

**Independent Review of the Banking Code  
Report to Code sponsors**

**Elaine Kempson  
Personal Finance Research Centre  
September 2004**

## **Contents**

	<b>Page</b>
<b>Summary of key recommendations</b>	<b>i</b>
<b>1 Introduction</b>	<b>1</b>
<b>2 Key changes to the Codes in 2003</b>	<b>3</b>
2.1 Re-ordering of the Codes	3
2.2 Key commitments	3
2.3 Section 3 Helping you choose products and services which meet your needs	5
2.4 Section 4 Interest rates	6
2.5 Section 7 Changing your account	9
2.6 Section 9 Running your account	9
2.7 Section 13 Lending	9
2.8 Business Banking Code (name and coverage)	13
<b>3 Areas requiring more substantial revision</b>	<b>14</b>
3.1 Credit cards	14
3.2 Summary boxes for products other than credit cards	19
3.3 Clearing cycle	20
3.4 Account switching and small businesses	21
3.5 Branch closures	23
3.6 Relationship between legislation, FSA rules and the Banking Codes	24
<b>4 Less extensive revisions</b>	<b>25</b>
<b>5 Future Code reviews</b>	<b>28</b>

## Summary of recommendations

### Key changes to the Codes in 2003

#### Re-ordering the Codes

Section 1.1 of the Codes should include signposting to subsequent sections that apply to each of the main product types listed. *(Page 3)*

Section 10 of the Codes should be renamed 'Cards' and should have two sections: one dealing with switch and debit cards; the other with credit cards. *(Page 3)*

#### Key commitments

The key commitments should be re-drafted along the following lines.

We promise that we act fairly and reasonably in all our dealings with you and that we will meet all the commitments and standards in this Code.

- Ensuring that our advertising and promotional literature is clear and not misleading and that you are given clear information about our products and services.
- When you have chosen an account or service we will give you clear information about how it works, the terms and conditions and the interest rates which apply to it.
- We will help you use your account or service by sending you regular statements (if appropriate) and keep you informed about changes in the interest rates, charges or terms and conditions.
- We will deal with things that go wrong quickly and sympathetically and consider all cases of financial difficulty sympathetically and positively
- We will treat all your personal information as private and confidential and operate secure and reliable banking and payment systems
- We will publicise this code, have copies available and make sure that our staff are trained to put it into practice.

I also recommend that the first paragraph in section 2 of the Guidance should be strengthened to indicate that where the meaning of a particular provision in the Code is ambiguous, the key commitments provide clarification on how to interpret it. *(Page 4)*

Further, I recommend that where an area of material consumer detriment is identified that is not covered at all in the Codes this should automatically trigger an interim review. This review could be initiated by either the Code sponsors or the Banking Code Standards Board (acting on behalf of other stakeholders) and would be supervised by the independent reviewer, who would also arbitrate if there were any dispute about whether an interim review was needed (see also section 5 of this report). *(Page 4)*

I also recommend that a new section is inserted into the body of the Codes that expands the key commitment regarding 'safe and reliable banking systems'. Likewise a section needs to be inserted that brings together and expands existing information on promotion of the Codes and staff training on them. *(Page 4)*

### **Section 3 Helping you choose products and services which meet your needs**

#### **Access to basic bank accounts (Banking Code only - paragraph 3.1)**

The wording of the second bullet point in paragraph 3.1 should be amended to ensure that where a bank offers a basic bank account, staff assess whether it is suited to the needs of a customer wanting to open a current account and, if so, offer them one. It should also give an undertaking to open one if a customer specifically requests it. The reworded Guidance should take account of the difficulties listed above. *(Page 5)*

This is, moreover, an area where careful monitoring of compliance is still required.

I also recommend that reference be made to the Post Office in paragraph 3.2 of the Banking Code and Guidance. *(Page 5)*

### **Section 4 Interest rates**

#### ***Interest rate notifications (paragraphs 4.4 and 4.5) and Downgraded accounts (paragraph 4.8)***

This section of the Codes is in need of up-dating to reflect the provisions of the Unfair Terms in Consumer Contract Regulations, 1999 and to remove the difference in notification procedures for branch and non-branch-based accounts. At the time of writing, discussions are still taking place between the FSA, OFT and Code sponsors on how the Unfair Terms in Consumer Contracts regulations are to be interpreted in the Banking Code (they do not apply to Business accounts). The Guidance to paragraphs 4.4 and 4.5 of the Banking Code, relating to interest rate notifications should be revised to reflect the outcome of the negotiations of the Unfair Terms in Consumer Contract Regulations. It is important that these negotiations are concluded as swiftly as possible – ideally in time for the outcome to be incorporated into the revised Guidance on the Codes, due for publication in March 2005. If this proves impossible, it should be published as separate Guidance, but no later than December 2005.

Depending on the outcome of the negotiations, the Business Banking Code should either be revised in line with the Banking Code or, if more appropriate, to ensure delivery channel neutrality in some other way. *(Page 8)*

The provisions in the Banking Code dealing with Downgrading (4.8) should be left unchanged for the present as there is insufficient evidence to consider their effectiveness. This section should be considered in detail at the next review, or earlier through an interim review if there is evidence of consumer detriment. *(Page 8)*

The next review should consider whether or not the downgraded account section should be extended to current accounts. *(Page 8)*

### **Section 9 Running your account - Consolidated Annual Summary Statements**

No further consideration should be given to including Consolidated Annual Summary Statements within either the Banking Code or the Business Banking Code. *(Page 9)*

### **Section 13 Lending**

#### ***Credit checking (paragraph 13.1)***

I recommend that the APACS guidelines on credit card limit increases, which became effective from 20 April 2004, are incorporated into both the Banking and Business Banking Code Guidance. *(Page 9)*

The Guidance to the Codes should be revised to reflect best practice on credit checks within the industry. In doing so, it should be borne in mind that it is inadequate only to check past performance on a credit card before raising the credit limit. It should also refer to the Office of Fair Trading guidance on non-status lending. *(Page 10)*

The Guidance should also recommend that consumer enquiries about products with risk-based pricing should be supported by enquiry checks with credit reference bureaux not a full credit search. *(Page 10)*

***Financial difficulties (Banking Code paragraphs 13.10 to 13.12; Business Banking Code paragraphs 13.13 to 13.16)***

The Codes should make specific reference to subscribers accepting the Common Financial Statement (and other similar statements such as that used by the Consumer Credit Counselling Service(CCCS)). *(Page 11)*

I recommend that the Codes should include a commitment to use best endeavours to ensure that third parties comply with paragraph 13.10 of the Banking Code (13.13 of the Business Banking Code) if a debt is sold or its management transferred to them. The Guidance should require subscribers to have a 'due diligence' process when selecting third parties for debt management or debt sale. This should include compliance with the Data Protection Act 1998, Consumer Credit Act 1974, Office of Fair Trading guidance on debt collection and debt management, and code of the Credit Services Association. *(Page 11)*

The Guidance should also indicate that subscribers should pass to third parties who collect debts on their behalf details of any previous negotiations and current arrangements for repayment of the money owed. *(Page 11)*

I recommend that Code sponsors work with the national money advice associations listed in the Codes, and any other interested parties, to redraft the Guidance so that it clarifies what is meant by acting 'sympathetically and positively'. I recognise that this will take time, but it should be completed by the time of the next review of the Codes *(Page 11)* This is potentially an important compliance issue and money advisers should alert the Banking Code Standards Board compliance officer to instances where they believe individual Code subscribers are failing to act sympathetically and positively.

I also recommend that the Guidance should indicate that subscribers will take steps to ensure that negative amortisation does not occur (ie outstanding balances do not increase as a result of interest and default charges) on any account while a customer adheres to an agreed repayment plan that is based on the Common Financial Statement (or an agreed equivalent) and has been set up through a money adviser. In practical terms this will mean suspending, or reducing, interest and default charges where agreed repayments do not cover them. *(Page 12)*

Code sponsors should also work with the national money advice associations listed in the Codes to agree guidance on the most appropriate ways for subscribers to assist people who have diagnosed mental health problems that impair their ability to handle money. This will take time and should be incorporated into the Guidance on the Codes when agreement has been reached. *(Page 12)*

The Guidance should be amended either to omit specific reference to payments being ‘in line with the amount outstanding to each creditor’ or to include other generally accepted ways of achieving equitable distribution. *(Page 12)*

A new section should be included in the Business Banking Code bringing together existing information on business failure. The proposed wording of this should be sent for comment to small business representatives and the DTI Small Business Service and other interested parties. *(Page 12)*

Finally, I agree with the recommendation of Code sponsors (endorsed by others) that section 12 of the Codes should include a paragraph on the importance of customers who are in financial difficulty contacting their lender and responding to communications from them. *(Page 12)*

