniquely important. We found considerable concern amongst consumers about problems, and perceived problems, of switching current account providers. Considerable barriers remain which inhibit those dissatisfied with their account provider from moving – such barriers primarily centre around the “hassle factor” of changing payment instructions, and the fear that things will go wrong. The Cruickshank report found that one in seven people who switched current account providers encountered problems. To facilitate easier account switching, we therefore recommend the following:

- ***Recommendation 1: a new standard for switching accounts***

*When a personal customer wants to switch current account to a new bank, the old bank should provide a five day guarantee to transfer customer information to the new bank. All banks should publish the average time it takes them to complete the transfer process for a new customer and they should commit to a five week target for the end to end process by the end of 2002. The Banking Code Standards Board should monitor compliance with this new '5 day start – 5 week finish' standard.*

- ***Recommendation 2: a portable credit history***

*At the customer's request, their current bank should provide their 'positive data' credit history to any other bank that the customer specifies.*

### **Better customer information**

There is evidence that consumers are not being informed about the codes as well as they could be. Customers lack clearly presented information about their accounts, which frustrates financial planning and inhibits them from comparing their products against alternatives. We therefore recommend:

- ***Recommendation 3: Customer Annual Summary Statement (CASS)***

*Every bank customer should receive a personal statement summarising the total charges paid and interest received on their current accounts, savings accounts, personal loans and credit cards for each tax year (ending 5 April) before the end of June.*

- ***Recommendation 4: three code formats***

*Codes should be produced in three formats: a leaflet, the full code; and guidance notes. The leaflet should be distributed biennially to all current account and mortgage holders, while the full code and guidance notes should be readily available to anyone who wants them.*

### **Clearer code review processes**

While the process for revising the Banking Code has worked reasonably well, the experience with the Mortgage Code and the Business Banking Code has highlighted some of the problems with an informal, industry controlled process. We therefore recommend:

- ***Recommendation 5: biennial code reviews***

*The code review process should be formalised, made more transparent, and led by an independent 'Reviewer'.*

### **More information on code compliance**

The Group believes there are benefits to be gained from greater disclosure of compliance data. This applies both at an aggregate level and at an individual firm level. Disclosing data at an aggregate level can give codes credibility by showing the extent to which they are complied with. Publication of individual firms' compliance data would enable customers to make better informed choices amongst providers for products, and also provide a powerful

incentive to firms to improve their internal compliance procedures. However, we recognise such a grading system must be developed carefully to be both fair and objective. We therefore recommend:

- ***Recommendation 6: published aggregate compliance data***  
*Aggregate data on compliance with key code provisions should be published by the monitoring bodies*
- ***Recommendation 7: published individual compliance data***  
*The monitoring boards should develop an objective formula to rate code compliance by individual institutions and publish the results.*

### Further recommendations

In addition to our seven broad recommendations, we have five further recommendations designed to target specific problems we have identified.

Both the Banking Code and the Mortgage Code currently have impressive coverage, with the vast majority of providers in each market subscribing to the relevant code. However, with new entrants expected to increase in the future, it is important that these institutions do not seek to avoid subscribing to the relevant code and the significant safeguards that these provide to consumers. We therefore recommend:

- ***Recommendation 8: universal coverage of codes***  
*All banking services providers should sign up to the relevant code(s).*

The postponement in updating the Mortgage Code has meant several issues have not been fully addressed. However, the Mortgage Code will also have to undergo a full revision once the Financial Services Authority rules are finalised. We therefore recommend:

- ***Recommendation 9: an interim Mortgage Code***  
*The Mortgage Code should be updated to address key outstanding issues by November 2001. A full review of the Mortgage Code should begin once the FSA rules are finalised.*

As part of its reform of financial services regulation, the Government has brought together several previously separate ombudsman schemes into the Financial Ombudsman Service. However, mortgage intermediaries are not required to be part of this scheme, and consumers seeking redress against intermediaries have to use a different route. We therefore recommend:

- ***Recommendation 10: mortgage intermediaries to be covered by the FOS jurisdiction.***  
*Mortgage intermediaries not already covered by the FOS jurisdiction should submit themselves to this voluntary regime as soon as is practicable.*

Poor treatment can have a particularly damaging effect on individuals already burdened with financial difficulties. There is evidence that financial institutions do not always deal appropriately with these individuals. We therefore recommend:

- *Recommendation 11: a better deal for those in financial difficulties*

*The guidance notes to the Banking Code should be revised to spell out key practices which are consistent with the Code principles on the treatment of people in financial difficulties. The revised Guidance should be re-issued to subscribers by November 2001.*

The Banking Code has provided considerable safeguards to personal consumers since its introduction. We believe these principles should be extended to small business banking customers. We therefore recommend:

- *Recommendation 12: a Business Banking Code*

*The work that has already taken place on creating a Business Banking Code should be completed on schedule and a first edition of the Code introduced by March 2002, with subsequent reviews and revisions following the new biennial procedures.*

# INTRODUCTION

## THE ROLE OF CODES

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**1.1.** Codes of conduct are a form of market intervention. Like other forms of regulation, they are not a free good. Regulation can stifle innovation, and inhibit competition, ultimately leading to higher costs and/or lower quality for consumers. Any form of regulation must therefore be justified by demonstrating that the benefits it delivers outweigh the costs it creates.

**1.2.** Regulation can take many forms. Where regulation is deemed necessary, statutory regulation will often be the most appropriate vehicle. However, self-regulation can in some cases be a cheaper and more flexible way to achieve the same ends. Self-regulatory schemes may also be able to make better use of the expertise of those being regulated.

**1.3.** Self-regulation is normally associated with a 'code of practice'. Self-regulation can take a wide range of forms, from little more than a code of general practice without monitoring compliance at one end, to formal monitoring and disciplinary procedures that blur into statutory regulation at the other<sup>6</sup>. Voluntary codes can also be backed by reserve statutory powers<sup>7</sup>.

**1.4.** The Better Regulation Task Force has identified seven main policy objectives that can justify regulation<sup>8</sup>. Of these, two are of relevance to banking services: to promote the efficient working of markets; and to protect consumers, [employees] and vulnerable groups from abuse.

**1.5.** Regulation can serve as 'synthetic' competition by enforcing standards on suppliers that would be driven by competition under a perfectly working market. Indeed, the original rationale for the Banking Code in the Jack Report of 1989 was that the competitive forces in the industry were not strong enough to provide adequate standards of service in banking, and that these weaknesses were best addressed through a code of conduct rather than statutory regulation<sup>9</sup>.

**1.6.** In this respect, codes tend to provide a set of minimum standards, rather than standards of excellence. It needs to be recognised that there are limitations to what codes can do. Compliance with codes can be misinterpreted by consumers as a mark of service excellence when in reality codes represent a baseline below which subscribers will not fall.

**1.7.** Informational asymmetries are a problem in the banking market, as with supplier-customer relationships in other sectors, which can inhibit competition. Codes can also target this, by requiring greater and/or clearer disclosure from suppliers. However, providing customers with all the relevant information on their financial products can lead to 'information overload'. Research by the FSA<sup>10</sup> has found that few consumers read the product information they are given and those that do find the information confusing<sup>11</sup>. There is therefore a strong case for presenting consumers with only the key information, making it more likely that this information is assimilated. But this will be at the inevitable cost that some customers do not feel they have sufficient information.

**1.8.** Codes can also seek to address directly areas of anticompetitive practice, for example, prohibiting the adverse changing of product terms and conditions without prior warning.

**1.9.** Vulnerable consumers of financial services fall into three partially overlapping groups: those who have difficulty getting access to basic services such as current accounts; those who lack a basic understanding of financial matters; and those in financial difficulties.

Codes can provide protection to people in these situations, who may otherwise suffer further disadvantage. Codes can also play some role in consumer education, although broader issues of financial illiteracy cannot be dealt with through codes alone or simple disclosure rules.

**I.10.** Finally, an important ingredient of regulation through codes or otherwise can be to set out a system of redress for when things go wrong.

**I.11.** For codes of conduct to be effective, it is important that appropriate procedures and structures are in place. The National Consumer Council has set out the measures needed to make self-regulation work<sup>12</sup>. These include the opportunity for all stakeholders to participate in developing the code, sanctions for non-observance, and good publicity for the scheme. However, structures in themselves are never the most important element in making a voluntary system effective. The industry needs to be committed to the regime, to ensure that the code is kept up to date, and that the code provisions are adhered to. Strong trade bodies make this more likely.

**I.12.** Consumer codes of conduct are used, to varying degrees, in many countries. The UK tends to make more use of codes than continental European countries (although in Scandinavia there is a strong tradition of ombudsman schemes). The US is not a major user of voluntary codes, tending to prefer the clarity of either regulated or non-regulated industries. Codes of conduct are used extensively in Australia, often backed by statutory provisions. The Australian banking services market is similar in structure to the UK, and so serves as a useful comparator<sup>13</sup>.

## THE KEY TRADE OFFS

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**I.13.** Regulation will almost inevitably have to face competing objectives, and consequently some trade off between these will be required. At a high level, one has to consider whether regulation – be it through a code or otherwise – should be simple and focus only on general principles to be followed, or instead set out detailed prescriptive rules.

**I.14.** At a theoretical level, simple principle based codes have many advantages. They allow flexibility in service delivery, thus enabling firms to deal with consumers as individuals and promoting competition through differentiation. However, judging compliance with such codes is often difficult and open to dispute.

**I.15.** Detailed prescriptive rules have the advantage of being clear. However, they can create inflexibility and threaten innovation. In addition, participants can often find loopholes in such rules, thus complying with the letter but not the spirit. This in turns leads to more detailed rules, which may be confusing for customers and further reduce the flexibility of providers.

**I.16.** A code has to manage provider and consumer considerations. Self-regulation is by definition regulation agreed by the industry. A voluntary code will only be viable if it is backed by the practitioners that have to abide by it. However, to command confidence amongst consumers, a code needs to be seen to address their legitimate concerns. No set of customer standards can be set without reference to consumers in some way. The mechanism for drawing up codes therefore needs to be able to deal with these sometimes conflicting considerations.

## THE GROUP'S REMIT

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**I.17.** The Banking Services Consumer Codes Review Group was set up in November 2000 by the Government as part of its response to the Cruickshank report. Cruickshank felt it was “inappropriate for the banks to determine the standards against which complaints against them are judged”<sup>14</sup>. The Review Group’s terms of reference<sup>15</sup> were to examine:

- whether the voluntary codes are delivering sufficiently strong benefits to consumers;
- what scope there is to introduce greater independence and consumer representation in the drawing up of codes;
- what role there is for the Ombudsman in influencing or determining standards for consumers; and
- whether greater information disclosure can be achieved without the need for further regulation.

**I.18.** This report sets out the results of our study. In light of the Competition Commission investigation into the provision of banking services to small and medium sized enterprises (SMEs) that has run concurrently with our review<sup>16</sup>, we decided at the outset to focus on the two personal banking service codes, that is the Banking Code and the Mortgage Code. The Business Banking Code is still in development, which has meant that it is not possible to judge its performance. There are also a number of other voluntary consumer codes in financial services which were not part of our remit. However, our recommendations on code mechanisms may be relevant to other voluntary codes, whether they be in financial services or other sectors.

