Competition and the banking crisis

Standard Note: SN/BT/5272
Last updated: 13 January 2010
Author: Louise Smith
Section Business and Transport Section

Since the beginning of the financial crisis a large number of financial institutions both in the UK and abroad have been assisted by state interventions, for example, capital injections and state guarantees on bank liabilities. The European Commission estimates that the UK financial sector as a whole has been "propped up by £1.26 trillion of government support."

The European Commission is responsible for state aid control. Its main aim is to ensure that government interventions do not distort competition and trade inside the EU. For that reason there is a general prohibition on state aid, but to which there are exemptions. In response to the financial crisis the Commission published a number of Communications to provide guidance to Members States on use of state aid in response to the crisis.

State aid was not the only response to the financial crisis: a number of mergers and acquisitions have also taken place in the financial sector. There is concern that contraction in market and a reduction in competition may start to have a detrimental impact for consumers of certain products, such as mortgages, personal accounts and business banking.

In order to meet EU state aid approval, some banks which have received a large amount of state aid support – Northern Rock, the Royal Bank of Scotland and Lloyds Banking Group – have all announced restructuring plans. This will mean that the eventual sale of certain banking products, brands and bank branches from these groups.

Concern in the press has focussed on lack of competition in banking products and what happens for customers when bank branches are closed. Consumers with competition concerns should first contact a consumer group, such as Consumer Focus. Consumer Focus has the power to make a super-complaint to the Office of Fair Trading, which has a number of powers at its disposal and can make a reference for further investigation to the Competition Commission. In relation to branch closures, industry guidance about how banks should behave is published by the British Bankers' Association.

This note sets out to: provide further information on the state aid rules and assistance to the financial sector; explain some of the competition concerns; and set out briefly the powers of the competition authorities to address such concerns.

This information is provided to Members of Parliament in support of their parliamentary duties and is not intended to address the specific circumstances of any particular individual. It should not be relied upon as being up to date; the law or policies may have changed since it was last updated; and it should not be relied upon as legal or professional advice or as a substitute for it. A suitably qualified professional should be consulted if specific advice or information is required.

This information is provided subject to our general terms and conditions which are available online or may be provided on request in hard copy. Authors are available to discuss the content of this briefing with Members and their staff, but not with the general public.

Contents

1 Government Aid **2**

1.1 State Aid and EU rules 3

2 Change in the retail banking market **6**

3 Future changes to the banking market **10**

4 Bank customers **12**

4.1 Competition concerns 12

4.2 Changes to bank branches 15

1 Government Aid

The Bank of England dates the beginning of the financial crisis in the UK to 5 March 2007, when HSBC announced that one portfolio of sub-prime mortgages showed much higher default levels than had been built into the pricing of the product.[1]

The uncertainty surrounding the credit risk of individual financial institutions had a detrimental effect on the market of interbank lending. It made access to liquidity progressively more difficult for financial institutions across the board. This difficulty was particularly shown in the period from Friday 14 September 2007 to Monday 17 September which saw the first run on the retail deposits of a United Kingdom bank, Northern Rock, since Victorian times.[2]

The global financial crisis impacted heavily on the banking sector. In response to it governments have intervened, through a variety of measures, to support their financial systems. A December 2009 report by the National Audit Office sets out the levels of UK government aid to the banking sector:

> The scale of the support provided by the taxpayer is unprecedented in modern times. In addition to the support provided to Northern Rock, the Treasury:
>
> - purchased £37 billion of shares in RBS and Lloyds Banking Group (£2.5 billion of preference shares in Lloyds Banking Group were subsequently redeemed), and in November 2009, agreed to purchase up to an additional £39 billion of shares in both of these banks;
> - indemnified the Bank of England against losses incurred in providing over £200 billion of liquidity support;
> - agreed to guarantee up to £250 billion of wholesale borrowing by banks to strengthen liquidity in the banking system;
> - provided approximately £40 billion of loans and other funding to Bradford & Bingley and the Financial Services Compensation Scheme; and

---

1 Bank of England, *Financial Stability Report Issue No. 24*, October 2008, annex

2 House of Commons Treasury Committee, *The run on the Rock*, Fifth Report of Session 2007–08, HC 56-I, 26 January 2008, p3

- agreed in principle in January 2009 to provide insurance covering nearly £600 billion of bank assets, reduced to just over £280 billion in November 2009.