## **2.8 Business Banking Code**

The alignment of Business Banking Code with the Banking Code, agreed following the previous review, seems to be unproblematic and I recommend that the two Codes should continue to be revised in parallel and kept as similar as possible. *(Page 13)*

I, do however, recommend that the Business Code be renamed the Small Business Banking Code. *(Page 13)*

And I also recommend that the Business Banking Code continues to cover small businesses with a turnover of up to £1 million. But this should be kept under review and changed should there be an alteration to the remit of the Financial Ombudsman Service. *(Page 13)*

Finally, it would appear that the Business Banking Code is not being displayed (or in some cases even held) in branches. This is a compliance issue that may need investigation by the Banking Code Standards Board. *(Page 13)*

## **Areas requiring more substantial revision**

### **Credit cards**

#### ***Summary (or Schumer) boxes***

I recommend that the APACS guidelines for summary boxes on pre-contract information should be incorporated into the Guidance on the Codes and that reference be made to the use of summary boxes to draw attention to key features of credit cards in Section 6 Terms and Conditions and Section 8 Advertising and Marketing and the new section 10 on Cards. *(Page 15)*

I also recommend that further research be undertaken into the level of consumer demand for including summary boxes on credit card statement; the form that they might take, where they are best placed and whether or not they need to be included on every statement. I understand that this is already being taken forward by APACS and the outcome should inform the revision to the Codes. *(Page 15)*

***Minimum payments on credit cards (paragraph 9.2)***

I recommend that the explanatory note to existing paragraph 9.2 in the Guidance to the Banking Code (9.3 in the Business Banking Code) is revised to cover the inclusion on statements of a warning in plain English about the consequences of repeatedly making only the minimum payment on a card. *(Page 16)*

I also recommend that a new paragraph be inserted into section 10 of the Codes, giving a commitment that the minimum payment on a credit card will always cover at least the interest payable and (if appropriate) that month's proportion of any fees that are still to be paid. The Guidance will require careful wording to take account of people who settle an annual fee in a single payment. *(Page 17)*

***Allocation of payments***

I recommend that section 10 of the Code should give an undertaking to include information on the allocation of payments on the front of credit card statements. *(Page 17)*

The Guidance should make clear that this information could be included in a summary box, if one is placed on the statement.

***Unsolicited credit card cheques***

The APACS Best Practice Guidelines on credit card cheques should be incorporated into the Guidance on section 10 of the Codes. The groups for whom these cheques are not suitable should be made explicit in the Guidance and include people who are at the credit limit on their card; who are in default, or who have made only the minimum payment on their card for the past three months. The Guidance should also prohibit the sending of cheques with pre-completed amounts. *(Page 18)*

***Recurring transaction authorities***

Code sponsors should investigate ways of dealing with situations where merchants fail to act on requests to cancel recurring transaction. This should be completed by the time of the next Code review, at the latest. Code Guidance should include reference to the provisions on recurring transactions in the APACS Code of Best Practice on merchant responsibilities. *(Page 19)*

There is also clearly a need for consumer organisations to promote this advice to consumers.

***Interest charges on disputed transactions***

A commitment be included in section 10 to refund any interest incurred on any unauthorised transaction. *(Page 19)*

### **Summary boxes for products other than credit cards**

Before the next Code review, Code sponsors should commission further research into the possible content of summary boxes for other products, such as unsecured loans, current accounts, and savings account. *(Page 19)*

### **Clearing cycle**

#### ***Transparency of the clearing cycle***

Paragraph 9.4 of the Codes and its accompanying Guidance should be revised to provide an explanation of the clearing process for standing orders and telephone and internet payments, rather than a commitment to do so. This should include a reference to clearing normally taking three days, with a commitment to tell customers ‘if extra days are added to this’. It should also include a commitment to tell new customers when they can draw on cheques that they pay into their account. The Guidance should include a reference to the new APACS booklet on the cheque clearing cycle and the one on BACS payments that is in preparation. *(Page 20)*

#### ***Payment of interest on ‘float’***

This is an important issue but requires a level of investigation that is considerably beyond the resources of the independent reviewer of the Banking Code. I therefore recommend that the Office of Fair Trading explore this issue further and that the outcome is subsequently incorporated into the Code, if appropriate. *(Page 21)*

### **Account switching and small businesses**

A new paragraph should be added to section 7 of both the Banking Code and the Business Banking Code giving a commitment not to make any additional charges for either closing or switching an account. The corresponding paragraph of the Guidance should indicate that this includes additional charges to close standing orders or direct debit payments. It will be essential to ensure that this does not conflict with the Undertakings from individual banks to the Competition Commission. *(Page 22)*

I recommend that the Business Banking Code Guidance on not making charges for account switching should also make clear that it also refers to any charges, other than early settlement fees, for terminating loans at the same time. Again it is essential to ensure that this does not conflict with the Undertakings from individual banks to the Competition Commission. *(Page 22)*

A new commitment should be inserted in section 7 of the Business Banking Code to tell customers the bank’s policy on paying legal/valuation charges for transfer of any security they hold on behalf of a business customer. *(Page 23)*

Paragraph 7.2 of the Business Banking Code, dealing with credit histories, should remain unchanged. *(Page 23)*

I propose that paragraph 7.1 of the Business Banking Code includes a commitment not to require customers to hold a current account to obtain a deposit account or loan. *(Page 23)*

### **Branch closures**



I recommend a number of changes to paragraph 7.6 dealing with branch closures. First, the radius for the extended notification for closure of last branches should be reduced to 1 mile in urban areas and no more than four miles in rural ones, with the Guidance making it clear that this distance is by road, not as the crow flies. Second, the Guidance should make it clear that ‘closure’ includes replacing all counter services with automated provision. Thirdly, the Guidance should make it clear that telling people ‘how we will continue to provide banking services to you’ should be specific to provision in the locality, not just a generic statement of the channels through which banking services are provided. Fourthly, there should be a commitment to give notice of any substantial reduction in opening hours, with substantial being defined as a 50 per cent reduction or more. The Guidance on these notifications should mirror the provisions for branch closures. Finally, the Business Banking Code should also include a commitment to tell small businesses affected by closures about Inter-Bank Agency Agreements where these exist. *(Page 24)*

### **Relationship between legislation, FSA rules and the Banking Codes**

Where appropriate, brief reference should be made to legislation, but the Code and Guidance should not go further than this. In view of this:

I recommend that reference be made the Child Trust Fund legislation in the Guidance to section 3.3 of the Banking Code. A new paragraph should be inserted after paragraph 6.2 in the Banking Code stating that subscribers comply with the Distance Marketing Directive and explaining briefly what rights it confers. The Guidance should include a reference to the FSA rules. *(Page 24)*

If necessary, the wording of the Code and Guidance should be revised to take account of the Credit Advertising and Form and Content of Agreements Regulations that will be introduced in October 2004. *(Page 24)*

Code sponsors should also investigate whether it is appropriate to refer to the FSA financial promotion rules regarding the marketing of structured capital at risk products. *(Page 24)*

### **Less extensive revisions**

A number of less extensive revisions have also been recommended. These are given on pages 25 to 27.

### **Future Code reviews**

I recommend provisionally that formal reviews should be held every three years, but only if two safeguards are in place. First, there should be a fast track procedure for Code amendments between the formal reviews. These interim reviews should deal with areas of material consumer detriment not adequately covered by the Code, be initiated by either the BCSB or Code sponsors and be overseen by the independent reviewer, who will also arbitrate if there is any dispute about the need for an interim review. Secondly, the final decision on frequency of reviews should be made in

November 2005, following consultation with stakeholders through the independent reviewer. (*Page 29*)

## **1 Introduction**

The Banking Code, has been in existence for more than thirteen years, and the sixth edition was published in March 2003. The Business Banking Code, which is based closely on the Banking Code, was published for the first time in March 2002, and revised in March 2003. Both Codes set down standards of good banking practice for banks and building societies to follow when they deal with their customers and are complemented by more detailed Guidance, which is designed to assist subscribers in interpreting the Code. Implementation of the Code is monitored by the Banking Code Standards Board, the majority of whose directors are independent but include representatives from banks and building societies.

The 2003 editions of the two Codes were produced following the first review to be carried out by an independent reviewer. Previously, the Banking Code had been revised by the Code sponsors, after consultation with key stakeholders. This second independent review has considered the content of both the Codes themselves and also their accompanying Guidance for Subscribers.

The review began in January 2004 when letters and a consultation paper were sent to key stakeholders. Views were sought on a number of things:

- Whether there are any key omissions from the Codes or areas that are redundant.
- Whether any problems had arisen from the aligning the Business Banking Code with the Banking Code.
- Experiences of the key changes made in March 2003 Codes.
- Implications for the Codes of important developments since the 2002 review.
- Relationship between the Codes and the growing body of legislation.
- The frequency of the future Code reviews.

The closing date for submissions was the end February 2004.