**I.19.** The report is structured thus:

- chapter two provides an overview of the current retail banking market and the key participants in it;
- chapter three gives our assessment of how the current codes and participants operate in that market; and
- chapter four presents our recommendations for change.



**2.1.** The UK's financial services markets are large and diverse. As well as an heterogeneous set of consumers and producers, there are also a number of regulatory players, both relating to the voluntary codes and the statutory requirements in financial services. This chapter summarises the current situation.

**2.2.** However, it needs to be borne in mind that the situation is not standing still. The internet has facilitated greater market entry, especially for savings products and mortgages. The statutory framework is undergoing extensive reform with the implementation of the Financial Services and Markets Act 2000. An investigation is underway by the Competition Commission into the provisions of banking services to SMEs. Many of the key bodies, such as the FSA, the FOS, the BCSB and the MCCB are relatively new and will take time to have their full impact on how well the market works and how gains are shared between consumers and providers.

**2.3.** In such a complex and rapidly evolving system, it is unrealistic to aim to define the optimal code for financial services or the optimal set of regulatory interventions. A better approach is to identify where changes can be made to shift the incentives facing consumers, producers and monitoring bodies in ways that would foster more effective competition and provide greater consumer benefits. Then these new incentives need to be left in place long enough to allow the system to respond to them and adapt appropriately. Our Group was well aware that the adaptation process to recent regulatory and market changes is proceeding rapidly in retail banking, as this chapter sets out.

### CONSUMERS

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**2.4.** Consumers of retail financial services are by no means an homogenous group. Research for the FSA<sup>17</sup> found that financial decision makers vary in terms of:

- attitudes to financial matters;
- confidence in dealing with financial matters; and
- consumption of financial services.

**2.5.** The vast majority of UK households have financial products of some kind, and most financial decision makers have at least a rudimentary understanding of financial services, although this varies between products. However, many individuals and households lack specific types of financial services. For example<sup>18</sup>:

- 6 per cent to 9 per cent of adults have no bank or building society account of any kind;
- 15 per cent to 23 per cent of adults lack a current account;
- 31 per cent to 37 per cent of households have no savings or investment products; and
- 29 per cent have no credit products from a mainstream provider.

**2.6.** This profile of financial services consumers is likely to change significantly in the near future. There is a general trend towards greater financial self-reliance, which, coupled with rising household wealth, will increase the proportion of the population with savings products. Banks are marketing 'private banking' services to middle income, as well as affluent

clients in an attempt to expand the range of products sold. At the other end of the scale, benefit payments are due to be paid directly into recipients' bank, building society or Post Office accounts from 2003 and government sponsored efforts are underway to spread the availability of 'basic bank accounts'. Consequently, the penetration and use of banking services is expected to rise rapidly in the coming decade.

**2.7.** Coupled with initiatives to promote financial inclusion<sup>19</sup>, is a drive to increase financial literacy, with a number of initiatives underway from the FSA and the government. The primary focus of this work is on school aged children, so the main benefits will accrue over the long term rather than immediately.

**2.8.** As financial understanding has increased, so have consumers' expectations, with higher levels of service increasingly demanded. This trend too can be expected to continue.

**2.9.** There are over three and a half million small businesses in the UK<sup>20</sup>, all of whom require banking services. Small business customers vary markedly, depending on the scale and type of their business. Most small business owners will require both personal and business banking services, and a number of sole traders operate their businesses through personal accounts. Many of the same services are required by both personal and business customers, although the intensity with which they use them, and the charges they face for these services, can be markedly different. In addition there is a range of services, for example, merchant acquiring, that are only of relevance to business customers.

## PROVIDERS AND PRODUCTS

**2.10.** Just as there are large variations across consumers of banking services, so there are many differences amongst providers of these services. At one end there are large multi-national companies; at the other one branch building societies employing a handful of staff, and sole trading mortgage advisors.

**2.11.** As in many other markets, larger players tend to dominate in the provision of banking services, but there are significant variations in the extent of this domination. Table 1 sets out the market shares of the 'big four'<sup>21</sup> banks for the main banking service products.

**Table 1. Market concentration<sup>22</sup>**

Product	Market share of big four
Current account	68%
Credit card	61%
Mortgage	23%
Savings account	19%
Personal loan	46%
Small business services	83%

**2.12.** The most concentrated market is that for small business services, which led in part to the Cruickshank recommendation that the Competition Commission investigate this market. Their report is expected in June 2001.

**2.13.** Of the personal retail products, the big four banks have a smaller share in the mortgage market, where building societies (some of which have now de-mutualised) have historically played a larger role. The mortgage lending market is still relatively concentrated, with five firms accounting for over fifty per cent of mortgage lending in 1999<sup>23</sup>. The mortgage broker market is more diverse, with over 10,000 registered broker firms<sup>24</sup>. However, again there is a considerable degree of market concentration – while there are no figures available

for market share, the MCCB estimate the largest forty of these employ around fifty per cent of the total number of advisors.

**2.14.** All of the personal retail markets, to varying degrees, have seen an increase in competition in recent years. The Cruickshank report found evidence<sup>25</sup> of shifts in market share in the credit card, personal loan and mortgage markets. The large proportion of remortgaging – around 30 per cent of the total market by value in 2000<sup>26</sup> – is also reflective of the robust competition in this market.

**2.15.** Some measures are being taken to increase competition in the current account market. The Banking Code now includes a commitment by banks and building societies to cooperate when customers decide to change providers. In addition, BACS are piloting a series of initiatives which should ultimately lead to the automated transfer of Direct Debit and standing order instructions when customers switch accounts<sup>27</sup>. However, switching rates remain relatively low compared to other markets. For example, a report by the DTI which studied a number of markets found that only six per cent of current account customers had switched providers, compared with, for example, thirty seven per cent of domestic gas customers and fifty three per cent of those with car insurance<sup>28</sup>.

**2.16.** While there has been a move toward greater product competition, there has also been a trend towards consolidation of the providers of retail financial products, with a number of mergers and acquisitions. In the main this has been between firms whose strengths lie in different markets, for example between ‘traditional’ high street banks and ‘traditional’ mortgage providers.

**2.17.** This trend is in part reflective of the blurring of product boundaries that is also occurring. For example, a number of providers now offer accounts which combine mortgage and current account functions. There has also been increased entry of foreign firms and credit is now more readily and cheaply available to higher risk groups.

## THE CODES

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**2.18.** The three codes considered by this Review are at different stages of development. The Banking Code has been in existence for a decade, and its fifth version came into force in January 2001. The Mortgage Code began in 1997 for lenders and 1998 for intermediaries. Work started on its revision in 2000, but the CML decided to suspend this until the FSA’s statutory rules were finalised. The Business Banking Code is still being formulated with a planned launch in March 2002, although a Statement of Principles for business banking was introduced in 1996, and a revised version comes into force on 1 June 2001. Table 2 sets out the main participants involved in the codes.

**2.19.** The ‘industry’ of banking service providers owns each code through the relevant trade bodies. For the Banking Code, this is the BBA, the BSA and APACS. For the Business Banking Code it is the BBA and APACS. The BSA plays little direct role as its members have minimal involvement in lending to businesses. The CML issues the Mortgage Code. It should be noted that the CML only represents mortgage lenders – mortgage intermediaries are not part of this organisation and therefore are not owners of the code, despite being bound by it.

**Table 2. Bodies involved in banking services consumer codes**

	Content	Monitoring	Enforcement	Redress	Communication
Industry bodies	*				⊕
Consumer bodies	⊕	⊕		⊕	⊕
Banks and mortgage firms	+	+		*	+
Compliance boards	⊕	*	*	⊕	+
FOS	⊕	⊕		*	⊕
OFT	⊕	⊕			
FSA	⊕				⊕
HMT	⊕				
DTI	⊕				
Media	⊕	⊕			⊕

Key: \* = lead player; + = major role ; ⊕ = some role

**2.20.** The codes are drawn up using similar processes. For the revision of the Banking Code in 2000, the process included:

- key stakeholders invited to make contributions through written submissions and bilateral meetings;
- representations sought from members of the public through a press release;
- consultation workshop held to consider main themes.

**2.21.** The process of drafting the Banking Code was overseen by a working party of banks and building societies and chaired by the BBA. The representations received were assessed against three criteria: the benefit to consumers; feasibility; and cost.

**2.22.** The Banking Code is produced jointly by the BBA, the BSA and APACS, and is now in its fifth version. It covers 136 banks and building societies, representing the vast majority of the industry. Subscription is not a condition of membership of any of the sponsor organisations – this would not be practicable for the BBA as a large proportion of its members are not involved in UK retail banking. The Code has evolved from a practitioner-facing document to a consumer-facing one. However, it has grown more detailed with each revision as the breadth and depth of coverage has increased and as consumers and practitioners have sought additional clarification.

**2.23.** The Mortgage Code is produced by the CML, and all of the CML's members subscribe. The Code covers 118 mortgage lenders, representing 98 per cent of the market, and over 10,000 broker firms. CML members will accept business only from intermediaries who subscribe to the Code, and therefore intermediaries are effectively required to subscribe.

**2.24.** The Statement of Principles for business banking was introduced in 1996 to assist SMEs when in financial difficulties. The decision to introduce a more comprehensive banking code for small businesses was made in the late 1990s. Some preliminary work was done while the latest revision to the Banking Code was taking place, and a full consultation process with key stakeholders was launched in the second half of 2000. The process is ongoing, and the BBA has announced that the Code is due to take effect from March 2002<sup>29</sup>.

## MONITORING BODIES

**2.25.** The monitoring of the codes has undergone a transformation in the last two years, with the establishment of the Banking Code Standards Board and the Mortgage Code Compliance Board. These bodies are considerably better resourced than their predecessor,

the Independent Review Body, and have better governance structures, including in-built 'public interest' majorities on both boards of directors.

**2.26.** The introduction of these new bodies has led to changes in the way the codes are monitored and enforced. Previously, compliance monitoring consisted simply of an annual declaration by each firm, signed by the chief executive. This has now been supplemented by compliance monitoring visits. Due to the large number of subscribers to the Mortgage Code, the MCCB uses a risk rating system to establish priorities for visits. Those with higher risk ratings – which tend to be larger firms as non compliance by these would cause detriment to more consumers – could potentially be visited as frequently as every six months. Very low risk firms are more likely to receive visits on a five or six year cycle<sup>30</sup>. The BCSB, which has far fewer subscribers than the MCCB to monitor, is conducting compliance visits to all firms over a two year cycle, although it is currently examining the possibility of moving to a risk based system.

**2.27.** The visits review the strength of the compliance framework in place, list identified breaches and record an agreed plan for changes. Subsequent visits take place if necessary to ensure remedial action has been taken. In addition, the boards carry out other compliance assessments, such as mystery shopping exercises.

**2.28.** Both boards have also established disciplinary procedures to deal with serious cases of non compliance. Both have the power to issue a warning or reprimand, and to suspend or cancel a subscriber's registration.

**2.29.** However, there are some differences in these procedures. The BCSB has chosen to focus on using public 'naming and shaming' of institutions when major breaches of the code occur, and has consciously not sought the power to fine institutions. The MCCB on the other hand has sought the power to fine institutions for non compliance. Consequently it has had to establish its disciplinary procedures very carefully to ensure they comply with the Human Rights Act 1998<sup>31</sup>.