The Treasury's net cash outlay for purchases of shares in banks and lending to the banking sector, including Northern Rock, will, after allowing for measures announced in November 2009, amount to about £117 billion.[3]

According to the EU Competition Commission in June 2009 the UK financial sector as a whole was "propped up by £1.26 trillion of government support".[4]

1.1 State Aid and EU rules

State aid is defined by the European Commission as "an advantage in any form whatsoever conferred on a selective basis to undertakings[5] by national public authority."[6] The UK government is not alone in providing state aid to its financial sector: the Commission has recently considered over 100 state aid applications from across Member States in connection with assistance for financial institutions.[7] An overview of national measures adopted in 2008 and 2009 in response to the financial crisis is available from the European Commission website.[8]

The objective of State aid control is to ensure that government interventions do not distort competition and trade inside the EU. There is a general prohibition on state aid, but there are a number of policy objectives with which state aid is compatible. The decision regarding the applicability, or not, of these exemptions to the general prohibition of State aid rests exclusively with the European Commission. The Commission's concern is that state aid can have a detrimental effect on competition, particularly where Member States act independently within the context of the EU single market. The Commission has explained these concerns in the context of national interventions in the banking sector:

State-financed bail-outs have various negative effects. State interference:

- goes against the principle of competition on merits;
- reinforces the market power of the aid recipient;
- reduces dynamic incentives of non-aided competitors;
- encourages moral hazard and excessive risk-taking; and
- undermines the Single Market.

All these effects are still present in times of crisis. Moreover, there are additional reasons why the competition rules are more important than ever during a systemic crisis.

---

[3] National Audit Office, *Maintaining financial stability across the United Kingdom's banking system*, HC 91 Session 2009–2010, 4 December 2009, summary page 5

[4] Neelie Kroes European Commissioner for Competition, *Did government interventions help in the crisis? Address at International Banking Conference of British Bankers Association London*, SPEECH/09/324, 30 June 2009

[5] The term "undertakings" does not have an official or legal definition. It is generally used to mean organisations engaged in economic activity.

[6] European Commission, *Competition State Aid website* [on 12 January 2009]

[7] Neelie Kroes, European Commissioner for Competition Policy, *Keynote address at conference organised by EStALI (European State Aid Law Institute)* London, 27 November 2009

[8] European Commission, *State aid: Overview of national measures adopted as a response to the financial/economic crisis*, Memo 09/499, 12 November 2009

> First, if on the one hand, for reasons of financial stability, a more limited contribution of the bank and its shareholders to the cost of the restructuring has to be accepted, on the other hand, it is vital to pave the way for a rapid return to normal market conditions. This requires that moral hazard is properly tackled to avoid repeating the mistakes of the past.
>
> Second, banks and Member States across Europe have been hit by the crisis by very different degrees. In a situation of financial, economic and budgetary crisis, differences between Member States in terms of resources available for state intervention become even more pronounced. And those banks which today need huge subsidies may have in recent years engaged in expansionary strategies to the detriment of their competitors.
>
> Finally, national interventions in the current economic crisis are by their nature bound to promote a focus on national markets. Even where there is no explicit requirement of lending to the domestic economy, there is a risk of promoting retrenchment into national boundaries. This would hinder the functioning of the Single Market for financial services, create entry barriers and reduce incentives for cross-border activities to the detriment of European businesses and consumers.[9]

State aid control is laid down under what was Article 87 of the *Treaty of the European Community*. This is now renumbered as Article 107 in the *Treaty on the Functioning of the European Union* (better known as the Lisbon Treaty), which entered into force on 1 December 2009.[10] State aid to Member States and to individual undertakings in difficulty is normally assessed under Article 107(3)(b) and (c):

> 3. The following may be considered to be compatible with the internal market:
>
> [...]
>
> (b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;
>
> (c) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;

EU Commission guidelines on state aid for rescuing and restructuring firms in difficulty (hereafter the Guidelines) also articulate the Commission's understanding of these rules.[11] The Guidelines make clear that derogation from these rules should be strictly limited:

> The exit of inefficient firms is a normal part of the operation of the market. It cannot be the norm that a company which gets into difficulties is rescued by the State. Aid for rescue and restructuring operations has given rise to some of the most controversial State aid cases in the past and is among the most distortive types of State aid. Hence, the general principle of the prohibition of State aid as laid down in the Treaty should remain the rule and derogation from that rule should be limited.[12]