In March 2004 two round tables were held, also with key stakeholders, to consider in detail the major points raised in the submissions. One of these concentrated on the Banking Code; the other on the Business Banking Code. Both were very well attended. Subsequently, participants were invited to submit further written evidence on the points discussed at the round table.

All the information collected during these early consultations was brought together, along with any available research reports, in a further consultation paper, which formed the basis for bilateral meetings with stakeholders during May 2004. The aim of these meetings was to give everyone an opportunity to comment on all the suggestions for changes to the Codes. Again there was an opportunity for further submissions following

these interviews and the reviewer requested further information from some of the people interviewed. A number of organisations responded with additional information and views

The period of consultation concluded in June 2004, when a third round table was held to discuss the initial conclusions and recommendations of the independent review and also to discuss the review process itself. Like the two earlier round tables, this was very well attended.

Throughout the review I was provided with administrative support by members of staff from the three sponsoring bodies: Elanor Cann, APACS; Jerry Fearnley, British Bankers Association and Ruth Lamb, Building Societies Association. I am very grateful to them for all the help they have given me.

I would also like to thank everyone who has made an input to the review, with particular thanks to those who, at various stages in the review, have provided additional detailed information at my request. I am impressed by the constructive and thoughtful way that everyone has approached the review of the Codes. This has made a significant difference to both the process and the outcome of this review.

At no stage have I felt that my independence was compromised and I hope that everyone who has contributed feels that they were given the opportunity to express their views and that I have listened to what they have said. In the end, though, I have had to reach my own conclusions on the changes that need to be made to the Codes. These are set out in the sections that follow. Section 2 considers key changes that were made to the Banking and Business Banking Codes in 2003, Section 3 covers the major issues that have arisen since the previous review and require substantial revision, with Section 4 listing a number of areas of the Codes where I am recommending less extensive revision. The report concludes with a section that considers the review process itself, including the frequency of future reviews and the need for a procedure to deal with interim reviews.

## **2 Key changes to the Codes in 2003**

A number of important changes were made to the Banking and Business Banking Codes following the first independent review. These include re-ordering of the Codes, revision of the key commitments and major changes and additions to the sections dealing with interest rate changes, account switching and lending. It has become clear from the consultation with stakeholders that the present Codes now deal adequately with some of these issues but that others still require further revision.

### **2.1 Re-ordering of the Codes**

The previous review recommended substantial re-ordering of the Codes to separate out sections that deal only with lending, to accommodate the needs of smaller building society subscribers and their customers. This seems to be working well although the smaller building societies re-iterated their desire for a separate ‘Savers Code’, which would include only those sections that deal with savings products. Other submissions have called for a clearer section on credit cards, in the light of additions that will be made in the next revision of the Codes and are discussed in section 3.1 of this report.

I rehearsed the arguments for and against a ‘Savers Code’ in my previous report, concluding that, on balance, it was preferable to retain a single, but re-ordered Code. I have received no new evidence to change my mind, although I agree with the suggestion that there should be clearer signposting at the beginning of the Codes to indicate which sections apply to particular products.

***I recommend that that section 1.1 of the Codes should include signposting to subsequent sections that apply to each of the main product types listed.***

There is also a need to ensure that future editions of the Codes keep information relating to specific products together. This applies especially to credit cards, where a number of important changes are proposed for the next edition.

***I recommend that Section 10 of the Codes be renamed ‘Cards’ and should have two sections: one dealing with switch and debit cards; the other with credit cards.***

### **2.2 Key commitments**

The Key Commitments section of the two Codes was revised quite substantially following the previous review. Responses to the consultation did not identify any

problems arising from this revision. However, both the Banking Code Standards Board (BCSB) and the Financial Ombudsman Service (FOS) have queried the legal status of the key commitments and whether or not they are enforceable in their own right. I was given, in confidence, details of four instances where enforcement had relied on the key commitments either because the wording of the Code was ambiguous or because there no provision in the Code at all.

Code sponsors and subscribers were anxious about the enforceability of some of the existing commitments; others thought it illogical that the key commitments would not be enforceable. This discussion has also focussed attention on their limited coverage of the Codes' content and their varying degrees of specificity.

In view of this, it was agreed at the bilateral meetings that Code sponsors should convene one or more meetings to discuss the wording of the key commitments with the Banking Code Standards Board, the Financial Ombudsman Service and the independent reviewer.

***As a result of these discussions, I recommend that the key commitments be re-drafted along the following lines.***

We promise that we act fairly and reasonably in all our dealings with you and that we will meet all the commitments and standards in this Code. This will include:

- Ensuring that our advertising and promotional literature is clear and not misleading and that you are given clear information about our products and services.
- When you have chosen an account or service we will give you clear information about how it works, the terms and conditions and the interest rates which apply to it.
- We will help you use your account or service by sending you regular statements (where appropriate) and keep you informed about changes in the interest rates, charges or terms and conditions.
- We will deal with things that go wrong quickly and sympathetically and consider all cases of financial difficulty sympathetically and positively
- We will treat all your personal information as private and confidential and operate secure and reliable banking and payment systems
- We will publicise this code, have copies available and make sure that our staff are trained to put it into practice.

***I also recommend that the first paragraph in section 2 of the Guidance should be strengthened to indicate that where the meaning of a particular provision in the Code is ambiguous, the key commitments provide clarification on how to interpret it.***

***Further, I recommend that where an area of material consumer detriment is identified that is not covered at all in the Codes this should automatically trigger an interim review. This review could be initiated by either the Code sponsors or the Banking Code Standards Board (acting on behalf of other stakeholders) and would be supervised by the independent reviewer, who would also arbitrate if there were any dispute about whether an interim review was needed (see also section 5 of this report).***

***I also recommend that a new section is inserted into the body of the Codes that expands the key commitment regarding 'safe and reliable banking systems'. Likewise a section needs to be inserted that brings together and expands existing information on promotion of the Codes and staff training on them.***

## **2.3 Section 3 Helping you choose products and services which meet your needs**

### **2.3.1 Access to basic bank accounts (Banking Code only - paragraph 3.1)**

In my report of the previous review, I recommended that the commitment to give information on a basic account ‘...if we think you might be interested in one’ should be amended to read ‘...if we offer one and if you tell us you are interested in opening a current account’. In the event the wording was altered to ‘...if we offer one and it would appear to meet your needs.’

Despite this change there is clearly continuing concern about the lack of promotion of basic bank accounts. Research and practical experience shows that problems arise in three ways:

- People are not being told about a basic bank account when they open an account even when it is the most suitable one for their needs.
- People are being dissuaded or steered away from a basic bank account when they ask for one.
- People who are on debt management plans set up by a money adviser have been unable to switch to a basic bank account and close their current account.

I have consulted widely on whether this is a matter of compliance or whether the wording of the Code and/or the Guidance needs to be altered. On balance, I feel that the wording of the Code should be tightened.

***I, therefore, recommend that the wording of the second bullet point in paragraph 3.1, should be amended to ensure that where a bank offers a basic bank account, staff assess whether it is suited to the needs of a customer wanting to open a current account and, if so, offer them one. It should also give an undertaking to open one if a customer specifically requests it. The reworded Guidance should take account of the difficulties listed above.***

This is, moreover, an area where careful monitoring of compliance is still required.

Two related issues have also been raised. The first is the need to tell customers when basic bank accounts can be used at a Post Office.

***I recommend that reference be made to the Post Office in paragraph 3.2 of the Banking Code and Guidance.***

Secondly, there is continuing evidence of customers experiencing difficulties with providing suitable proof of identity. The Joint Money Laundering Steering Group has issued *Guidance Notes for the Financial Sector* and reference is already made to these in the Guidance on the Codes, along with an encouragement for subscribers to adopt a flexible approach within the Regulations and Guidance Notes. The Financial Services

Authority has convened a working group to explore this issue further, which will report in October 2004 and may result in further changes to these *Guidance Notes*. This issue is, therefore, primarily a problem of staff training and compliance and one that needs monitoring. Indeed, this was noted by the Banking Code Standards Board in the report of their mystery shopping research<sup>1</sup>.

## **2.4 Section 4 Interest rates**

This section of the Codes is in need of up-dating to reflect the provisions of the Unfair Terms in Consumer Contract Regulations, 1999. Some revision was made at the time of the last review, principally as an interim measure pending guidelines on the regulations that were to be published by the Financial Services Authority (FSA). However, a new section covering '*downgraded accounts*' replaced the one on '*superseded accounts*', that had proved to be problematic.

### **2.4.1 Interest rate notifications (paragraphs 4.4 and 4.5)**

Following the last review, this section was redrafted in the 2002 Codes to make it less specific and to ensure that the Codes comply with the Unfair Terms in Consumer Contracts Regulations 1999. The Guidance, however, remained unchanged. This was an interim measure until the FSA issued its guidelines on the regulations, when the Guidance for Code Subscribers would be revised. These guidelines have still to be finalised. There was also a recommendation in the report of the previous Code review that the Codes should remove the distinction between branch-based and non-branch-based accounts which was not implemented. A number of submissions to this review reiterated their desire for this issue to be addressed.