## OTHER BODIES

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**2.30.** Issues of consumer redress in financial services are dealt with through the Financial Ombudsman Service. This is due to assume statutory powers at N2<sup>31</sup>, and has been formed from an amalgamation of eight previously separate schemes, most of which were voluntary industry schemes<sup>32</sup>. The FOS deals with complaints where the customer and financial institution have failed to reach agreement. It is free to the consumer, and the Ombudsman's decision is binding only on the financial institution, not the complainant.

**2.31.** The FOS will have a compulsory jurisdiction over FSA authorised firms<sup>33</sup>. In considering cases before it, the Ombudsman takes into account, amongst other factors, 'best industry practice'. The relevant code will be used to inform these decisions, even for cases where the financial institution does not subscribe to the code.

**2.32.** Mortgage intermediaries per se<sup>34</sup> will not be part of the compulsory FOS regime, although they can voluntarily submit themselves to it. The Mortgage Code Arbitration Scheme was set up in July 1997 for those subscribers that do not come under an Ombudsman scheme. As with the Ombudsman, it is a free service for consumers.

**2.33.** There are a number of other bodies involved in the broader picture of financial services regulation. The three main bodies – HM Treasury, the Financial Services Authority, and the Bank of England – set out their roles in a Memorandum of Understanding in 1997<sup>35</sup>.

**2.34.** Under the terms of the Memorandum of Understanding, HM Treasury is responsible for the overall institutional structure of regulation and the legislation which governs it. The Treasury also has broader concerns in financial services, as set out in its eighth objective “Securing an innovative, fair dealing, competitive and efficient market in financial services, while striking the right balance with regulation in the public interest”<sup>36</sup>. As part of this work, the Treasury has developed the voluntary ‘CAT’ standards for retail financial products.

**2.35.** The FSA’s objectives as set out in statute are to:

- a. maintain confidence in the UK financial system;
- b. promote public understanding of the financial system;
- c. secure an appropriate degree of protection for consumers; and
- d. contribute to reducing financial crime.

**2.36.** As part of addressing its consumer focused objectives, the FSA’s aim is to help consumers make informed choices and manage their finances better. Work to achieve this falls under two main headings:

- a. education for financial capability – to provide individuals with the knowledge, aptitude and skill base necessary to become questioning and informed financial consumers.
- b. consumer information and advice – to provide impartial information and generic advice to enable consumers to plan their finances and make informed choices. This work does not involve recommending individual products and services.

As part of this work, the FSA has issued a series of plain language booklets in a bid to help consumers make sense of their finances<sup>37</sup>.

**2.37.** The FSA also has statutory functions relating to other parts of retail banks’ business, such as retail investment products<sup>38</sup>. It also sets conduct of business rules, some of which are relevant to deposit takers.

**2.38.** In addition to its monetary policy activities, the Bank of England is responsible for the overall stability of the financial system and the effectiveness of the UK’s financial services. As part of the latter objective, it is involved in small business financing issues, and publishes a quarterly review of small business finance.

**2.39.** The DTI is involved in financial services issues as it has policy responsibilities on consumer and competition issues, including policy responsibility for the Consumer Credit Act. In October 2000, the DTI set up a task force on personal indebtedness. This reported to the DTI in April.

**2.40.** The OFT has a number of responsibilities which relate to financial services. Together with local Trading Standards Offices, it implements the Consumer Credit Act and has responsibilities relating to Unfair Contract Terms, and Competition Issues. Under Government proposals, the OFT would also be given specific powers to deal with competition issues relating to payment systems<sup>39</sup>. The precise nature of these powers is yet to be finalised, but it is envisaged that they will include ensuring price transparency and fair and open access to payment systems.

**2.41.** Following the 1999 DTI consumer white paper<sup>40</sup>, the OFT is also taking forward work on self-regulation and consumer codes. A consultation document was issued in February

2001<sup>41</sup> setting out proposals for the OFT's future approach towards endorsing codes of conduct.

**2.42.** The Competition Commission does not have any standing responsibilities relating to financial services, but is currently conducting two enquiries dealing with banking services. The first, the inquiry into the provision of banking services to SMEs, was launched in March 2000 in light of a recommendation in the Cruickshank report, and is due to report in June 2001. In addition, the Commission was asked to investigate the Lloyds TSB bid for Abbey National. The results of this inquiry are due in early June.

**2.43.** There are also non public sector bodies which form part of the wider regulatory picture. For example, the Finance and Leasing Association – whose members provide consumer credit – has a Code of Practice that mirrors the Banking Code provisions in this area. The General Insurance Standards Council similarly has a code for general insurance.

**2.44.** There are a number of other bodies whose broader responsibilities mean they have some role to play in financial services. The Department for Education and Employment plays a role in financial education, both for young persons and adults. And the remits of the bodies monitoring advertising – the Advertising Standards Authority, the Independent Television Commission, and the Radio Authority – cover the advertising of financial, as well as other products.

**2.45.** Consumer bodies play an important role in influencing the content of consumer codes in banking as well as many other sectors. They, along with the media, are a vital conduit for consumer concerns. Consequently they are important in monitoring compliance with codes, and also in highlighting areas of detriment to be tackled when codes are next revised.

**2.46.** As can be seen, there are a large number of actors involved in the issues that relate to banking services consumer codes. Ideally a regulatory system should avoid both gaps in consumer protection and duplication of regulatory authority. It is not clear that the current UK system achieves either. However, it is a system undergoing a rapid pace of change, where the roles and procedures of many of the key bodies are themselves evolving. The next chapter presents the Group's assessment of the strengths and weaknesses of the current system.



**3.1.** The background to the establishment of the Code Review Group was the perception of widespread public discontent with the standards of banking services in the UK. Our Group did not find strong evidence for this<sup>42</sup>. We did find evidence of consumer detriment in some well-known areas, as discussed below, but this needs to be seen in the context of the large number of transactions that take place in these markets, the vast majority of which are conducted satisfactorily. The percentage of bank customers whose complaints are unresolved by their own banks' procedures is very low.

**3.2.** While it is difficult to make quantitative comparisons, there are other areas where customer dissatisfaction is arguably more widespread than in banking services. An OFT survey<sup>43</sup> of consumers ranked problems with banks and building societies as the seventh greatest cause of detriment in the UK in 1999, behind, for example, food and drink, telephones, and utilities. Problems with credit cards came thirty-sixth in the list, while problems with mortgages and private landlords were forty-third.

**3.3.** However, the Group did find some continuing problems in banking services. The absolute size of consumer detriment is not really possible to quantify in any robust way. Even the relative size of problem areas is difficult to judge because some of the problems are 'broad' – i.e. affect a large number of consumers but only by a small amount; some are 'deep' – i.e. have a high marginal effect on a few individuals.

**3.4.** The Group took evidence from consumer groups and the general public on where consumer detriment was greatest in banking services. The results of our consultation exercise are summarised in Annex B. The areas cited most often were:

- treatment of consumers and small businesses in financial difficulty;
- problems, and fears of problems, with switching to another current account provider;
- complaints handling arrangements;
- unexpectedly high charges for some transactions, overdrafts and early repayment of some loans and mortgages; and
- interest paid on old ('superseded') savings accounts and business accounts with large positive balances.

**3.5.** The first area is an example of 'deep' detriment affecting a small number of consumers, while the last is a 'broad' detriment area affecting many consumers, but probably not by a large amount. In addition, the second area – difficulties in switching accounts – may be the root of other problems. If switching suppliers were easier, then dissatisfaction with low returns or high charges at a consumer's current bank could be more effectively addressed by changing banks. Competition would eventually drive out the poor payers, over chargers, or poor service providers.

**3.6.** As noted in Chapter 2, the codes covered by the Group's review are at different stages of development. Thus it is not surprising that their effectiveness in delivering benefits to consumers also differs. Our consultation exercise revealed much greater satisfaction with the Banking Code than with the Mortgage Code in this respect. Both industry and consumer groups agreed that mortgages should be subject to statutory regulation (as will be the case after N3) rather than covered by a voluntary code. Many believed that mortgage advice and

those who provide it should also be regulated by the FSA (which the Government has so far rejected). In the meantime it is felt that the Mortgage Code needs considerable updating and strengthening in order to protect consumers from inappropriate or misleading advice. It would also be advantageous to give mortgage intermediaries co-ownership of the Mortgage Code.

**3.7.** The Business Banking Code is at an even earlier stage of development. Its provisions are still under discussion, so it has not been possible for the Group to review its content, much less its effectiveness in delivering consumer benefits.

## THE BANKING CODE

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**3.8.** There is broad consensus that service standards in banking can be effectively dealt with by self-regulation. Indeed, our consultation exercise revealed that many feel the Banking Code, while not perfect, is an exemplar of self-regulation. The Banking Code has evolved over time in light of changing market conditions and customer needs. The consultation process for drawing up the Code is wide ranging, resulting in a code which addresses most of the key issues and has earned praise from consumer groups<sup>44</sup>. The areas of customer benefit that successive revisions to the Code have delivered include:

- abolition of unlimited loan guarantees;
- limitation of card liability to £50;
- pre-notification of bank charges; and
- customer self-selection of PINs.

**3.9.** Despite the overall satisfaction, we have some concerns about the process for drawing up the Code, notably:

- consultees do not have a sufficiently clear idea of the structure of the review process, including the timetable for review;
- feedback from those conducting the reviews is not systematic or transparent enough; and
- decisions on final Code content are not seen to have sufficient independent scrutiny.

**3.10.** We also have some specific areas of concern about the content of the Banking Code, notably on account switching and dealing with people in financial difficulty.

**3.11.** The latest edition of the Banking Code includes commitments to cooperate if customers decide to move their current accounts. However, there are still considerable barriers which prevent those dissatisfied with their account from moving – such barriers centre primarily around the “hassle factor” of moving Direct Debits, standing orders, etc, the time this takes, and a fear that crucial payments will be missed as a result. The Cruickshank report found that fourteen per cent of consumers who had switched current account provider had encountered problems.

**3.12.** Poor treatment can have a particularly damaging effect on individuals already burdened with financial difficulties. There is evidence that financial institutions do not always deal appropriately with these individuals. Specific problems include the imposition of punitive and unexpected charges, and a lack of respect for consumers’ right to first

appropriation (i.e. to decide in what order to pay off debts)<sup>45</sup>. The Code at present provides little guidance on what the commitment to deal “sympathetically and positively”<sup>46</sup> with customers in financial difficulties means. In addition, privacy rules mean it is not easy for the BCSB to obtain copies of individual customers’ files which have evidence of non-compliance. It is consequently very difficult for the BCSB to assess compliance with this Code commitment. Even where the Code is clear, there appear to be problems. For example, we have received evidence of failure by some institutions to adhere to the commitment to deal directly with debt counselling organisations acting on behalf of customers.

**3.13.** Historically, there have been concerns that even if areas were covered by the Code, compliance by providers tended to be poor. The Independent Review Body which monitored compliance with the Code until 1999 was seen to be insufficiently funded and too closely tied to the industry to have credible independent ‘bite’, and was consequently replaced (for the Banking Code) by the BCSB. The BCSB’s short existence means it has not yet had the chance to establish a track record of effectiveness and hence credibility. However, we believe that the resources and governance structures that have been put in place provide a framework for the BCSB to carry out its current monitoring and compliance functions effectively.