---

[9] State aid: *Commission presents guidelines on restructuring aid to banks - frequently asked questions*, MEMO/09/350 23 July 2009

[10] *Consolidated Version of the Treaty on the Functioning of the European Union*, Official Journal of the European Union, 9 May 2008, C 115/47

[11] Official Journal of the European Union, *Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty* 2004/C 244/02

[12] Official Journal of the European Union, *Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty* 2004/C 244/02, para 4

In response to the financial crisis, the EU Commission has issued several Communications to provide guidance to Members States in their efforts to resolve the situation by using state aid:

- the "Banking Communication" adopted on 13 October 2008 which provided a European framework to allow rescue operations in order to stop or prevent runs on financial institutions; [13]
- the "Recapitalisation Communication" of 5 December 2008 which identified a set of standards and safeguards to allow Member States to recapitalise banks in order to ensure adequate levels of lending to the economy; [14]
- the "Impaired Assets Communication" of 25 February 2009 which provides the framework for the clean-up phase of financial institutions' balance sheets in relation to removing toxic assets and underperforming loans;[15]
- the Communication on a "temporary framework" for state aid measures to support access to finance in the current financial and economic crisis, adopted on 17 December 2008 and amended on 25 February 2009;[16] and
- the "Restructuring Aid Communication" of 23 July 2009 on the return to viability and assessment of restructuring measures in the financial sector in the current crisis under the state aid rules, 23 July 2009.[17]

The Communications show that the Commission has recognised that the severity of the crisis justified the granting of aid. In a keynote speech to the European State Aid Law Institute in November 2009, the EU Competition Commissioner, Neelie Kroes, said that the rules relating to state aid were not being bent on demand, but were able to provide "flexibility built on principle".[18] The Commission explains that its primary rationale in relation to financial services state aid is to:

> ensure that rescue measures can fully attain the objectives of financial stability and maintenance of credit flows, while also ensuring a level playing-field between banks located in different Member States as well as between banks which receive public support and those which do not, avoiding harmful subsidy races, limiting moral hazard and ensuring the competitiveness and efficiency of European banks in Community and international markets.[19]

The Commission made clear that any state aid should be in line with the general principles as set out in the 2004 Guidelines:

---

[13] Communication from the Commission – *The application of the State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis*, OJ C 270, 5 October 2008, p. 8–14

[14] Communication from the Commission– *The recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition,* OJ C 10, 15 January 2009, p. 2-10

[15] Communication from the Commission on *the Treatment of Impaired Assets in the Community banking sector*, of 25 February 2009, OJ C 72, 26.3.2009, p. 1.

[16] Communication from the commission — *Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis*, OJ C 83 7 April 2009

[17] Commission Communication on *the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules*, 23 July 2009

[18] Neelie Kroes, European Commissioner for Competition Policy, *Keynote address at conference organised by EStALI (European State Aid Law Institute)* London, 27 November 2009

[19] Commission Communication on *the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules*, 23 July 2009, para 2

> Moreover, in line with the general principles underlying the State aid rules of the Treaty, which require that the aid granted does not exceed what is strictly necessary to achieve its legitimate purpose and that distortions of competition are avoided or minimized as far as possible, and taking due account of the current circumstances, all general support measures have to be:
>
> - well-targeted in order to be able to achieve effectively the objective of remedying a serious disturbance in the economy,
> - proportionate to the challenge faced, not going beyond what is required to attain this effect, and
> - designed in such a way as to minimize negative spill-over effects on competitors, other sectors and other Member States.[20]

State aid interventions in the banking sector have taken a number of forms across the EU. The main ones, as defined by the Commission, are:

> - Recapitalisation: all capital injections, either via a national scheme or via an ad hoc individual rescues; acquisitions of stakes by the governments in the banking sector.
> - Guarantee: all state guarantees on bank liabilities (bond issuance), coverage of the guarantee may vary from one country to another.
> - Assets: all interventions aiming at asset relief, i.e. toxic and impaired assets, "bad banks".
> - Liquidity: all interventions aiming at supporting liquidity and providing extra financing to the bank thanks to a state guarantee. This includes a broad range of interventions, such as liquidity facilities at central banks when there is an explicit guarantee by the state, loans or high quality assets swaps. This category also includes measures supporting the supply of credit to the real economy via banking intermediation.[21]