On balance, most of those who commented on this section felt that the current, much reduced, wording of paragraphs 4.4 and 4.5 in the Codes was working adequately. There was general support for waiting until the FSA guidelines are published before finalising changes to the Guidance, while recognising that any changes will have to remove the different interest rate notification provisions for branch-based and non-branch-based accounts.

It is, however, important to note that information provided by Code subscribers indicates that the cost of notifying all account-holders of every interest rate change would be high – and ultimately borne by consumers. Consumer Groups recognise this and would support a *de minimis* provision.

There are a number of options for reducing the costs of routine personal notification:

- Restricting the accounts where notification is required by:
  - making it contingent on a minimum balance in the account (figures provided by Code subscribers suggest that, for the majority, a *de minimis* of £250 would significantly reduce the number of accounts, but further reduction to £500 or £1,000 would not have a large effect);

---

<sup>1</sup> Banking Code Standards Board *Survey of subscriber institutions on basic bank accounts*. July 2003.



- excluding tracker accounts.
- and
- Issuing personal notifications periodically, but not after every rate change.
- Suggestions made in the course of consultation on the Codes included:
- when the cumulative interest rate change reaches a trigger point – the Consumers Association have suggested a 1% change;
  - after a fixed number of interest rate changes – after every third change has been suggested by the Consumers Association;
  - regularly every quarter, giving the current rate applying to a customer's account and how that had changed since the last statement.

Subscribers would then notify other changes through notices in their branches, on websites or in newspapers.

Discussion with the Financial Services Authority and Office of Fair Trading identified that such restrictions on personal notification would only meet the Unfair Terms in Consumer Contract Regulations, provided adequate provision is made in cases of consumer detriment, where interest rates fail to match changes in the Bank of England base (repo) rate. This is what the downgraded accounts section of the Banking Code (discussed below) is designed to do, although it would need further strengthening to comply with the Regulations.

An alternative approach, and possibly more satisfactory, approach would be for the Codes to require personal notifications when the rate has not changed in line with base rate within a specified period of time from that change. Again this would be subject to a minimum account balance. In this case, the downgraded accounts section could remain unchanged. The advantages of this approach are that it would ensure that all consumers are told of any change that is to their detriment, even if their account is currently considered 'branch-based' and it would also appear not require the development of new systems by subscribers. It could also mean that revision of the downgraded account section could be deferred until there is further evidence on how well it is working. As the Unfair Terms in Consumer Contracts Regulations do not apply to small business banking, consideration will need to be given to whether the wording of paragraphs 4.4 and 4.5 of the Business Banking Code should mirror that of the Banking Code or whether the notification of interest rate changes should be made delivery channel neutral in some other way.

#### **2.4.2 Downgraded accounts (paragraph 4.8)**

Following the last review, this section replaced one dealing with 'superseded accounts' that was, at that time, the most problematic section of the Banking Code. This new paragraph (4.8) shifted focus from accounts that were superseded to ones where the interest rate had fallen relative to the Bank of England base (repo) rate. It required Code subscribers to notify customers where downgrading had occurred and also gave customers the right to withdraw the balances on such accounts without a period of notice or incurring a penalty. The package of features that constitutes downgrading and is included in the Code Guidance took some considerable time to agree.

The initial consultation indicated that this new section of the Codes seems to be easier for the two enforcement bodies and most subscribers to apply but, as there had been little change in interest rates, that it had not really been put to the test. In view of this, there was general consensus that the Codes should remain unchanged but reviewed in more detail in the light of greater experience with changes in base rate. That said, a number of Code subscribers indicated that the current Guidance on paragraph 4.8 should be re-written more concisely, with an additional paragraphs dealing with promotional rates and a definition of a savings account.

However, this section is also affected by the Unfair Terms in Consumer Contract Regulations. In particular, it is likely that the level of potential detriment may be set too high and the level of downgrading may need to be reduced from 50 basis points to 25 (0.5% to 0.25%). This is likely to be the case unless personal notification of rate changes are sent in all cases where the rate has not changed in line with base rate within an agreed period of time from that change (see above).

At the time of writing, discussions are still taking place between the FSA, OFT and Code sponsors on how the Unfair Terms in Consumer Contracts regulations are to be interpreted in the Codes.

***I recommend that the Guidance to paragraphs 4.4 and 4.5 of the Banking Code, relating to interest rate notifications should be revised to reflect the outcome of the negotiations of the Unfair Terms in Consumer Contract Regulations. It is important that these negotiations are concluded as swiftly as possible – ideally in time for the outcome to be incorporated into the revised Guidance on the Codes, due for publication in March 2005. If this proves impossible, it should be published as separate Guidance, but no later than December 2005.***

***Depending on the outcome of the negotiations, the Business Banking Code should either be revised in line with the Banking Code or, if more appropriate, to ensure delivery channel neutrality in some other way.***

***The provisions in the Banking Code dealing with Downgrading (4.8) should be left unchanged for the present as there is insufficient evidence to consider their effectiveness. This section should be considered in detail at the next review, or earlier through an interim review if there is evidence of consumer detriment.***

It has also been proposed that the downgrading provisions should also apply to current accounts as a growing number now pay more than a token level of interest. However, in contrast to many savings accounts, they do not carry lock-ins and would be better addressed through the arrangements for routine notifications (see above). The adequacy of this approach should, however, be kept under review.

***I recommend the next review should consider whether or not the downgraded account section should be extended to current accounts.***

## **2.5 Section 7 Changing your account**

Paragraphs 7.2 to 7.4 *Moving your account* were new provisions in the 2003 edition of the Codes, that were accompanied by detailed service standards in the Guidance. Consultation has shown that these are working smoothly from the viewpoint of both consumers and subscribers. Indeed, some consumer organisations referred to account-switching as ‘yesterday’s problem’.

During the consultation, it became apparent that some banks are imposing charges for the closure of standing order or direct debit arrangements when accounts are switched. This is discussed further on in section 3.4.2 of this report.

## **2.6 Section 9 Running your account - Consolidated Annual Summary Statements**

The previous review considered the proposal for Consolidated Annual Summary Statements made by the Banking Services Consumer Codes Review Group. Based on the evidence received, it was decided not to recommend their introduction, but the report of the review included a recommendation that further research should be undertaken into the information needed by consumers on the statements they receive on a range of accounts.

This research was subsequently undertaken by the Banking Code Standards Board and the initial consultation paper sought views on Consolidated Annual Summary Statements in the light of its findings. There was no support for taking this suggestion further.

***I recommend that no further consideration be given to including Consolidated Annual Summary Statements within either the Banking Code or the Business Banking Code.***

## **2.7 Section 13 Lending**

A number of changes were made to section 13 on lending following the previous review. These included a commitment to check ability to repay before increasing credit limits on overdrafts or credit cards; amending the Guidance on credit checks to reflect good practice in the industry, and the inclusion of a commitment to provide a clear explanation for a credit application being declined. In addition, new Guidance had just been introduced on dealing with customers in financial difficulty that was incorporated into the Code.

### **2.7.1 Credit checking (paragraph 13.1)**

A large number of submissions indicated that the revised wording of paragraph 13.1 of the Codes has not led to a significant improvement in credit checking before credit limits on credit cards and overdrafts are increased. APACS has, however, issued a set of

guidelines on credit card limit increases (including provision for people to reduce or opt out of unsolicited increases), which became effective from 20 April 2004.

***I recommend that the APACS guidelines on credit card limit increases are incorporated into both the Banking and Business Banking Code Guidance***

Others reported that there has been no significant improvement in credit checks generally (ie not just on credit card limit increases) following the revision of the Guidance. Currently, the Guidance includes a list of six ways that ability to repay may be judged. These include:

- The customer's income and financial commitments.
- How they have handled their finances in the past.
- Information from credit reference agencies and, with the customer's permission others such as lenders, the customer's employer and landlord
- Information the customer provides including information to prove their identity and why they want to borrow the money.
- Credit assessment techniques, such as credit scoring.
- Any security provided.

The Guidance also notes that '*there is no obligation to take all these areas into account when making a lending decision, but one or more should be taken into account.*'

This leaves open the possibility of subscribers making lending decisions based solely on security; proof of identity, or a customer telling the lender why they want to borrow the money.