**3.14.** We agree with the BCSB’s decision not to seek the power to fine its members on the grounds that reputational risk via “naming and shaming” presents a more powerful sanction for its members. We also welcome the BCSB’s early use of its powers of public censure, for example regarding customer self-selection of PINs.

**3.15.** An area of continuing concern is the interest paid on ‘superseded’ accounts. We welcome the strengthening of the provisions in this area in the latest edition of the Banking Code, and the action the BCSB has subsequently taken<sup>47</sup>. This has resulted in a number of providers increasing the rate of interest paid on such accounts. We look to the BCSB to continue to use its powers of discipline effectively where serious breaches in this, and other areas of the Code, occur.

## THE MORTGAGE CODE

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**3.16.** As with the Banking Code, the Mortgage Code has delivered a number of customer benefits, including:

- constraints on poor intermediaries;
- enhanced information disclosure to borrowers; and
- free redress arrangements for all borrowers.

**3.17.** However, we are concerned that self-regulation is not a sufficiently strong regime for service standards for mortgages. Mortgages involve a long term commitment and for many consumers represent their largest financial undertaking. Therefore, for those who want it, the provision of good quality, unbiased advice is essential. We note the Government has already conducted a wide ranging consultation exercise on its proposals for mortgage regulation. However, we remain concerned that the proposals for statutory regulation, with their focus on disclosure, will fall short of what is required. In particular, we feel the statutory regime should cover mortgage advice, and that intermediaries should be regulated directly. We are also concerned that the split in regulatory regimes, between statutory FSA requirements, the Mortgage Code, and in some cases Consumer Credit Act requirements, could present the problems of regulatory overlap in some areas and gaps in consumer protection in others.

**3.18.** Given the statutory regime that has been agreed to date, we believe there will be an ongoing need for the Mortgage Code in some form, as the FSA itself has indicated<sup>48</sup>. We believe that post-N3, areas the Mortgage Code will need to address include<sup>49</sup>:

- advice on the repayment method (not currently covered);
- advice on the product;
- advisors' training and competence;
- firms' fitness and propriety; and
- marketing.

**3.19.** Our concerns about the process for drawing up the Banking Code apply equally to the Mortgage Code. In addition:

- the CML decided to delay reviewing the Mortgage Code (pending greater clarity over mortgage regulation) against the near universal opinion of non-industry stakeholders;
- CML's advocacy of statutory regulation of mortgage advice makes it difficult for them to be committed to the Mortgage Code; and
- intermediaries, despite being bound by the requirements of the Code, are not formally involved in its approval.

**3.20.** As with the Banking Code, the Mortgage Code contains little detail on the treatment of those in financial difficulties, and we feel it needs to be strengthened in this area if the FSA's post-sales rules do not cover this from N3. In addition, the CML's Statement of Practice on Handling Arrears and Possessions has become outdated. While the CML has also produced an agreement on the pursuit of mortgage shortfall debts (limiting this to no more than six years), this is not yet part of the Code requirements. We note the CML has stated its intent to deal with the last two issues in the next revision of the Code.

**3.21.** As with the BCSB, the establishment of the MCCB to monitor and enforce the Mortgage Code has provided resources and governance structures which are a considerable improvement on the previous arrangements with the Independent Review Body. The MCCB can point to areas where it (in conjunction with the CML) is delivering consumer benefits, for example, raising the standards of intermediaries through tougher registration rules and training requirements. We particularly welcome the latter which should go some way towards raising the standards of mortgage advice.

**3.22.** In contrast to the BCSB, the MCCB has sought the power to fine members. There are strong arguments for this – the MCCB has many smaller members for whom the fines would be a serious penalty, arguably more so than public censure. However, the need to comply with the requirements of the Human Rights Act has meant the MCCB has had to spend considerable time and energies setting up its disciplinary procedures, and these became functional only in early 2001. The MCCB needs to show these disciplinary procedures can produce real results if it is to establish credibility as an enforcement body.

## THE BUSINESS BANKING CODE

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**3.23.** As already noted, the Business Banking Code has not yet been finalised, let alone come into force. There are clearly problem areas in small business banking, some of which may be addressed by the Competition Commission review. However, we believe that many of

the benefits delivered over the years to personal consumers by the Banking Code have their counterpart in the small business market for banking services. Thus it is regrettable that there has not been greater urgency in the development of a banking code for small businesses. We believe it could bring benefits alongside, and possibly in advance of, whatever remedies the Competition Commission may propose.

## OVERALL ASSESSMENT

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**3.24.** The Group's overall assessment is that the voluntary consumer codes for banking and mortgages have delivered benefits to consumers. They should continue to be updated to deal with new concerns and changes in the competitive and regulatory environment.

**3.25.** Compliance monitoring has improved with the creation of the BCSB and MCCB. In principle, they have sufficiently independent governance structures and are well enough funded to deal effectively with their current responsibilities. In practice, both are new bodies and have yet to establish a record of success in improving compliance across the industry, enforcing change on institutions found to be significantly non-compliant, and raising standards across the board. The data on individual banks that are generated by the current system of site visits are not of a high enough standard to permit publication nor, in most cases, to serve as the basis for public reprimand. Both organisations intend to improve this and both are experimenting with new approaches to raising industry standards.

**3.26.** The Financial Ombudsman Service is also a new body, which is likely to assume statutory powers only later this year. As the successor organisation to several well-functioning, but separate ombudsman schemes, it is reasonable to expect that it will continue to provide timely and adequate redress for consumers who have exhausted the complaints procedures of their bank. However, this can only be assured once the FOS has had a reasonable period to establish a record of cases.

**3.27.** The hiatus in code development that has arisen for the Mortgage Code and Business Banking Code due to potentially cross cutting activities by the FSA and Competition Commission is understandable but regrettable. Gaps in consumer protection persist, especially for mortgage advice and for dealing with the concerns of small businesses.

**3.28.** In addition, our consultation process revealed that many customers feel inadequately equipped to make sound financial decisions. They do not find it easy to get the information they need when they need it and in a form they can understand. They are often not aware of the protections and remedies provided by the relevant consumer codes. As a result, they are reluctant to change banks, even when they are dissatisfied. Codes cannot resolve all of these problems – better financial education and a more pro-active approach by consumers are also needed – but codes can go some way further towards empowering consumers to act in their own best interests.



# 4

## RECOMMENDATIONS

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**4.1.** The Group believes there are four areas where the voluntary codes relating to banking services for consumers can be improved without creating excessive costs or red-tape for banks and building societies. Our main seven recommendations are set out below to deliver benefits in these four areas:

- easier account switching;
- better customer information;
- clearer code review processes; and
- more information on code compliance.

**4.2.** We believe these recommendations, if implemented in full, would change the incentives for both consumers and providers of banking services in ways that would make the market work more efficiently and deliver greater consumer benefits.

**4.3.** Consumers would be more inclined to switch banks if they were dissatisfied, because the hassle and uncertainty around moving their accounts would be reduced. Consumers, and the newspapers they read, would have new information on banks' performance to help them compare and choose among providers. They would have clearer information on what the code commitments mean to them. They will also receive a regular summary statement of the actual charges they have paid and the total interest they have received, where applicable, from their current bank each year. This should prompt them to shop around for better terms, as they currently do, for example, with car insurance and gas supply.

**4.4.** Trade bodies would share the responsibility for reviewing and updating the codes with consumer groups and others. This would give them greater legitimacy, while the final code approval would remain with the industry. Greater disclosure of code compliance data would improve performance and discourage free-riders.

### EASIER ACCOUNT SWITCHING

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- *Recommendation 1: a new standard for switching accounts*

*When a personal customer wants to switch current account to a new bank, the old bank should provide a five day guarantee to transfer customer information to the new bank. All banks should publish the average time it takes them to complete the transfer process for a new customer and they should commit to a five week target for the end to end process by the end of 2002. The BCSB should monitor compliance with this new '5 day start – 5 week finish' standard.*

**4.5.** We believe that effective competition is at present inhibited by the real and perceived hassle involved in switching current accounts. Whether the new bank or the customer is managing the switch, a considerable time lapse occurs as the list of mandates for Direct Debits, authorised payments and credits is received from the old bank, and as these are changed with the originators (e.g. utility companies, loan companies) and others such as employers. It is not unusual for the process to take twelve weeks<sup>50</sup> and to result in missed or mistaken payments by either the old or the new bank. This process needs to be made simpler and surer for the customer.

**4.6.** We recognise that the process is inherently complex and involves banks, most of whom subscribe to the Banking Code, and originators and creditors, most of whom do not. Broadly speaking, the stages involved in a single current account switch carried out by the new bank on the customer's behalf are:

- a. customer approaches new bank;
- b. new bank requests regular payment details ('customer mandates') from old bank;
- c. old bank provides details;
- d. customer checks details;
- e. new bank notifies originators of change of account;
- f. originators amend their records;
- g. new bank receives confirmation that originator has changed records;
- h. new bank instructs old bank to cancel regular payment instructions;
- i. old bank cancels regular payment instructions.

There is clearly a potential for delay at each stage of the process.

**4.7.** The first stage, involving the exchange of information on customer mandates, is purely an inter-bank communication, and so standards here can be determined under the Banking Code. We believe the current standard of ten days is excessively long given modern communication techniques. We therefore recommend that the old bank should provide a full list of mandates to both the customer and the new bank in no more than five working days from the date of request. We note that some providers are now committing themselves to speedier targets than this<sup>51</sup>.

**4.8.** The current account is uniquely important, both in terms of the crucial set of transactions it provides for the individual customer, and also in terms of its impact on competition in other banking services. We therefore believe it is appropriate that an automatic £50 penalty, payable to the customer, be imposed for a breach of the five day rule. We do not see this as setting a precedent for breaches in other areas of the Banking Code. As noted in Chapter 3 we believe the BCSB is correct in not seeking to use fines as part of its disciplinary procedures.

**4.9.** We recognise that delays in the provision of the list of mandates may not always be the fault of the old bank. However, where there are delays, the old bank should pay the penalty immediately to the customer, and any dispute should be sorted out separately, "behind the counter" between the agents.

**4.10.** In terms of time required, the main part of the switching process involves the transfer of payment and credit instructions once the new bank has received details of them. There are some 16,000 originators<sup>52</sup> (i.e. those who take Direct Debit or standing order payments). Similarly, there are many hundreds of thousands of employers and others who pay salaries and other credits directly into current accounts. It is important to recognise that the time it takes these institutions to deal with transfer requests plays a central role in determining the total time the account transfer takes. The problems of switching accounts will never be fully resolved without this part of the process being properly addressed.

**4.11.** The vast majority of these institutions are not banks or building societies, and therefore are not bound by the Banking Code. However, the industry can still work to produce improvements in this area. The automated transfer of Direct Debits and standing order instructions, currently being piloted by BACS, and due to be introduced in full in November 2001, will be an important contributor to this. The industry should continue to look for further ways of making improvements, for example:

- looking at ways in which time limits can be enforced on originators;
- originators should be required to deal with the new bank (rather than directly with the customer) where the customer has given permission to the new bank to act on his/her behalf; and
- information required from banks, originators and others should be standardised to assist clear communication and ensure a 'right first time' approach.