The latest figures from the Commission, dated August 2009, set out the levels of EU state aid to the banking sector:

> In the period from October 2008 until mid-July 2009 the Commission approved 11 guarantee schemes, 6 recapitalisation schemes and 5 schemes providing for both guarantees and recapitalisation. In addition, 40 State aid measures were approved outside the schemes. The total volume of the approved guarantee measures amounts to €2.9 trillion and the recapitalisation measures amount to €313 billion.[22]

2 Change in the retail banking market

State aid was not the only response to the financial crisis; a number of mergers and acquisitions also took place within the market. The OFT summarises:

> In the UK, one of the most important changes to the financial landscape was the large-scale investment by the government in the Lloyds Banking Group and the Royal Bank

[20] Communication from the Commission – *The application of the State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis*, OJ C 270, 5 October 2008, para 15

[21] European Commission, *DG Competition's review of guarantee and recapitalisation schemes in the financial sector in the current crisis*, 7 August 2009, annex 2

[22] European Commission, *DG Competition's review of guarantee and recapitalisation schemes in the financial sector in the current crisis*, 7 August 2009, p2

of Scotland Group (RBSG). This followed the announcement of the anticipated merger between Lloyds TSB and Halifax Bank of Scotland. The government also nationalised the mortgage book of Bradford & Bingley following its collapse, its branch network and savings business were sold to Banco Santander. At the time of writing, Government owns significant shareholdings in the Lloyds Banking Group and RBSG, wholly owns Northern Rock and owns Bradford & Bingley's mortgage book.

Additional changes include:

- the acquisition of Alliance & Leicester by Banco Santander
- the acquisition of the Cheshire and Derbyshire building societies by Nationwide, and
- the Britannia building society anticipated to soon merge with Cooperative Financial Services.[23]

Since the publication of this report, the Yorkshire Building Society has also acquired the Chelsea Building Society.[24]

Part of the OFT's work is to obtain and review information relating to merger situations.[25] Under part 3 of the *Enterprise Act 2002*, most mergers above a certain size and which meet one of two thresholds (set out below) are referred to the Competition Commission (CC) by the OFT for a full inquiry into the competition effects. The mergers may be either completed (that is, may have happened already) or anticipated. The OFT must normally make a reference to the CC if it believes that there is or may be a relevant merger situation that has resulted or may be expected to result in a "substantial lessening of competition". A relevant merger situation is created if one of the following thresholds is met:

- the value of the UK turnover of the enterprise acquired (or to be acquired) exceeds £70 million (the turnover test); or
- the share of supply of goods or services in the UK or in a substantial part of the UK held (or to be held) by the merged enterprise is at least 25 per cent (the share of supply test).

> If at least two-thirds of the group [of CC members appointed to consider the merger] decide both questions in the affirmative, there is an anti-competitive outcome from the merger and the CC must go on to consider remedies.[26]

None of these mergers have been referred to the Competition Commission. The OFT's reasoning in each case is published on its *website*; the main reason for non-referral appears to be that the OFT has not found evidence to believe that there would be a substantial lessening of competition.[27] For further information about the Lloyds TSB and HBOS merger see Library Standard Note: *The Lloyds-TSB and HBOS Merger: Competition Issues*, SN/BT/4907,15 December 2008.

---

[23] Office of Fair Trading, *Financial Services Strategy: A consultation document*, April 2009, Annex B para11 and 12

[24] "Yorkshire seals Chelsea merger deal" *Financial Times*, 3 December 2009

[25] Office of Fair Trading, *Mergers: substantive assessment guidance*, May 2003, para 1.6

[26] Competition Commission, *CC4 – General Advice and Information*, March 2006, p11

[27] See for example, OFT, *Anticipated merger between Co-operative Financial Services Limited and Britannia Building Society* , No. ME/4008-09, February 2009

Lord Saatchi recently asked the government to provide information of the UK market share of the top five companies in: a.) retail banking; b.) corporate banking; c.) mortgages; d.) insurance and re-insurance; e.) government bond issues; f.) foreign exchange; and g.) credit swaps and derivates. The government responded that the information requested could be provided only at disproportionate cost.[28] Lord Saatchi explained his question in the *Financial Times* saying he had concerns that these companies had between an 80 -100% market share in these products and that as a consequence, competition was "almost over."[29]

Some figures are available, however. The Council of Mortgage Lenders (CML) publishes statistics every year showing the largest mortgage lenders. Using the CML data, the following table shows the largest mortgage lenders for 2006, 2007 and 2008, by gross mortgage lending in a calendar year.