***I recommend that the Guidance to the Codes is revised to reflect best practice on credit checks within the industry. In doing so, it should be borne in mind that it is inadequate only to check past performance on a credit card before raising the credit limit. It should also refer to the Office of Fair Trading guidance on non-status lending.***

***The Guidance should also recommend that consumer enquiries about products with risk-based pricing should be supported by enquiry checks with credit reference bureaux not a full credit search.***

#### **2.7.2 Explanation of reasons for declining credit applications (Banking Code paragraph 13.2; Business Banking Code paragraph 13.6)**

The 2003 edition of the Codes included a new paragraph in the Banking Code giving a commitment to provide an explanation when loan applications are turned down, reflecting the one already included in the Business Banking Code. At that time, some subscribers were concerned about the potential for fraudulent applications if reasons were given for declining applications. This does not seem to have been borne out in practice.

#### **2.7.3 Financial difficulties (Banking Code paragraphs 13.10 to 13.12; Business Banking Code paragraphs 13.13 to 13.16)**

Shortly before the previous review, new Guidance was issued on dealing with consumers who are in financial difficulties, following extensive consultation with money advisers and others. This was incorporated into the 2003 edition of the Guidance for Subscribers.

Since then the format of a Common Financial Statement has been agreed between Code sponsors and the Money Advice Trust. Code sponsors have proposed that this should be mentioned explicitly in Guidance and briefly in the Code. This was welcomed by money advisers, with the proviso that it also encompasses other financial statements (such as that used by the Consumer Credit Counselling Service) which include the same information in a different format.

***I recommend that the Codes should make specific reference to subscribers accepting the Common Financial Statement (and other similar statements such as that used by the Consumer Credit Counselling Service (CCCS)).***

Money advice organisations have indicated that the current Guidance is not always working as intended. In particular, three main issues have been raised:

- Third parties dealing with debt recovery on behalf of subscribers are not following Code
- Some lenders are not complying with what money advisers see as the spirit of Code and are continuing to add interest to accounts
- The need for guidance on dealing with customers with mental health problems

The first of these is a difficult issue. The Guidance to the Codes currently requires subscribers who transfer the management of customers' debts to third parties to 'use all reasonable best endeavours to ensure that Code standards are applied to such agents'. It also requires that if debts are securitised and sold to a third party 'the subscriber must ensure that the purchaser accepts agreements previously reached with customers and that they undertake to comply with the Code'. There is, however, no comparable provision for use of third parties who collect debts on behalf of subscribers. Problems seem to arise particularly when the third party involved is not a Code subscriber and is also outside the jurisdiction of the Financial Ombudsman Service.

***I recommend that the Codes should include a commitment to use best endeavours to ensure that third parties comply with paragraph 13.10 of the Banking Code (13.13 of the Business Banking Code) if a debt is sold or its management transferred to them. The Guidance should require subscribers to have a 'due diligence' process when selecting third parties for debt management or debt sale. This should include compliance with the Data Protection Act 1998, Consumer Credit Act 1974, Office of Fair Trading guidance on debt collection and debt management, and code of the Credit Services Association.***

***The Guidance should also indicate that subscribers should pass to third parties who collect debts on their behalf details of any previous negotiations and current arrangements for repayment of the money owed.***

Money advisers allege that some Code subscribers are not acting within the spirit of paragraph 13.10 (13.13 in the Business Banking Code) to ‘*consider cases of financial difficulty sympathetically and positively*’, and, in particular, continue to add interest and default charges to accounts when their clients are on an agreed debt management plan. The current Guidance does not attempt to define ‘*sympathetically and positively*’ and currently says that ‘*Subscribers may consider agreeing with their customers in difficulty appropriate concessions, relating to charges and interest payable by the customer*’.

***I recommend that Code sponsors work with the national money advice associations listed in the Codes, and any other interested parties, to redraft the Guidance so that it clarifies what is meant by acting ‘sympathetically and positively’. I recognise that this will take time, but it should be completed by the time of the next review of the Codes.***

This is potentially an important compliance issue and money advisers should alert the Banking Code Standards Board compliance officer to instances where they believe individual Code subscribers are failing to act sympathetically and positively.

***I also recommend that the Guidance should indicate that subscribers will take steps to ensure that negative amortisation does not occur (ie outstanding balances do not increase as a result of interest and default charges) on any account while a customer adheres to an agreed repayment plan that is based on the Common Financial Statement (or an agreed equivalent) and has been set up through a money adviser. In practical terms this will mean suspending, or reducing, interest and default charges where agreed repayments do not cover them.***

The debt problems faced by people with mental health difficulties have only recently begun to be acknowledged. There are particular difficulties where mental health conditions impair people’s ability to maintain repayment schedules. I note that both the Money Advice Association and the British Bankers Association are undertaking work in this area.

***I recommend that Code sponsors work with the national money advice associations listed in the Codes to agree guidance on the most appropriate ways for subscribers to assist people who have diagnosed mental health problems that impair their ability to handle money. This will take time and should be incorporated into the Guidance on the Codes when agreement has been reached.***

A more specific problem relates to the section of the Guidance on *pro rata* payment which refers to payments being ‘*in line with the amount outstanding to each creditor*’. At least one of the networks of money advice agencies (the Consumer Credit Counselling Service) calculates payments in line with the contractual monthly payments to each creditor.

***I recommend that the Guidance is amended either to omit specific reference to payments being ‘in line with the amount outstanding to each creditor’ or to include other generally accepted ways of achieving equitable distribution.***

Code sponsors have suggested that section 13 of the Business Banking Code should conclude with a section entitled ‘*When businesses fail*’, bringing together information that is already in the Code. This was supported by others.

***I recommend that a new section should be included in the Business Banking Code bringing together existing information on business failure. The proposed wording of this should be sent for comment to small business representatives and the DTI Small Business Service and other interested parties.***

Finally,

***I agree with the recommendation of Code sponsors (endorsed by others) that section 12 of the Codes should include a paragraph on the importance of customers who are in financial difficulty contacting their lender and responding to communications from them.***

## **2.8 Business Banking Code**

The alignment of Business Banking Code with the Banking Code, agreed following the previous review, seems to be unproblematic and ***I recommend that the two Codes should continue to be revised in parallel and kept as similar as possible.***

The previous review also considered both changing name of this code to the Small Business Banking Code and extending its coverage from firms with an annual turnover of up to £1 million. Both issues were raised again in the current review and I have reached the same conclusions: that there is a case for changing the name but not yet for increasing the coverage, as it would lead to potential confusion if it were out of step with the Financial Ombudsman Service.

***I, therefore, recommend that the Business Code be renamed the Small Business Banking Code.***

***I also recommend that the Business Banking Code continues to cover small businesses with a turnover of up to £1 million. But this should be kept under review and changed should there be an alteration to the remit of the Financial Ombudsman Service.***

Finally, it would appear that the Business Banking Code is not being displayed (or in some cases even held) in branches. This is a compliance issue that may need investigation by the Banking Code Standards Board.

### 3 Areas requiring more substantial revision

A number of new issues have arisen since the previous review and revision of the Codes. These include a large number arising from the Treasury Select Committee report on credit cards, some relating to clearing processes that have arisen from the Office of Fair Trading report on UK payment systems, and a number of issues that derive from the bi-lateral undertakings on business banking that were signed by the eight main clearing banks. In addition, subscribers raised the question of whether, and if so how, the Codes should reflect new legislation and FSA rules.

#### 3.1 Credit cards

In December 2003, the Treasury Select Committee published the report of its enquiry into credit card charges<sup>2</sup>. A response from the Department for Trade and Industry was published in March 2004<sup>3</sup> and a supplementary response from the Department for Trade and Industry in June 2004<sup>4</sup>.

The Select Committee report set out a list of recommendations some of which have particular relevance to both the Banking and the Business Banking Code. Since the report was published, APACS has been following up many of these recommendations and has produced sets of guidance which Code sponsors believe should be incorporated into the Guidance on the Banking Codes. The recommendations of the Select Committee stimulated a large number of submissions to the review, many of them endorsing the Committee's recommendations and proposing their inclusion in the Banking Codes.

The areas covered by submissions to the review include:

- Credit checks when raising credit limits on cards (covered above)
- The introduction of summary boxes on promotional material and statements
- APRs
- Interest rate calculations
- The level of minimum payments
- Allocation of payments
- Unsolicited credit card cheques.

Other proposals not covered by the Select Committee report included:

- Replacement of cards of one a different kind

---

<sup>2</sup> *Transparency of credit card charges*. House of Commons Paper No 125. 17 December 2003

<sup>3</sup> House of Commons Paper No 431. 16 March 2004

<sup>4</sup> House of Commons Paper No 761. 29 June 2004



- Recurrent transaction authorities
- Interest charges on disputed transactions

### **3.1.1 Summary (or Schumer) boxes**

Following the Treasury Select Committee APACS, in conjunction with subscribers, has researched and produced Best Practice Guidelines for summary boxes, which will provide consumers with succinct information about the key features of credit cards. It is proposed that these should be included in pre-contract information.