**4.12.** For the customer, the key concern is how long the end-to-end process to switch accounts will take. The longer this process takes, the greater the deterrence to switching. We therefore recommend that the BCSB should monitor the average time it takes its subscribers to complete a switch, and publish these data on an individual firm basis every six months. This would improve customer information in this area, and encourage competitive pressures to speed up the process.

**4.13.** Looking ahead, once the automated transfer of Direct Debit and standing order payment instructions is complete, we believe the industry standard for completing the switch should be set at no more than eight weeks. However, we recommend the industry continue to look for further means by which the process could be speeded up. We note that APACS is looking at a three week average time for the full switch to take place<sup>53</sup>. Given this, we believe it is reasonable that all switches could be completed within five weeks by the end of 2002. The BCSB should monitor compliance with this standard and look for ways in which further improvements could be made.

**4.14.** This 'five day start, five week finish' standard would only apply to the transfer of personal accounts. We recognise that account switchability is also important for small businesses. However, the transfer of business accounts is inevitably a more complex process, and so we do not believe it would be appropriate to apply this standard to them. We note the Competition Commission is looking at assistance in switching as one of the possible remedies in its investigation into banking services provided to SMEs. We expect that many of the methods developed to improve switching in the personal market will also be applicable to the business account market.

- *Recommendation 2: a portable credit history*

*At the customer's request, their current bank should provide their 'positive data' credit history to any other bank that the customer specifies.*

**4.15.** A further barrier to account switching can be the burden on the customer to prove his/her positive credit history. The new bank may require this before it will grant the same terms and conditions that had been established over time with the old bank (e.g. overdraft limits). This credit history, or 'positive data', includes the date the account was opened, its overdraft limit, whether the customer is currently utilising the overdraft, and whether the account has operated within its terms and conditions.

**4.16.** Such data establish the customer's track record of good performance and, although held by the old bank, rightly belongs to the customer. We recognise that for a variety of reasons, including privacy, customers may not want these data shared, and therefore this should only take place at the customer's request.

**4.17.** When such a request is made, we suggest the target for providing this should be five working days, so that the provision of this occurs simultaneously with that of mandate details (assuming both sets of data are requested simultaneously).

**4.18.** This issue is likely to be of even greater importance for small business customers, and therefore we recommend a similar requirement is incorporated into the forthcoming Business Banking Code.

## BETTER CUSTOMER INFORMATION

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- *Recommendation 3: Customer Annual Summary Statement (CASS)*

*Every bank customer should receive a personal statement summarising the total charges paid and interest received on their current accounts, savings accounts, personal loans and credit cards for each tax year (ending 5 April) before the end of June.*

**4.19.** Despite the vast array of financial information available, consumers still find it difficult to get hold of the information they need to make informed decisions about their own finances. Even assembling the baseline data on the accounts they currently hold, including the interest and charges they are paying, can be difficult for many customers.

**4.20.** The Group therefore recommends that consumers should be provided with an individualised customer annual summary statement (CASS) detailing the costs and benefits of the banking products that they hold. This annual information would act as a prompt to consumers to review their finances at least once a year, and so potentially encourage better financial planning. It may also promote competition by triggering switching, as consumers would be able to see clearly their annual charges and interest paid and received, and banks would be able to highlight any competitive advantages they may have.

**4.21.** There are considerable benefits for the consumer in receiving all of this information at around the same time. This would enable consumers to have a 'spring clean' of their finances. If the information from different products and different providers reaches them at differing times of the year, this process will lack focus, and would probably fail to add benefit for most consumers. In addition, a 'switching season' may promote competition amongst providers similar to that seen amongst ISA providers near the end of the tax year.

**4.22.** However, set against these benefits, there are potential problems for banks of 'peak loading'. Issuing such statements simultaneously would put pressure on printing services, delivery channels, and call centres. More generally, the provision of a CASS, whatever its timing, would result in systems costs which would ultimately be borne by customers.

**4.23.** On balance, we believe that the CASS should be provided at the same time of year. To ease the problem of peak loading, we recommend that CASS be sent out between the beginning of April and the end of June, giving three months for the information to be processed and disseminated. Its mailing could be combined with other customer mailings during that period. A June deadline would also ensure self-assessment tax payers received the information in time for their form preparation<sup>54</sup>.

**4.24.** The Group recommends that a CASS covers the following products: current accounts; savings accounts; loans; and credit cards. The exact information provided for each product should be devised in consultation with relevant bodies, including the FSA and consumer organisations. As a prompt for discussion, Table 3 sets out suggestions for the information that should be provided. We recognise that annual statements are already provided for savings accounts, and that implementation of this recommendation is likely to affect only the timing of these statements. We recommend the CASS be introduced by June 2002.

**Table 3. Suggestions for data provided by the CASS**

<b>Current accounts:</b>	<b>Savings accounts:</b>
the AER on credit balances	the interest rate earned
the amount of interest earned over the year	the total amount of interest earned
the amount of interest paid over the year	the total amount of any penalties charged
the amount paid in overdraft charges	
<b>Personal loans:</b>	<b>Credit cards:</b>
the interest rate applied (if variable)	the APR
the amount outstanding	total interest paid
the total interest paid	total charges paid

**4.25.** As noted in Chapter 3, the mortgage market has shown itself to be competitive and consumers have demonstrated an increasing willingness to switch mortgage providers. As one of the prime aims of the CASS is to increase competition, the benefits of introducing it in the mortgage market would therefore be more limited. In addition, annual statements are already required for mortgages, and there seems little value in changing their timing. However, we note the FSA is looking at the value of providing post-sale information as part of its mortgage regime, and therefore we look to it to consider whether there should be changes to the way in which these data are provided.

**4.26.** We believe a CASS may also add value in the small business banking market in promoting competition between providers, and would therefore suggest a CASS for business bank accounts also be considered once the Competition Commission has reported.

- *Recommendation 4: three code formats*

*Codes should be produced in three formats: a leaflet, the full code and guidance notes. The leaflet should be distributed biennially to all current account and mortgage holders, while the full code and guidance notes should be readily available to anyone who wants them.*

**4.27.** We do not believe a ‘one size fits all’ system of producing and distributing codes is effective. People who are given relevant information at the appropriate time may still fail to appreciate it if it is presented in the wrong format. Moreover, as we noted in Chapter 1, there is an inevitable trade-off between a simple, principle-based code that the customer can understand and a detailed, prescriptive code that provides clear guidance for banks to ensure that their staff can be trained to comply with code commitments.

**4.28.** The existing arrangements for both the Banking Code and the Mortgage Code recognise this in different ways. We believe by combining the best elements from both of these systems, and improving the distribution of this information, consumers and others would be more knowledgeable about the codes and their provisions.

**4.29.** We therefore propose codes should be produced in three formats, each to suit different needs, and distributed at different times and in different ways.

**4.30.** Firstly, there should be a brief leaflet, similar in style to the existing “You and your mortgage” document. This should set out: (1) customers’ rights and responsibilities (the principles at the start of each code); (2) how to complain; and (3) how to obtain a copy of the full code.

**4.31.** This would be distributed when accounts are opened, credit cards taken out, mortgages are applied for, etc. We also feel this should be sent<sup>55</sup> to existing customers on a regular basis, as financial products (not least current accounts) can be held for many years. However, we recognise this would have cost implications; there are, for example, around thirty-eight million current accounts in the UK<sup>56</sup>. We therefore recommend that the leaflet should be distributed on a biennial basis following the codes’ revision (see recommendation 5) to current account holders for the Banking Code and mortgage holders for the Mortgage Code. Similar arrangements should be put in place for business bank account holders once the Business Banking Code comes into force.

**4.32.** As nearly all those who have credit cards and personal loans will also have current accounts, we see no need to duplicate distribution of the leaflet to those customers. In addition, the vast majority of savings account holders will also have current accounts, and individuals often hold several savings accounts. We recognise that there are currently a significant number of people who hold savings accounts but not current accounts, and that this group will be heavily weighted towards the most financially vulnerable. However, this population can be expected to decrease markedly in the near future with the introduction of Universal Banking Services. This will give people currently without any banking facilities access to a new post office based card account or one of the banks’ basic bank accounts through the post office network<sup>57</sup>. We therefore do not recommend that the Banking Code leaflet should be distributed to product holders other than for current accounts.

**4.33.** The second document would be the full code. This should be aimed primarily at customers, although it would also serve as a quick reference guide for front line staff. It should be in ‘plain English’ (as the Banking Code currently is), and should be largely a principle-based document. It should be seen as a reference document for customers to turn to if they feel they have a complaint. It should be available wherever accounts, etc can be opened, including the internet, and on request.

**4.34.** The final document would be the detailed guidance notes on the code. These would be primarily for financial services firms and their staff, but would be publicly available on request and via the internet. They should also be distributed to other relevant bodies, such as money advice organisations. These should be seen as non-exhaustive guidance – i.e. institutions would be free to meet code commitments in other ways, but in such cases the burden of proof would fall on them if there were questions about compliance.

## CLEARER CODE REVIEW PROCESS

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- *Recommendation 5: biennial code reviews*

*The code review process should be formalised, made more transparent, and led by an independent ‘Reviewer’.*

**4.35.** While the process for revising the Banking Code has worked reasonably well, the experience with the Mortgage Code and the Business Banking Code has highlighted some of the problems with an informal, industry controlled process. It can be subject to delay when the industry bodies have competing priorities or face regulatory uncertainty. The Group therefore recommends that more formalised and transparent procedures be introduced for

drawing up the codes and that the process should be led by a Reviewer from outside the industry body.

**4.36.** We considered a number of ways in which non-industry representation in the review process could be increased:

- a. a more formalised and transparent consultation process is used to revise the code;
- b. the draft code is drawn up by the industry, then 'endorsed' by an independent body/person;
- c. an independent body/person consults stakeholders and puts forward proposals for the code, which are then publicly accepted or rejected by the industry; and
- d. the code is drawn up by an independent body with the industry having no veto over its provisions.

**4.37.** Chapter 1 discussed the trade off between supplier and consumer considerations in drawing up voluntary consumer codes. While we believe the measures in 4.36(a) would be a positive step forward, we think more needs to be done to ensure the process is seen to be effective.

**4.38.** The description in 4.36(b) is broadly the process the OFT is proposing to promote more effective self regulation across a range of industries<sup>41</sup>. Independent endorsement could give a code added credibility, while retaining many of the benefits of self-regulation. However, the exact nature of 'endorsement' can vary. If the content of the code is to be endorsed, then the determination needs to be made by a body or person who is an expert on the industry (e.g. the FSA). If it is only the process of drawing up or monitoring compliance that is being endorsed (e.g. by the OFT) then another layer has been added to the whole process without the issue of independent scrutiny of code content being addressed. Under the proposed OFT scheme, failure to receive OFT endorsement would not preclude an industry from going ahead with its code, although of course the code's credibility could be weakened.