Table 1: Top five mortgage lenders 2006-2008 by gross mortgage lending in year

2006

Rank	Name of Group	£bn	Estimated market share
1	HBOS	73.20	21.20%
2	Abbey	32.60	9.40%
3	Northern Rock	29.00	8.40%
4	Lloyds TSB	27.60	8.00%
5	Nationwide BS	21.10	6.10%
Total market share			53.10%

2007

Rank	Name of Group	£bn	Estimated market share
1	Lloyds Banking Group	102.50	28.20%
2	Santander	48.60	13.40%
3	Nationwide BS	35.20	9.70%
4	Northern Rock	29.50	8.10%
5	Barclays	23.00	6.30%
Total market share			65.70%

2008

Rank	Name of Group	£bn	Estimated market share
1	Lloyds Banking Group	78.00	30.30%
2	Santander	35.20	13.70%
3	Nationwide BS	29.00	11.20%
4	Barclays	22.90	8.90%
5	The Royal Bank of Scotland	18.70	7.30%
Total market share			71.40%

Source: CML Statistics

[28] HL Deb 2 December 2009, c 45WA

[29] "Only competition can safeguard free markets", *Financial Times*, 25 November 2009

The table shows that, not only have the top five companies changed since 2006, but that their combined market share has gone from just over half, to nearly three quarters of the mortgage market. The CML speculates that the figures for 2009 may show even further contraction in the market and an increase again in market share for the largest companies:

> With so many lenders either merging or ceasing lending, this year's largest lenders' table has changed more than in other years. For gross lending in the year, there are significant changes throughout the table. Some larger lenders, most particularly in the specialist sector, have dropped a number of places down the list or been replaced by names not seen in the list before.
>
> While some specialist lenders remain in the list for last year, we would expect shrinkage of this sector to continue while current market conditions persist. Even if conditions in wholesale markets improve this year, the backwards looking nature of our largest lenders' table means that we would expect next year's data to show that the specialist lending sector has shrunk further. Meanwhile, the lending commitments from the nationalised and part-nationalised banks suggest yet more growth in market share for this sector. And, of course, we may not have seen the end of the current wave of consolidation. So, next year's table is likely to look different again, with more new names and an even larger market share in the hands of the largest firms.[30]

The *Financial Times* examined the market share of other financial products and the effect on competition:

> The big four UK banks - Lloyds Banking, Royal Bank of Scotland, Barclays and HSBC - have about 75 per cent of individual current accounts, according to the British Bankers' Association. On the business side, they have an even stronger grip, with almost 90 per cent of accounts, according to the Federation of Small Businesses.
>
> "The major high street banks have such a monopoly and it is very difficult for smaller operators to wedge themselves in," says Stephen Alambritis, a spokesman at the FSB. "It is also very difficult for business customers to switch from one account to another, even if there is more competition."[31]

At the time of the Lloyds TSB and HBOS merger, the OFT expressed concern about the loss of a large bank in the market; in particular that Lloyds would no longer have enough incentive to compete for new customers, which in turn would cause it focus on making more profit from existing customers:

> In relation to PCAs [personal current accounts], the OFT has concerns at the national (Great Britain) and local levels. The merger will remove a firm, HBOS, that was (at least until less than two months ago) a major driver of competition in the market, and strengthen the current market leader, Lloyds. In addition, the merger will significantly increase Lloyds' share of the market. As a consequence of its increased market share, coupled with characteristics of the market such as high levels of customer inertia and a limited degree of price discrimination, it is expected that its incentives to compete for new customers (and those of the other major banks in the market) will be diminished – in essence, the increase in Lloyds' customer base will encourage it to attach more weight to enhancing margins on current customers than to customer acquisition.[32]

It should be noted that concerns about competition in the financial sector are not new. In 1998 the government set up an independent investigation of banking services in the UK, led

---

[30] CML News and Views, *Largest Mortgage Lenders 2008*, issue 16, 18 August 2009

[31] "New groups emerging out of the drive for competition" *Financial Times*, 23 December 2009