The APACS research, along with other research undertaken by the Office of Fair Trading, the Department of Trade and Industry and the Banking Code Standards Board has shown that consumers like these summary boxes on pre-contract and promotional material and find the APACS proposed content appropriate and the format easy to use. Moreover, the APACS guidelines address concerns that they have not in the past been produced in a standard format or with a standard heading. Research undertaken for the BCSB suggests that the heading should be something like ‘Key terms and conditions’ rather than ‘Summary Box’, which meant little to the people surveyed..

***I recommend that the APACS guidelines for summary boxes should be incorporated into the Guidance on the Codes and that reference be made to the use of summary boxes to draw attention to key features of credit cards in Section 6 Terms and Conditions and Section 8 Advertising and Marketing and the new section 10 on Cards..***

The evidence and views on the value of including summary boxes on credit card statements are less conclusive. If they are to be included on statements, the content and positioning of them almost certainly needs more investigation. However, much of the information that they would need to contain already either appears on statements or is recommended for inclusion in section 3.1.4 and 3.1.5 below. There is, therefore, a real danger of credit card statements becoming confusing if they include too much additional information in an unstructured way. Collecting information together in a summary box may be the best solution. Research undertaken to date suggests that summary boxes may need to appear on the reverse of credit card statements if they are to be legible, yet not have an impact on the key information that people need to have – the balance outstanding and the minimum payment required. At the same time, it is clear that the front of the statement needs to contain a prominent statement drawing people’s attention to the summary box.

***I also recommend that further research be undertaken into the level of consumer demand for including summary boxes on credit card statement; the form that they might take, where they are best placed and whether or not they need to be included on every statement. I understand that this is already being taken forward by APACS and the outcome should inform the revision to the Codes.***

### **3.1.2 APRs on credit card statements (paragraph 9.2)**

Since the previous Code review, agreement has been reached on a single method of calculating the APR for credit cards, which will be brought into effect alongside revised

regulations on advertising of Consumer Credit. These were laid before Parliament in June 2004 and should come into force in October 2004. This is a welcome development.

Submissions to this review have proposed that the APR should be shown on every credit card statement, although opinions were divided on this point. There was a counter view that the APR quoted at the 'go to' rate would be confusing and consumers most need an indication of the interest rate(s) they are actually paying. This is already included in the Guidance to the Codes. The proposed research on summary boxes on statements should cover the issue of APRs

### **3.1.3 Calculation of interest rates**

The Treasury Select Committee drew attention to the wide variation and lack of transparency in the way that interest rates are calculated on different credit cards; and these comments were echoed in the submissions to this review, which called for a standardisation in the way that interest rates are calculated. While I have a great deal of sympathy with these arguments this is an issue that is beyond this review to resolve. Moreover, the supplementary Government response to the Treasury Select Committee notes that this is a competitive issue and one best dealt with through transparency<sup>5</sup>

The introduction of the Summary Box should provide greater transparency on the elements that feed into the interest rate (for example, interest free periods, minimum payment, and the period over which interest is charged). I also note that the DTI is discussing with APACS and card issuers and that 'consideration is being given to setting down in regulations a requirement that the information which currently appears in summary boxes concerning how each lender calculates its interest charges must be clearly explained in the pre-contract information and also in agreements.'<sup>6</sup>

### **3.1.4 Minimum payments on credit cards (paragraph 9.2)**

Following the Select Committee report, Code sponsors have proposed that the Code should require all credit card statements to carry a generic warning against continuously making only minimum payments and that this should be placed close to the minimum payment figure on the statement. The proposed wording is:

*'Only ever making the minimum repayment will significantly increase the time taken to clear your balance and cost you more.'*

There is a great deal of support for this proposal, although a general feeling that it would have greater impact if the sentence were in plainer English and did not begin with a conditional clause.

***I recommend that a plain English version of this statement is included in the explanatory note to existing paragraph 9.2 in the Guidance to the Banking Code (9.3 in the Business Banking Code).***

---

<sup>5</sup> House of Commons Paper No 761. 29 June 2004

<sup>6</sup> House of Commons Paper No 431. 16 March 2004

Some submissions have gone further and suggested that the minimum payment should be set so that it will cover the interest payable on the account, with a small number advocating that the minimum payment should also cover annual and other fees, default charges and premiums on payment protection insurance (PPI) that has been sold with the card.

Having consulted widely on this issue, there was widespread support for minimum payments covering the interest and annual and other fees, and so:

***I recommend that a new paragraph be inserted into section 10 of the Codes, giving a commitment that the minimum payment on a credit card will always cover at least the interest payable and (if appropriate) that month's proportion of any fees that are still to be paid. The Guidance will require careful wording to take account of people who settle an annual fee in a single payment.***

In contrast, very few consultees agreed that PPI should be covered by the minimum payment and many thought that including default charges could lead consumers into (worse) financial difficulties.

### **3.1.5 Allocation of payments**

It has been suggested that the Code should include a commitment to advise customers how payments are allocated to balances and how this affects the interest that will be charged.

This will be included in the Summary Box for pre-contractual information although there was a strong feeling that this information ought to be on statements too.

***I recommend that section 10 of the Code should give an undertaking to include this information on the front of credit card statements.***

The Guidance should make clear that this information could be included in a summary box, if one is placed on the statement.

### **3.1.6 Unsolicited credit card cheques**

Few topics create such a heated debate as credit card cheques. They were discussed in the second report of the DTI Over-indebtedness Taskforce<sup>7</sup> and picked up by the Treasury Select Committee in its report. They were also covered in many of the submissions to this review.

Following the Treasury Select Committee, APACS and card issuers have produced some Best Practice Guidelines, which will be effective by 1 October 2004. Code sponsors have proposed that these should be incorporated into the Guidance on the Codes and this was widely supported during the consultation for this review.

---

<sup>7</sup> Task Force on Tackling Over-indebtedness. Second Report.

These Guidelines include:

- A commitment to assess a customers' suitability and ability to repay before sending cheques out
- An opportunity for all new customers to opt out of receipt, and for existing customers to do so by contacting their card issuer
- Transparency about the terms, conditions and charges associated with credit card cheques

It was proposed by contributors to this review that the Guidance should spell out four main groups for whom credit card cheque would be unsuitable. They include:

- Young people aged under 25
- People at the credit limit on their card
- People in default
- People who have made only the minimum payment on their card for the past three months

Finally, there was a great deal of support for prohibiting the practice of sending cheques with pre-completed amounts.

I was originally minded to accept these proposals as they stand. However, Code sponsors have argued that the imposition of an age limit might be considered discriminatory. I have, therefore, accepted this argument provided other safeguards are robust and offer young people adequate protection. Sponsors also argued that as minimum payments are often linked to 0% balance transfers these too should be excluded. I was not minded to accept this as a blanket exclusion, although the Guidance could make it clear that it is intended to cover people who are in financial difficulties.

***I, therefore, recommend that the APACS Best Practice Guidelines on credit card cheques should be incorporated into the Guidance on section 10 of the Codes. The groups for whom these cheques are not suitable should be made explicit in the Guidance and include people at the credit limit on their card; who are in default, or who have made only the minimum payment on their card for the past three months. The Guidance should also prohibit the sending of cheques with pre-completed amounts.***

### **3.1.7 Replacement cards**

Following a well-publicised case of a retailer replacing its store card with a credit card, some submissions suggested that the Codes should include a commitment that a card would not be sent unsolicited as a replacement unless it is the same kind of card operating on an existing account. So, for example, a credit card would not be sent as a replacement for a store card.

Wider consultation showed that the general consensus is that this problem is unlikely to recur and so does not need be included in the Code. It is, in any case in contravention of the Consumer Credit Act. Code sponsors may, however, choose to insert a commitment into section 10 of the Codes to cover this situation as a precautionary step.

### **3.1.8 Recurring transaction authorities**

There would appear to be a growing problem when customers use their credit cards to set up recurring transaction authorities – for example giving an authority to an internet provider to process monthly transactions for the service they provide. Unlike direct debit authorities, these arrangements are solely between the merchant and the customer. The card issuer is not involved in the same way as providers of current accounts are for direct debits. Problems can arise when the customer writes to the merchant to cancel the recurring transaction but the request is ignored. This is a particular problem where transactions fall below the merchant's floor limit (often £50 - £100) as these do not require authorisation by the card issuer. Paragraph 9.5 of the Code already includes a commitment to tell consumers how to cancel recurring transactions and the APACS Code of Best Practice includes a requirement for merchants to ensure that instructions to cancel recurrent transaction authorities are carried out immediately. Despite this problems continue to arise and, as things stand, it is difficult for lenders to deal with them – even if the customer returns their card to the card issuer indicating that they wish to close the account and open a new one.

***I therefore recommend that Code sponsors investigate ways of dealing with situations where merchants fail to act on requests to cancel recurring transactions. This should be completed by the time of the next Code review, at the latest. Code Guidance should include reference to the provisions on recurring transactions in the APACS Code of Best Practice on merchant responsibilities.***

There is also clearly a need for consumer organisations to promote this advice to consumers.