**4.39.** Alternatively, the independent body could be given the absolute right of veto and the ability to demand changes. However, such a system could no longer be seen as self-regulation, as the subscribers would not have the ultimate right to determine by which rules they are governed. Participation in such a scheme could wane. The system set out in 4.36(d) would have similar drawbacks. We feel such systems can only be effective in a voluntary setting if there are very few participants in the market.

**4.40.** The system summarised in 4.36(c) is similar to the process currently used in Australia. This process allows the industry to retain 'ownership' of the code and thereby maintains industry support and commitment. By handing over the review process to an independent party, the industry frees itself of accusations that it controls the agenda to its own advantage. The requirement to explain any amendments proposed by the industry allows public scrutiny of the justification for any rejections. We recommend that this approach should be adopted in the UK.

**4.41.** We considered whether the review process should be done by an individual or a committee of stakeholders. As both would include wide ranging consultation to ensure stakeholder views were taken on board, the difference between these two models should not be overstated. We favour the individual option as this would be less bureaucratic. In particular, we feel it would allow the drafting process to get underway more quickly, and

facilitate greater flexibility in dealing with different stakeholders who will have differing degrees of interest in particular issues. The Reviewer would be supported by a secretariat, which we envisage would be provided through the trade bodies.

**4.42.** We also considered specifically whether the monitoring boards, with their inherent expertise of the issues involved, should control the review process. However, on balance, we feel it is important to retain the separation of powers between authorship and monitoring/enforcement, and therefore do not recommend that this route be taken. The monitoring boards would of course be key consultees in the review process.

**4.43.** It would be incumbent upon the industry to find an appropriate Reviewer, and we would expect them to do this in consultation with other stakeholders. We believe an important criterion is experience of the issues involved, and we would not preclude either serving or former board members of the BCSB and MCCB from filling these posts.

**4.44.** To start the review process, we would envisage the Reviewer would hold a roundtable of major stakeholders, including the industry, the relevant monitoring board, the Ombudsman, and consumer groups. This would enable the Reviewer to identify the main areas of concern and thus priority areas of work.

**4.45.** The Reviewer's consultation process would be conducted in full public gaze (except where consultees wish to remain anonymous). We would envisage this would include:

- advertisements in the press seeking views;
- a dedicated website;
- specific canvassing of organisations known to be interested in the review (including the industry);
- bilateral and roundtable discussions with all key consultees; and
- public meetings to gather the views of individual customers.

**4.46.** Having concluded this process, the Reviewer would present a public report to the industry setting out suggested areas for change in the code. While this would not be a full draft of the code, the Reviewer would have the discretion to recommend specific wording for any of the three code documents should he/she so wish.

**4.47.** The industry would then write the code documents in light of this report. Along with its publication of these, the industry would produce a report setting out its reasons for rejecting any of the Reviewer's recommendations. The revised code would then come into effect.

**4.48.** The Group considered how often the code review process should take place. The dynamic nature of the financial services industry means that issues which require urgent attention can arise on a regular basis. Indeed, in September 1998, in response to such pressures, a revised version of the Banking Code was issued only 18 months after the previous version had been introduced. However, there is a trade off between leaving issues unaddressed for too long, and creating continual uncertainty and costly changes to internal processes for banks.

**4.49.** On balance, we feel that the current cycle of reviewing the codes at least every three years is too long. We recommend that the codes should be reviewed every two years. Such a biennial cycle should result in most reviews leading to evolutionary changes in the codes rather than 'root and branch' reforms.

**4.50.** There should be an ongoing dialogue amongst stakeholders between reviews. The codes may benefit from clarification in certain areas within the two year time frame, and we would recommend that additions to the guidance notes could be made at any time if it is felt necessary. Similarly, if a full review process were deemed necessary ahead of the two year cycle, this should take place.

**4.51.** Table 4 summarises the stages we envisage in the review process. With the exception of the two years for the end to end process, the timings are for illustrative purposes. It should be for stakeholders to decide how much time is required for each stage. However, we believe it is important that there is a clear timetable for the review at its commencement.

**Table 4: the code cycle**

<b>Month 1</b>	<b>Revised code introduced</b>
<b>Month 12</b>	<b>Independent Reviewer appointed</b>
	<b>Timetable for review published</b>
<b>Month 13</b>	<b>Reviewer hosts roundtable of key consultees</b>
<b>Months 13-15</b>	<b>Consultation process</b>
<b>Month 17</b>	<b>Reviewer's proposals published and submitted to industry</b>
<b>Month 21</b>	<b>Industry publishes final code documents and report explaining any proposals it has rejected.</b>
<b>Month 25</b>	<b>Revised code introduced</b>

**4.52.** For the Mortgage Code, the 'industry' should consist of all those bound by the code, i.e. intermediaries as well as lenders. Under current arrangements, the code is drawn up by the CML without the formal approval of mortgage intermediaries, although they are bound by its provisions and pay the cost of its monitoring through the MCCB. We recognise that the large number of participants in the market makes it difficult to collect intermediaries' views. We recommend that intermediaries should seek to establish a way in which they could be represented, and if they can do this, be given co-ownership of the Mortgage Code with the CML.

**4.53.** The Ombudsman's position in handling complaints provides valuable insight into where codes may fail in unforeseen circumstances, and as such should continue to be a key consultee in the review process.

**4.54.** However, the Ombudsman's primary role is one of dispute resolution and we believe this should remain the case. There is a danger this function would be undermined if the FOS were asked to take too pro-active a role in standard setting, as it could neither guarantee industry commitment nor does it face the checks and balances of a regulator.

**4.55.** The Ombudsman has begun to issue guidance notes on issues where it detects a large number of cases may be emerging. The purpose of these is to explain how the Ombudsman is likely to treat cases that come before it. We believe these serve a worthwhile function, but it is important that they do not turn into 'back door' regulation. We also welcome the Ombudsman's moves to establish better and more frequent dialogue with stakeholders, through its newsletters and its proposals to establish quarterly bilateral liaison meetings with the monitoring boards and the trade bodies.

## MORE INFORMATION ON CODE COMPLIANCE

- *Recommendation 6: published aggregate compliance data*

*Aggregate data on compliance with key code provisions should be published by the monitoring bodies*

**4.56.** The Group believes there is value to be gained from greater publication of aggregate results from compliance monitoring. Currently both the BCSB and the MCCB publish some such data drawn from an analysis of the compliance forms completed by individual banks. The standards boards also receive detailed monthly assessments from compliance visits to their members. The Group recommends that aggregate information from these visits indicating key areas of compliance and non-compliance with the codes be published on a quarterly basis and collated in the boards' annual reports from 2002. The result of mystery shopping and other exercises assessing compliance with the code should also continue to be published.

- *Recommendation 7: published individual compliance data*

*The monitoring boards should develop an objective formula to rate code compliance by individual institutions and publish the results.*

**4.57.** The Group also believes there would be benefits from greater disclosure of compliance data on individual institutions. As noted in Chapter 2, publication of the names of non-compliant firms is part of the disciplinary procedure for both standards boards. However, this is viewed as a very serious sanction which is used only after exhaustive inquiry. Publication of all firms' compliance ratings – good, average and poor – would have the advantages of:

- enabling consumers to make better informed choices amongst firms for new products or when switching their accounts; and
- providing a powerful incentive to firms to improve their internal procedures so that their ratings, and consequent public image, improve.

**4.58.** Unfortunately, we do not think that the individual firm ratings now produced by the compliance boards are of publishable standard. There are a number of weaknesses with the current tests which could make the present ratings unreliable or misleading for consumers.

- Compliance visits are, currently, relatively short and cover only a small proportion of total outlets, products and services. A longer review would be necessary if the public is to have faith in the grading adopted.
- Full compliance assessment is difficult because the BCSB and the MCCB do not have access to consumer files, pending the outcome of consultations between the two compliance bodies, the Home Office and the Data Protection Registrar. It is therefore difficult to assess compliance with any aspect of the code that involves review of individual files.
- The MCCB's risk based approach used for compliance visits means that some institutions may only be visited at five or six yearly intervals. Consequently, these institutions' gradings would be out of date for a significant period of time between compliance assessments.

**4.59.** Consequently, we believe publication of the data at an individual firm level acquired under current compliance tests would be inappropriate. This points to the need to develop compliance tests which would facilitate the publication of such data – indeed, we believe

some of these weaknesses outlined in 4.58 should be addressed regardless of publication requirements.

**4.60.** We do not underestimate the difficulties of developing an objective and fair rating system. The methodology will need to be sufficiently simple to avoid a major increase in compliance costs, sufficiently robust to be meaningful and sufficiently objective to be free from legal challenge or dispute by the institutions involved.

**4.61.** However, we believe such a measure would have major benefits in increasing compliance and improving information available to customers. We therefore recommend that both the BCSB and the MCCB should seek to develop a system for publishing named ratings on subscribers' code compliance. To bring focus to this task, the standards boards should aim to have such a system in place within twelve months and, after a period of testing, to bring publication within twenty four months.

**4.62.** It is important that publication of such data be accompanied by a clear explanation of what it represented. For example, on the present system used by both boards, a green grading – the most favourable grading for a firm – is not evidence that the firm is totally compliant in all aspects with the code, but rather that a breach is relatively minor, and unlikely to result in significant consumer detriment. It would also be important to emphasise that the measure is not an assessment of prudential risk (i.e. not a measure of the safety of deposits), but of service standards.

**4.63.** There are particular difficulties in applying this recommendation to mortgage intermediaries. The large number of mortgage broker firms means it will be difficult to produce a timely rating of all these institutions, and so initially, at least, the system may need to be limited to the largest broker firms. In addition, the MCCB does not currently have the consent of intermediaries to publish their general details, and will therefore need to address this issue before it can publish the compliance ratings of those firms.

## FURTHER RECOMMENDATIONS

- *Recommendation 8: universal coverage of codes*

*All banking services providers should sign up to the relevant code(s).*

**4.64.** Since the Group began its work, National Savings has announced its intention to subscribe to the Banking Code by 31 March 2002<sup>58</sup>. We welcome this commitment and urge National Savings to see this through. As a major player in the savings sector, it is important that it adheres to the same standards expected of its major competitors.

**4.65.** Similarly we urge all other banking services providers to sign up to the appropriate code(s) if they have not already done so<sup>59</sup>. As noted in Chapter 3, while both the Banking Code and the Mortgage Code currently have impressive coverage, the number of new entrants is increasing as the markets become more open. It is important that these firms do not seek to avoid subscribing to the relevant code, either because they are unwilling to pay for the cost of compliance monitoring or because they are unwilling to commit to the minimum service standards and safeguards that the codes require. Non-subscription to the codes should be seen as a competitive disadvantage by consumers. The monitoring boards should promote this message.

- *Recommendation 9: an interim Mortgage Code*

*The Mortgage Code should be updated to address key outstanding issues by November 2001. A full review of the Mortgage Code should begin once the FSA rules are finalised.*

**4.66.** As noted in Chapter 3, under current government plans, we see a continuing role for the Mortgage Code once the FSA mortgage regime is introduced. A full review of the Mortgage Code, using the system in recommendation 5, should take place once the FSA mortgage rules are finalised to ensure the regimes dovetail and to prevent gaps and overlaps. We make some specific recommendations on the treatment of those in financial difficulties in Recommendation 11.