[32] Ibid, p5-6

by Don Cruickshank, former Director-General of OFTEL.[33] The review looked at levels of innovation, competition, and efficiency in the industry and how well it served the needs of business, other consumers and the UK economy. The final report, *Competition in UK Banking*, was published on 20 March 2000. The *Government Response to the Cruickshank Report* was published in August 2000. Further information about the Cruickshank Report and changes that emerged as a result of the report's conclusions are given on the *HM Treasury website*.[34]

3 Future changes to the banking market

On 28 October 2009, the EU Commission approved a business plan for Northern Rock as part of the state aid agreement. It announced that Northern Rock would be restructured and split up into what has been described as a "good" bank and a "bad" bank as follows:

> **Northern Rock plc** – a new savings and mortgage bank that will hold and service all customer savings accounts and some existing mortgage accounts. The bank is proposed to be authorised as a deposit taker by the FSA and will offer new savings products. It will also offer new mortgage lending to support the Government's objective of increasing mortgage supply and sustaining a competitive market. Northern Rock plc will hold some wholesale deposits.
>
> **Northern Rock (Asset Management) plc** – the existing company which is proposed to hold and service the balance of the existing residential mortgage book and, subject to FSA approval, will be regulated as a mortgage provider, not a deposit taking bank. 90% of the mortgages held by Northern Rock (Asset Management) will be fully performing and are not in arrears, and this company would not, therefore, be accurately described as a 'bad' bank. The portfolio will include the Company's interest in those mortgages allocated to the Granite securitisation and covered bond programmes. It will not offer any new mortgage lending.
>
> Northern Rock (Asset Management) will also hold all unsecured loan accounts, the Government loan and Northern Rock's current wholesale funding and subordinated debt instruments.[35]

The *Financial Times* reported that the "good" bank would eventually be sold to a private buyer. The article examined the impact of the restructuring for consumers:

> Mortgage brokers warned that this could be bad news for existing borrowers, as the "bad" bank is not expected to offer competitive rates.
>
> "There is a risk that the standard variable rate (SVR) may become uncompetitive, so those who can't easily remortgage will be stuck with the bad bank," warned Ray Boulger at John Charcol, the broker.
>
> Savers with Northern Rock will lose their 100 per cent deposit guarantee when the "good" bank is sold, making it a less attractive proposition to some savers.
>
> But the restructure could force Northern Rock to offer more competitive rates. "I think it may bring them back into play in the savings market," said Kevin Mountford at Moneysupermarket.com. "The bottom line is increased competition for savers."

---

[33] HM Treasury, *Pre-Budget Report 1998*, 3 November 1998

[34] HM Treasury website, *Financial Services: Banking* [on 12 January 2010]

[35] Northern Rock press release, *European Commission approves State Aid package for Northern Rock*, 28 October 2009

> And the presence of another active lender in the mortgage market should eventually be good news for consumers. Northern Rock has already offered new competitive rates to borrowers in the past few weeks, which is pushing others to lower their rates.
>
> "It is having a positive impact on lending across the piste," said Boulger.
>
> The "good" bank of Northern Rock will not be able to compete freely for mortgages and savings business for at least two years. Its mortgage deals must not appear in a top three position in Moneyfacts' comparison tables unless they offer loan-to-values above 80 per cent or are aimed at first-time buyers. There will be a cap on the overall size of its savings book of £20bn until the end of 2011 which will limit its ability to attract new depositors.[36]

In November 2009 the Royal Bank of Scotland and the Lloyds Banking Group announced plans to sell some of the retail bank branches in order to meet state aid support approval from the European Commission.[37] A press release from the Treasury explains that the approval package will involve the sale of assets from both banks to increase competition in the market:

> The Government has reached agreement in principle with Commissioner Kroes after constructive and helpful discussions on a package of restructuring and other measures, which we are confident will address the concerns of the European Commission. The package is now subject to agreement by the College of Commissioners.
>
> To promote greater competition in the UK banking sector, and as part of the State aid requirements of the European Commission, the Government has agreed restructuring plans for RBS and Lloyds that include the divestment of a significant proportion of their retail and corporate banking assets over the next four years.
>
> To ensure these divestments increase diversity and competition in the UK banking market, the assets can only be sold to small or new players in the market. The divestments from each bank will represent a viable stand-alone entity, together representing nearly 10% of the UK retail banking market.[38]