### **3.1.9 Interest charges on disputed transactions**

Submissions to the review expressed concern about interest being charged on disputed credit card transactions and suggested that interest should be suspended while the matter is being resolved. This could, however, have the undesirable consequence of providing a loop hole for unscrupulous card holders to dispute transactions in order to avoid interest. Further discussion with consumer groups and card issuers indicated that both would accept a commitment to refund interest on transactions that investigation finds to have been unauthorised.

***I recommend that a commitment be included in section 10 to refund any interest incurred on any unauthorised transaction.***

## **3.2 Summary boxes for products other than credit cards**

A number of submissions suggested that summary boxes should be extended to other products such as loans, current accounts and savings accounts. The Banking Code Standards Board has commissioned some preliminary research into this issue and identified considerable consumer interest. Experience with the design of summary boxes

for credit cards indicates that much more work will be needed on the content of similar boxes for other products.

***I recommend that before the next Code review, Code sponsors should commission further research into the possible content of summary boxes for other products, such as unsecured loans, current accounts, and savings account.***

### **3.3 Clearing cycle**

Arising from its report *UK payment systems*, published in May 2003, the Office of Fair Trading has raised two issues that relate to clearing processes: lack of transparency, linked to variations in practice, and the process by which financial institutions can earn revenue from the 'float' available when standing orders, telephone and internet payments are processed'. These issues were discussed at the initial round tables and followed up in the subsequent bi-lateral meetings.

#### **3.3.1 Transparency of the clearing cycle**

The OFT has proposed (and subscribers agree) that the Code should provide for greater transparency and clarity about the BACS clearing processes. There was widespread support for this. It has also been suggested that the Code should either incorporate a ceiling on clearing times or, as most subscribers operate to the same cycle of passing value on day 3 (T+2), explain the normal clearing time and include a commitment to explain when there is any deviation from this.

I note that APACS and a working group of the Banking Code Advisory Panel are considering ways of incorporating greater transparency into the Codes.

***I recommend that paragraph 9.4 of the Codes and its accompanying Guidance be revised to provide an explanation of the clearing process for standing orders and telephone and internet payments, rather than a commitment to do so. This should include a reference to clearing normally taking three days, with a commitment to tell customers 'if extra days are added to this'. It should also include a commitment to tell new customers when they can draw on cheques that they pay into their account. The Guidance should include a reference to the new APACS booklet on the cheque clearing cycle and the one on BACS payments that is in preparation.***

#### **3.3.2 Payment of interest on 'float'**

The more contentious issue was the question of 'float'. Additional revenue is being earned by almost all banks and building societies on customers' funds as a consequence of the clearing processes for standing orders and telephone and internet payments, and can be earned as an indirect consequence of the cheque clearing process. The OFT calculates that the total customer detriment is around £30 million a year; this figure is, however, disputed by the banks who quote a lower figure - £6 million.

The OFT has proposed that customers should continue to earn interest on funds ‘earmarked’ in their account for standing orders and telephone and internet payments until that money is actually transferred. In most cases this would normally mean an additional two days interest – but only if the current account pays interest. They also propose that all banks and building societies should pay interest on cheques deposited into accounts from the ‘normal’ date of clearance, three days after they have been deposited. One bank has already taken a decision to pay interest on ‘float’ to their personal customers and propose to extend it to their business customers as well.

At the same time, the OFT has established a Payments Systems Task Force which will ‘*identify, consider and seek to resolve any efficiency, competition, and incentive issues relating to payment systems.*’ They will be meeting at least quarterly for four years, with working groups taking forward specific areas. The OFT has indicated that the original terms of this Task Force did not include the issue of ‘float’, although it will be investigating ways of achieving improved methods of payment transfer. Indeed one of the first working groups to be set up is one looking at ways of improving the BACS system. In its consultation paper it notes that developments are already in place to improve the CHAPS and BACS systems.

Subscribers have indicated that introducing systems to enable them to pay ‘float’ will involve investment that is additional to those required to improve and speed up the payment process. Most are reluctant to invest in the first, when they see the second as almost inevitable. It should, however, be noted that the systems investment to pay interest on float is a good deal less than the investment needed to improve clearing systems generally. Consumer groups feel that the current situation is unfair to consumers but, on balance, would prefer the clearing process to be speeded up.

These are important issues but require a level of investigation that is considerably beyond the resources of the independent reviewer of the Banking Code.

***I therefore recommend that the Office of Fair Trading explore this issue further and that the outcome is subsequently incorporated into the Code, if appropriate.***

### **3.4 Account switching and small businesses**

When the previous review was completed, bilateral discussions were still taking place between the Office of Fair Trading and the eight main clearing groups on the ‘behavioural remedies’ recommended by the Competition Commission report on small business banking<sup>8</sup>. The eight main clearing banks have now agreed to set of bilateral undertakings on targets relating to the switching of current accounts of small businesses<sup>9</sup>. The detail of these undertakings differs from bank to bank.

---

<sup>8</sup> Competition Commission *The supply of banking services by clearing banks to small and medium-sized enterprises*. 2002.

<sup>9</sup> For further details see:

<http://www.gnn.gov.uk/gnn/national.nsf/0/981FB7FD165848C680256DCC0047A649?opendocument>

These include undertakings:

- On targets for account switching
- Not to charge for closing or switching an account
- Not to impose a penalty charge for terminating a loan when a customer switches a current account
- To publish policy on paying legal/valuation charges for transfer of any security
- To provide a portable credit history within five working days, with the first two copies provided free of charge.
- To provide compensation for failing to meet targets if customer suffers loss and it is the bank's fault.
- Not to require customers to hold a current account to obtain a deposit account or loan

I was asked to consider which, if any, of these should be included in the Business Banking Code. I discuss each, in turn, below.

#### **3.4.1 Account-switching targets**

During detailed discussion, it became clear that the precise nature of the undertakings on targets and definition for account switching varied between the eight clearing banks that had signed them. This complicates their inclusion in the Business Banking Code. Moreover, including them in the Code defeats their original purpose: to promote greater competition.

#### **3.4.2 Charges for account-switching**

There was general agreement that no charges should be made for the closing or switching of accounts – and that this should apply to personal customers as well as small business ones.

During the course of the consultation, however, it has become apparent that a minority of subscribers may be making charges to cancel standing orders and direct debits before switching an account.

*I recommend that a new paragraph should be added to section 7 of both the Banking Code and the Business Banking Code giving a commitment not to make any additional charges for either closing or switching an account. The corresponding paragraph of the Guidance should indicate that this includes additional charges to close standing orders or direct debit payments. It will be essential to ensure that this does not conflict with the Undertakings from individual banks to the Competition Commission.*

#### **3.4.3 Penalty charges for terminating a loan at the same time as switching a current account**

While there was agreement that there should be no specific charge linked to terminating a loan (as defined in the undertakings) at the same time as switching a current account, subscribers argued that early settlement fees allowed within the Consumer Credit Act



should be permitted. The undertakings do not include commercial mortgages and foreign currency loans within the definition of a loan.

***I recommend that the Business Banking Code Guidance on not making charges for account switching should also make clear that it also refers to any charges, other than early settlement fees, for loans. Again, it is essential to ensure that this does not conflict with the Undertakings from individual banks to the Competition Commission.***

#### **3.4.4 Legal/valuation charges for transfer of security**

There was general agreement that the Business Banking Code should give a commitment to tell small businesses the policy on legal and valuation charges for the transfer of any security.

***I recommend that a new commitment is inserted in section 7 of the Business Banking Code to tell customers the bank's policy on paying legal/valuation charges for transfer of any security they hold on behalf of a business customer.***

#### **3.4.5 Portable credit histories**

The Business Banking Code already includes a commitment to provide credit histories on request in paragraph 7.2. The undertaking signed by the eight main clearing banks goes further than this and says that the first two requests a year should be met free of charge.

Detailed discussions with the eight banks that have signed this undertaking showed that the demand for portable credit histories has been incredibly small and out of all proportion to the costs of developing the technological systems to deliver them. One bank had received five requests but invested a seven figure sum on the systems to enable them to comply fully with the undertaking. In view of this:

***I recommend that paragraph 7.2 of the Business Banking Code, dealing with credit histories, remains unchanged.***

#### **3.4.6 Compensation**

As the undertakings setting targets for switching will not be included in the Business Banking Code it follows that it is not possible to include a commitment to pay compensation for failing to meet them. In any case, neither Code covers the issue of compensation for failure to comply with other commitments. Customers can, however, seek compensation through a complaint to the Financial Ombudsman Service.

#### **3.4.7 Not requiring customers to hold a current account to obtain a deposit account or loan**

This undertaking does not seem to present problems for banks who have not signed a bilateral undertaking with the Office of Fair Trading.