**4.67.** In Chapter 3 we highlighted several issues that had not yet been addressed in the Mortgage Code because of the delay in its revision. The CML has already done much of the work on these, including a preliminary consultation exercise last year. We think there is sufficient value to be added to justify completion of this work to produce an “updated” Mortgage Code ahead of N3. We envisage the update would include:

- a plain English version of the Code;
- codifying the agreement on pursuit of mortgage shortfall debts;
- Fitness and Propriety requirement for firms; and
- Fitness and Competency requirements for staff providing advice.

The last three of these measures have already been implemented outside of the Code. Bringing them together in the Code will raise the profile and importance of these. The plain English version of the Code will also help consumers to understand the rights the Code gives them.

- *Recommendation 10: mortgage intermediaries to be covered by the FOS jurisdiction.*  
*Mortgage intermediaries not already covered by the FOS jurisdiction should submit themselves to this voluntary regime as soon as is practicable.*

**4.68.** While all mortgage lenders will be covered by the FOS, mortgage intermediaries will not. To ensure that customers dealing with intermediaries receive the same levels of protection as those who deal with lenders, we recommend that the Mortgage Code should include a requirement that all intermediaries sign up to the FOS jurisdiction as soon as practicable.

**4.69.** We recognise that, with over 10,000 registered broker firms, this will require considerable resources, not least for the FOS, and therefore achievement of this objective will only be feasible in the medium term. In the interim, to highlight progress against the target, the MCCB should publish each year in its annual report the number of MCCB registered intermediaries that have and have not signed up to the FOS jurisdiction.

- *Recommendation 11: a better deal for those in financial difficulties*  
*The guidance notes to the Banking Code should be revised to spell out key practices which are consistent with the Code principles on the treatment of people in financial difficulties. The revised Guidance should be re-issued to subscribers by November 2001.*

**4.70.** As noted in Chapter 3, there is evidence that financial institutions do not always deal appropriately with people in financial difficulty. We believe clearer guidance would help banks improve their procedures, and improve the BCSB’s ability to assess compliance with these commitments.

**4.71.** The revision should be conducted in full consultation with representatives of advice agencies and consumer organisations and take into account the information gleaned from the BCSB's study of Citizen Advice Bureaux case reports on the treatment of customers in financial difficulties. Some of the key areas the Group would expect to see covered in the revised Guidance include:

- the importance of prompt referral of accounts to specialist debt recovery teams;
- the application of Code standards (and compliance monitoring) to third parties acting for the banks in the debt recovery process, e.g. debt collectors and enquiry agents;
- the importance of working with customers' nominated advisors and respecting customers' right of first appropriation; and
- the importance of giving named contacts on all communications.

**4.72.** It is not clear at the time of writing whether the FSA rules on mortgages will cover post-sale practice on handling arrears and repossessions or, if they do, in what way such rules may regulate practice. After N3, the scope of FSA rules could remove the continuing need for the provisions of the Mortgage Code dealing with customers in financial difficulties. In the meantime, we recommend the interim Mortgage Code (Recommendation 9) and its associated guidance notes include changes to the Statements of Practice on arrears and repossessions, to update these documents, including a reflection of changes in court procedures.

**4.73.** In the event that the FSA rules relating to handling arrears and repossessions do not cover all of the terrain currently covered by the Mortgage Code, the CML and FSA will need to work together to ensure that there is no diminution in consumer protection compared with the present regime. If the FSA proposes no rules relating to handling arrears and repossessions, the CML should, as part of its major review of the Code, look to produce comprehensive guidance on handling customers in financial difficulties as is proposed for the Banking Code above. The specific issues the Group would expect to see addressed in such guidance include those listed above and, in addition, the importance of considering all options for dealing with mortgage arrears before taking repossession proceedings.

- *Recommendation 12: a Business Banking Code*

*The work that has already taken place on creating a Business Banking Code should be completed on schedule and a first edition of the Code introduced by March 2002, with subsequent reviews and revisions following the new biennial procedures.*

**4.74.** We believe there are significant consumer benefits to be gained from the introduction of a Business Banking Code. This code should be implemented as soon as possible, and we welcome the BBA's commitment to complete its current review and introduce the Code by March 2002<sup>60</sup>.

**4.75.** We recognise that there may be implications for this Code from the findings of the Competition Commission report. If this finds that statutory regulation or behavioural remedies are required to deal with SME banking issues, then certain areas of a small business banking code may become redundant in the longer term. These should be dealt with at the first code review, which itself could be advanced if stakeholders feel it necessary.

**4.76.** Annex A contains a timetable of these recommendations.

## COMPLEMENTARY MEASURES

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**4.77.** Consumer codes are not a panacea for dealing with issues of consumer detriment, nor do they exist in a vacuum. Many issues are best dealt with by other means. We highlight here some of the measures which we feel are important contributors to resolving the problems that exist.

**4.78.** Complaints handling arrangements are being set out by the FSA, including setting standards and times for dealing with complaints. We believe this will assist in addressing many of the problems with these arrangements we have identified. The codes have a role to play in providing an information ‘gateway’.

**4.79.** We support the wide range of measures set in place to address financial exclusion, including:

- basic bank accounts;
- AdFLAG recommendations on adult financial education; and
- wider FSA work on consumer education.

**4.80.** The FSA issued revised money laundering rules in January 2001. We welcome the clarification provided in the guidance notes setting out the flexibility available in fulfilling proof of identity requirements. We look to banks and building societies to act in accordance with these guidelines, and recommend the Joint Money Laundering Steering Group monitor compliance with this.

**4.81.** We welcome the FSA led drive to improve the quality of information available to customers through the use of key features documents and the introduction of comparative tables. We also believe the media – through the written press, radio, television and increasingly the internet – and consumer groups, play a useful role in improving consumer awareness and understanding of personal finances.

**4.82.** Finally, we believe CAT standards can be useful where financial products are complicated or susceptible to “toxic features”. In these circumstances, CAT standards ensure “safe harbour” products can be found by those consumers who are unable or unwilling to devote the time necessary to investigate these products in depth.

## Notes:

- 1 Source: "In or Out?", FSA Consumer Research paper 3, July 2000.
- 2 Source: CML, 16 February 2001.
- 3 "Competition in UK banking: a report" Don Cruickshank, March 2000, henceforth referred to as the Cruickshank report.
- 4 N3 is the point at which the FSA assumes responsibility for its regulatory functions relating to mortgages.
- 5 N.B.: throughout the remainder of this document, references to "banks" include building societies.
- 6 For a further discussion of the self-regulation spectrum, see 'Models of self-regulation: an overview of models in business and the professions', National Consumer Council, October 2000.
- 7 This is sometimes referred to as 'co-regulation', although 'co-regulation' can also be used to refer to codes jointly owned by providers, customers and/or other stakeholders.
- 8 Better Regulation Task Force, "Principles of Good Regulation". Cabinet Office Publications and Publicity Team, October 2000. The seven main policy objectives are: to protect and enhance the rights and liberty of citizens; to promote a safe and peaceful society; to collect taxes and ensure that they are spent in accordance with policy objectives; to safeguard health and safety or protect citizens from 'harming' themselves; to protect consumers, employees and vulnerable groups from abuse; to promote the efficient working of markets; and to protect the environment and promote sustainable development.
- 9 "Banking Services: law and practice report by the review committee". HMSO, Command Paper Cm 622, February 1989.
- 10 See annex D for a glossary of abbreviations and technical terms.
- 11 FSA Consumer Research paper 5, "Informed decisions?", November 2000.
- 12 "Better business practice: how to make self-regulation work for consumers and business", National Consumer Council, December 2000.
- 13 Details of the Australian banking system, including the Australian banking code review, can be found on the internet at <http://www.bankers.asn.au/>.
- 14 The Cruickshank report, paragraph 4.112.
- 15 Treasury press release PN128/00, 8 November 2000.
- 16 The Competition Commission investigation into the provision of banking services to SMEs was set up by the Chancellor of the Exchequer and the Secretary of State for Trade and Industry in March 2000 following the publication of the Cruickshank report. The Competition Commission is due to issue its final report in June 2001.
- 17 Research carried out by BMRB International Limited. Taken from FSA Consumer Research paper 1, "Better Informed Consumers", April 2000.
- 18 Figures taken from "In or Out?", FSA Consumer Research paper 3, July 2000.
- 19 The Policy Action Taskforce on Access to Financial Services ("PAT14") reported in November 1999, making 44 recommendations. In January 2001, the Social Exclusion Unit of the Cabinet Office published an audit of progress in implementing these recommendations.
- 20 Source: DTI, 7 August 2000.
- 21 Barclays, HSBC, Lloyds TSB, RBS/NatWest.
- 22 Source: The Cruickshank report, 1998 figures, except Mortgage market, source CML, May 2000, 1999 figures.
- 23 Source: CML, May 2000, - stock of lending. The largest five lenders were Halifax, Abbey National, Lloyds TSB, Nationwide, and the Woolwich.
- 24 Source: MCCB, May 2000.
- 25 The Cruickshank report, paragraph 4.87.
- 26 Source: CML, February 2001.
- 27 APACS press release, 14 July 2000.
- 28 Source: "Switching Suppliers", DTI, October 2000.
- 29 BBA press release, 27 April 2001.
- 30 The MCCB annual report 2000 provides further details of the risk rating and compliance visiting system they use.
- 31 N2 is the term for the point at which the FSA assumes responsibilities for most of its functions by a regulated activities order under the Financial Services and Markets Act.
- 32 The eight schemes being brought together are: The Banking Ombudsman; The Building Societies Ombudsman; The Insurance Ombudsman; The Investment Ombudsman; the Personal Insurance Arbitration Service; The Personal Investment Authority Ombudsman; The Securities and Futures Authority Complaints Bureau and Arbitration Service; and The Financial Services Authority Direct Regulation Complaints Unit.
- 33 An authorised firm is one registered by the FSA to carry out regulated activities. This will include banks, building societies, and mortgage lenders, but not mortgage brokers per se as the latter are not due to be regulated. However, around fifty per cent of mortgage brokers are registered with the FSA as providers of investment advice.
- 34 Many mortgage brokers are involved in other business, such as investment business, for which they will be required to subscribe to the FOS jurisdiction.
- 35 For a full text of the Memorandum of Understanding, see the Bank of England website,

<http://www.bankofengland.co.uk/financialstability/mou.htm>.

36 Source: "Spending review 2000: new public spending plans 2001-2004", HM Treasury, November 2000.

37 See FSA press release FSA/PN/055/2001, 14 May 2001.

38 This includes life insurance, but not general insurance, which is covered by the General Insurance Standards Council.

39 Detailed in "Competition in payment systems: a consultation document", HM Treasury, December 2000.

40 "Modern markets: confident consumers", DTI, July 1999.

41 "The OFT's new approach to consumer codes of practice", OFT, February 2001.

42 It should be borne in mind that the Group only solicited comment on personal banking services, and as a consequence our analysis focuses on this area, not business banking services.

43 "Consumer Detriment", February 2000, OFT. A full explanation of the methodology employed is set out in the text.

44 At the launch of the revised Banking Code in September 2000, the Consumers' Association described the Code as "a meaningful and demanding code with good coverage".

45 Source: NACAB, April 2001. The BCSB is currently investigating these issues in association with NACAB.

46 Paragraph 15.1 of the Banking Code.

47 For example, see BCSB press release, 19 March 2001.

48 Howard Davies' speech to the CML, 4 December 2000.

49 Based on our current understanding of what statutory rules will cover. This may alter once the FSA's rules are finalised.

50 Source: Abbey National, April 2001.

51 For example, Lloyds TSB have announced that they will complete this process in 3 days and pay a £50 penalty to the customer if they fail to do so (Lloyds TSB press release, 15 March 2001), while Abbey National have established an e-mail service to facilitate the transfer of mandate details to the new bank within 24 hours (Abbey National press release, 17 April 2001).

52 Source: APACS, March 2001.

53 Evidence to the Treasury Committee, 16 January 2001.

54 For self-assessment, forms have to be returned to the Inland Revenue by end September for the Inland Revenue to calculate the tax due.

55 This could be done electronically for those customers preferring it.

56 BBA estimate, May 2001.

57 DTI press release P/2001/291, 8 May 2001.

58 National Savings press release 14/01, 2 April 2001.

59 The BCSB internet site contains a list of institutions which do not subscribe to the Banking Code. On 30 May 2001, these were listed as: American Express Card Products; The Associates; Capital One; Century Building Society; Chartered Trust; Citibank; Colonial; First-e; Frizzell Bank Limited; Hoare & Co; Investec Bank (UK) Ltd; Julian Hodge Bank Limited; Marks & Spencer; MBNA; Morgan Stanley Dean Witter; National Savings; Providian Financial Corporation; and Secure Trust Bank PLC.

60 BBA press release, 27 April 2001.

# A

## TIMETABLE OF RECOMMENDATIONS

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### 2001

May	Codes Review Group reports to HM Treasury
November	Revised Banking Code guidance on consumers in financial difficulties
	Updated Mortgage Code introduced
	Full revision of Mortgage Code to commence if FSA rules finalised

### 2002

January	Reviewer appointed for Banking Code revision
March	Business Banking Code introduced
June	CASS for current accounts, savings accounts, credit cards and loans
	Introduction of new system for individual code compliance ratings
December	5 day start- 5 week finish standard for current account switching

### 2003

January	New Banking Code introduced
Q1	Leaflet on Banking Code distributed to current account holders
June	Publication of individual firms' code compliance ratings



## CONSULTATION RESULTS

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**B.1.** The Group issued a press release “Seven key questions about bank service” (CRG PN01) on 18 December 2000. This was sent directly to over 100 groups and individuals known to have an interest in the issues involved, and articles appeared in the national press<sup>1</sup>.

**B.2.** Seventy-eight written responses were received. Of these, fifty-four were from individuals, four from trade associations, six from firms, nine from consumer groups, and five from other bodies.

**B.3.** During January and February 2001, Group members met directly with thirteen organisations<sup>2</sup>. In addition, the Group held a seminar on 27 February, which forty-four people attended, representing a broad range of stakeholders.

### *Question 1: is the process of drawing up the codes satisfactory?*

**B.4.** The trade bodies noted that broadly similar processes were used for all three codes. Those responding generally agreed that stakeholders from all sides were well consulted in the drawing up process. While some argued that the board composing the code should be independent or contain independent representation, others argued that in a voluntary regime it was essential that the industry ultimately decided what was in the code. A number of respondents felt that the current process was opaque, with no preset timetable, and a lack of public explanation at the end of the process as to why suggestions had or had not been included. No support was received for the Ombudsman being the primary standards setter.

**B.5.** Several respondents had concerns specific to the Mortgage Code. Some respondents noted that intermediaries who were bound by the Code did not have any veto over the Code’s provisions. There was also widespread concern amongst non industry respondents that the Code revision planned for 2000 had been postponed, and a feeling that the reasons for this had not been properly explained.

### *Question 2: do the codes cover all the issues that they should?*

**B.6.** Representations from industry and elsewhere felt there were no significant omissions from the Banking Code. Several respondents noted that the Code was there to set minimum standards, not standards of excellence. Consumer groups raised a number of specific areas where they thought the Banking Code needed to say more, most prominently on the treatment of people in financial difficulties and in facilitating account switching.

**B.7.** Respondents from both consumer groups and the industry felt that regulation of mortgage advice was needed, but that this could best be achieved through statutory regulation.

**B.8.** Several respondents felt the delay in revising the Mortgage Code meant several issues were not covered as fully as they should be. This included a number of issues where standards had already been set elsewhere, including requirements on firms’ fitness and propriety, and advisors’ training and competency. Consumer groups also felt, in the absence of statutory regulation, the Mortgage Code should set standards on mortgage advice.

### *Question 3: are the codes fully complied with by the industry?*

**B.9.** Many respondents felt it was unreasonable to expect to achieve 100 per cent compliance with the codes. A number of respondents pointed to the BCSB’s mystery shopping exercise in May 2000 as showing compliance with the codes in most areas was fairly strong.

**B.10.** Several respondents pointed out that both the Banking Code and the Mortgage Code have very good coverage of the market. However, some were concerned that an increase of new entrants to these markets may mean this coverage falls unless new entrants are pursued to subscribe. Consumer groups were also concerned that third party agents employed by subscribers were not covered by the codes.

**B.11.** Consumer groups were concerned about compliance with the codes in some specific areas, including the treatment of superseded accounts, dealing with debt advice agencies, and publicising the codes.

*Question 4: are the codes monitored and enforced effectively?*

**B.12.** Many respondents felt that monitoring and enforcement arrangements up to 1999 under the Independent Review Body had been inadequate. Most of these respondents also felt the arrangements had now been greatly improved, with the BCSB and the MCCB having larger budgets, better governance structures, and more effective powers of sanction.

**B.13.** Many respondents felt these bodies needed to be given time to prove their worth. A number of respondents pointed to improvements they felt the new boards had already delivered, for example, noting the thoroughness of compliance visits. A number of respondents were encouraged by the early use of disciplinary powers which the BCSB had made. A number of those responding were concerned about the length of time it had taken the MCCB to establish its disciplinary procedures. Some respondents questioned the worth of fines given the onerous procedures using these required as a result of the Human Rights Act.

*Question 5: do the codes offer adequate redress for legitimate grievances?*

**B.14.** A number of respondents felt complaints procedures were difficult and slow, acting to discourage customers from pursuing complaints. Some respondents noted that the FSA would be introducing standards for complaints handling, and therefore it would be inappropriate for the codes to duplicate this, although some were disappointed that the codes had not sought to set standards in the interim.

**B.15.** Both the Banking Code and the Mortgage Code require subscribers to belong to an ombudsman or arbitration scheme. Many respondents felt these schemes were consumer friendly and efficient, although some noted the arbitration scheme did not have the same flexibility as an ombudsman.

*Question 6: could consumers be better informed about what their rights are?*

**B.16.** There was broad feeling that the existence of the Banking Code was not sufficiently well known by consumers. Some respondents felt awareness of the Mortgage Code had improved, for example pointing to the increase in complaints under the Code as evidence of this. Some respondents noted both standards boards had initiatives in place designed to improve awareness of the codes. A number of respondents felt that consumers would not want to know the details of the codes unless they wanted to complain.

**B.17.** Many respondents were concerned about information overload, and that the full code could be dismissed by customers as unnecessary small print. Some of these respondents felt that a brief leaflet, setting out the main points of the code and/or how to complain, should be issued to customers when they opened an account and sent to them on a regular basis. Some respondents noted the “You and your mortgage” and the “How to make a complaint under the Mortgage Code” leaflets already covered these functions for mortgages.

*Question 7: do customers need more information or more clearly presented information?*

**B.18.** The overwhelming view of respondents was that more information per se was not required. Many respondents felt the information currently provided needed to be presented more clearly, and more carefully targeted.

**B.19.** Many of those responding felt the current information requirements under the codes were already extensive. Several respondents noted that there had been pressure to add detail to the codes in specific areas – while this in itself may be justified, its cumulative effect could lead to information overload and so render this extra information ineffective.

<sup>1</sup> Daily Mail, 24 January 2001; and The Guardian, 27 January 2001.

<sup>2</sup> British Bankers' Association, Building Societies Association, Banking Code Standards Board, Consumers' Association, Council of Mortgage Lenders, Department of Trade and Industry, Financial Services Authority, Financial Services Consumers' Panel, Financial Services Practitioners' Forum, Financial Ombudsman Service, Mortgage Code Compliance Board, National Association of Citizens Advice Bureaux, Office of Fair Trading.



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## GLOSSARY

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<b>APACS</b>	The Association for Payment Clearing Services is a non-statutory association of those involved in providing payment services including banks, building societies and the Post Office. Its principal task is to manage the major UK payment clearing schemes through three operational clearing companies: BACS; CCCL; and CHAPS. It currently has 31 members. <a href="http://www.apacs.org.uk">www.apacs.org.uk</a>
<b>BRTF</b>	Better Regulation Task Force <a href="http://www.cabinet-office.gov.uk/regulation/TaskForce/Index.htm">www.cabinet-office.gov.uk/regulation/TaskForce/Index.htm</a>
<b>BBA</b>	British Bankers' Association <a href="http://www.bba.org.uk">www.bba.org.uk</a>
<b>BACS</b>	BACS Ltd runs a payment scheme and provides central infrastructure for bulk electronic clearing and the management and provision of related payment services in the UK. It processes a number of different payment services - direct credits, direct debits and standing orders. It currently has 15 direct members. <a href="http://www.bacs.co.uk">www.bacs.co.uk</a>
<b>BCSB</b>	Banking Code Standards Board <a href="http://www.bankingcode.org.uk">www.bankingcode.org.uk</a>
<b>BSA</b>	Building Societies Association <a href="http://www.bsa.org.uk">www.bsa.org.uk</a>
<b>CML</b>	Council of Mortgage Lenders <a href="http://www.cml.org.uk">www.cml.org.uk</a>
<b>DTI</b>	Department of Trade and Industry <a href="http://www.dti.gov.uk">www.dti.gov.uk</a>
<b>FSA</b>	Financial Services Authority <a href="http://www.fsa.gov.uk">www.fsa.gov.uk</a>
<b>FOS</b>	Financial Ombudsman Service <a href="http://www.financial-ombudsman.org.uk">www.financial-ombudsman.org.uk</a>
<b>HMT</b>	Her Majesty's Treasury <a href="http://www.hm-treasury.gov.uk">www.hm-treasury.gov.uk</a>

<b>IRB</b>	Independent Review Body. Responsible for monitoring and enforcing the Banking Code and Mortgage Code prior to October 1999.
<b>MCCB</b>	Mortgage Code Compliance Board <a href="http://www.mortgagecode.org.uk">www.mortgagecode.org.uk</a>
<b>N2</b>	N2 is the point at which the FSA assumes responsibilities for most of its functions by a regulated activities order under the Financial Services and Markets Act.
<b>N3</b>	N3 is the point at which the FSA assumes responsibilities for mortgage regulation.
<b>NCC</b>	National Consumer Council <a href="http://www.ncc.org.uk">www.ncc.org.uk</a>
<b>OFT</b>	Office of Fair Trading <a href="http://www.offt.gov.uk">www.offt.gov.uk</a>
<b>SME</b>	Small/Medium Sized Enterprise