***I propose that paragraph 7.1 of the Business Banking Code includes a commitment not to require customers to hold a current account to obtain a deposit account or loan.***

### 3.5 Branch closures

Paragraph 7.6 of the Codes was not revised in line with the recommendation made in the previous review and a number of submissions drew attention to this and made a range of additional proposals relating to branch closures.

*I recommend a number of changes to paragraph 7.6. First, the radius for the extended notification for closure of last branches should be reduced to 1 mile in urban areas and no more than four miles in rural ones, with the Guidance making it clear that this distance is by road, not as the crow flies. Second, the Guidance should make it clear that 'closure' includes replacing all counter services with automated provision. Thirdly, the Guidance should make it clear that telling people 'how we will continue to provide banking services to you' should be specific to provision in the locality of the branch, not just a generic statement of the channels through which banking services are provided. Fourthly, there should be a commitment to give notice of any substantial reduction in opening hours, with substantial being defined as a 50 per cent reduction or more. The Guidance on these notifications should mirror the provisions for branch closures. Finally, the Business Banking Code should also include a commitment to tell small businesses affected by closures about Inter-Bank Agency Agreements where these exist.*

### 3.6 Relationship between legislation, FSA rules and the Banking Codes

Early in the consultation, Code sponsors raised the issue of how the Banking Codes should deal with new legislation and FSA rules. Three examples of this are relevant to the current review: Unfair Terms in Consumer Contracts Regulations; the FSA rules implementing the Distance Marketing Directive (in October 2004) and legislation relating to the Child Trust Fund. Looking further ahead, there is the Unfair Commercial Practices Directive which is likely to be transposed into UK law in 2006/7.

Clearly the Codes should comply with all relevant legislation; the initial round tables discussed in some detail whether the Code include reference to rights and responsibilities conferred by legislation or restrict itself to rights and responsibilities that go beyond that legislation.

The general view was that, where appropriate, brief reference should be made to legislation, but the Code and Guidance should not go further than this. In view of this:

*I recommend that reference be made the Child Trust Fund legislation in the Guidance to section 3.3 of the Banking Code. A new paragraph should be inserted after paragraph 6.2 in the Banking Code stating that subscribers comply with the Distance Marketing Directive and explaining briefly what rights it confers. The Guidance should include a reference to the FSA rules.*

*If necessary, the wording of the Code and Guidance should be revised to take account of the Credit Advertising and Form and Content of Agreements Regulations that will be introduced in October 2004.*

*Code sponsors should also investigate whether it is appropriate to refer to the FSA financial promotion rules regarding the marketing of structured capital at risk products.*

## **4 Less extensive revisions**

In addition to the issues covered above, submissions to the review have also proposed changes to a large number of other sections of the Code. My recommendations are listed below under the section of the Code to which they apply.

### **4.1 Section 3 Helping you choose...**

Paragraph 3.2 (Business Banking Code only) should be revised to include a commitment to tell people how they can get information on Inter-Bank Agency Arrangements, including the charges made for them.

### **4.2 Section 5 Charges**

Paragraph 5.2 (Business Banking Code only) should include a reference to the Business Account Finder on the BBA's web site.

Paragraph 5.3 (5.4 in the Business Banking Code) on changes to charges needs to be revised to bring it into line with Paragraph 6.4 changes to terms and conditions.

Paragraph 5.4 There are errors in the Guidance in Table 5 on p24. The heading of column 3 should refer to section 5.4 not 5.5 and the heading of column 4 should refer to section 5.5 not 5.6.

Paragraphs 5.7 and 5.8 (Business Code only) were inserted in the 2003 edition of the Code. Consultation identified no problems and no need for further revision

### **4.3 Section 6 Terms and conditions**

Paragraph 6.1 and the accompanying Guidance should refer to the requirements of the Distance Marketing Directive.

Paragraph 6.2 and the accompanying Guidance should refer to terms and conditions also being legible. I have considered whether or not this should refer to a minimum point size, but decided this alone would not be sufficient as legibility also depends on the font used, the contrast between text and background, word spacing and line length. One possibility is for the Guidance to say that the text should be easy to read by someone with normal or corrected eyesight.

### **4.4 Section 7 Changing your account**

Paragraph 7.5 Closing your account. The Codes should indicate the type of circumstances that are not considered 'normal' – the Guidance currently refers to fraud and being threatening or abusive to staff.

#### **4.5 Section 8 Advertising and marketing**

Paragraphs 8.1 and 8.2 The Guidance should make reference to the provisions in the Consumer Credit (Advertisement) Regulations 2004 and ensure that advertising and marketing do not encourage irresponsible borrowing.

Paragraph 8.6 Insurance: The Guidance on this paragraph should include a reference to the FSA Conduct of Business Rules on General Insurance.

#### **4.6 Section 9 Running your account**

A new section should be inserted on sponsors dormant accounts schemes, explaining that the money in such accounts remains the property of the account holder and a giving a commitment to tell customers how to access the money in their dormant account. It should also refer to section 16 giving details of how customers can obtain tracing forms. The Guidance should refer to the BBA, BSA and NS&I dormant account schemes.

Paragraph 9.2 Statements: The paragraph excluding fixed-rate fixed-term loans from annual statements creates problems for consumers and leads to complaints to the Financial Ombudsman Service that would not, otherwise, arise. This exclusion should be removed as soon as the necessary systems can be put in place, and ideally ahead of the new Consumer Credit Act, which will not come into force until 2006, at the earliest.

Paragraph 9.6 (9.12 Business Banking Code) The Guidance on this paragraph needs to be expanded, including: what information need to be given to consumers about the Direct Debit Guarantee and telling subscribers where they can obtain further information about it.

Paragraph 9.11 should be revised to require greater transparency on exchange rates and fees relating to overseas transactions. The Guidance should also be revised to cover currency accounts

#### **4.7 Section 12**

A new sub-section should be inserted dealing with dormant accounts, alerting customers to the fact that they should tell the providers of their accounts when they move home and referring to section 16 giving details of how customers can obtain tracing forms.

A new sub-section should be inserted dealing specifically with on-line banking.

In the Business Banking Code only, reference should be made to the APACS Cardwatch web site and how to report credit card fraud.

#### **4.8 Section 13 Lending**

Paragraph 13.1 of the Business Banking Code should include a commitment to tell customers about the Small Firms Loan Guarantee scheme if the subscriber is a member of the scheme and if it is appropriate to the lending needs of the customer.

#### **4.9 Section 16 Further information**

Reference needs to be made in this section to:

- The Financial Services Compensation Scheme
- Dormant account schemes operated by the BBA, BSA and NS&I
- The APACS Cardwatch web site

## 5 Future Code reviews

It was originally intended that the Codes should be reviewed every two years. At the previous review it was felt that this might be too frequent and agreed that the timetable should be re-considered in the light of experience. The consultation indicated a division of opinion. Code sponsors and subscribers and one consumer organisation thought that reviews should occur less frequently: say every three years. Others, including the Banking Code Standards Board, felt that the current frequency is appropriate.

I have every sympathy with Code sponsors and subscribers, as the present review process began only nine months after the new Code had been introduced and, in some areas (for example the downgraded accounts section) insufficient time had elapsed to permit a detailed assessment of how revisions to the Code were working. However, the number of changes needing to be considered in this review would suggest that it would be inappropriate to consider lengthening the time between reviews.

In the course of this review, it has become apparent that there is a need for a mechanism to deal with urgent matters that occur between formal reviews and that the Banking Code Standards Board has produced a paper on handling changes to the Code and Guidance between formal Code reviews. This issue was discussed at the final round table and further submissions invited on:

- Whether or not there is a need for interim reviews
- What they should cover
- Who should initiate them
- Whether or not the independent reviewer should chair them
- The implications for the time frame for formal reviews.

On balance, the people who responded agreed that:

- Provision needs to be made for interim reviews
- These should be restricted to any new issue or circumstances involving material consumer detriment.
- Code sponsors and/or the Banking Code Standards Board should be able to initiate them.
- They should be chaired by the independent reviewer who will also arbitrate if there is any dispute about whether an interim review is needed.
- The frequency formal reviews could be extended to three years, but only if there is a robust system for informal reviews. The final decision on whether to extend the time frame should be taken in November 2005, after reasonable consultation with stakeholders.

*I, therefore, recommend provisionally that formal reviews should be held every three years, but only if two safeguard are in place. First, there should be a fast track procedure for Code amendments between the formal reviews. These interim reviews should deal with areas of material consumer detriment not adequately covered by the Code, be initiated by either the BCSB or Code sponsors and be overseen by the independent reviewer, who will also arbitrate if there is any dispute about the need for an interim review. Secondly, the final decision on the time frame for reviews should be made in November 2005, following consultation with stakeholders through the independent reviewer.*