Lloyds Banking Group has announced a sale of some of its branches in order to meet the conditions for state aid support:

> As a condition of receiving Government support, we expect that we will need to reduce our market share of personal current accounts by 4.6% and also reduce our mortgage assets by up to 19%. This is a requirement from the European Commission.
>
> Because of this we need to prepare to sell a stand-alone banking business which will meet these requirements.
>
> This stand-alone business will include:
>
> - all Lloyds TSB Scotland branches
> - additional Lloyds TSB branches in England & Wales, with Branch Based Customers

---

36 "Rock split to increase competition" *Financial Times*, 30 October 2009

37 "10 per cent of UK banking market up for grabs" *Herald Scotland*, 3 November 2009

38 HM Treasury press release, *Implementation of Financial Stability Measures for Lloyds Banking Group and Royal Bank of Scotland*, 3 November 2009

- all C&G [Cheltenham & Gloucester] branches
- all C&G savings and certain C&G mortgages
- the Intelligent Finance business
- the TSB brand.

In total this package amounts to at least 600 branches.[39]

Royal Bank of Scotland has announced the main elements of its restructuring plan as follows:

- we will reduce our presence in the UK banking sector by divesting the RBS branches in England and Wales and the NatWest branches in Scotland, together with our direct SME customers across the UK and appropriate infrastructure to support this business. This network comprises for the most part what some of you will recall as Williams and Glyn's, and we believe it will be a viable, standalone nationwide banking business.
- we have also agreed to divest, between now and 2013, RBS Insurance, including the Direct Line and Churchill businesses; Global Merchant Services, which is our card payments acquiring business; and our interest in RBS Sempra Commodities, a leading global commodities trader.[40]

4 Bank customers

4.1 Competition concerns

There are several different ways that competition concerns can be addressed, depending on the type of breach and its severity.

The first port of call for individual consumers with concerns would normally be a consumer group. The powers of the consumer group, Consumer Focus include "the right to investigate any consumer complaint if they are of wider interest, the right to open up information from providers, the power to conduct research and the ability to make an official super-complaint about failing services." Contact information for Consumer Focus is available from its website: www.consumerfocus.org.uk/contact-us

A super-complaint is made to the OFT and is defined under section 11(1) of the *Enterprise Act 2002* as a complaint submitted by a designated consumer body that 'any feature, or combination of features, of a market in the UK for goods or services is or appears to be significantly harming the interests of consumers'. Under section 11(2) of the *2002 Act*, the OFT must, within 90 days after the day on which it receives the complaint, publish a response stating how it proposes to deal with the complaint, and in particular:

(a) whether it has decided to take any action, or to take no action, in response to the complaint, and

(b) if it has decided to take action, what action it proposes to take.

If the OFT decides to take no action, the response must state why.

[39] Lloyds Banking Group Announcements, *State aid restructuring announcement* [accessed on 22 December 2009]

[40] Royal Bank of Scotland press release, *The Royal Bank of Scotland Group plc General Meeting Statement*, 15 December 2009

The OFT does not have to wait for a super-complaint to be made before it can begin to investigate a market. Whether by a super-complaint or not, if the OFT suspects that a market is not operating effectively, it can undertake a market study. The OFT has powers to obtain documents and information from businesses suspected of committing an infringement as well as from their competitors, customers or suppliers. It can also enter and (when a warrant is obtained), search premises. Anyone who fails to cooperate with an investigation (e.g. does not respond to a notice or refuses to provide requested information or documents), obstructs OFT officials or hides, destroys or falsifies relevant documents may be guilty of a criminal offence punishable by a fine and/or, in some cases, imprisonment.[41]

For example, the OFT may choose investigate whether there has been an abuses of a dominant position. Section 18(1) of the *Competition Act 1998* prohibits, in certain circumstances, conduct by companies which amounts to an abuse of a dominant position. The prohibition is based however, not on the *holding* of a dominant position in the market, but on the *abuse* of that position. Before deciding if there had been an abuse of a dominant position the OFT must first conduct a detailed examination of the market concerned and the effects of the company's conduct.[42]

Guidance from the OFT sets out by way of example the sorts of practices which may be considered to be an abuse of a dominant position:

> …that conduct may constitute an abuse if it consists of:
>
> (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions
>
> (b) limiting production, markets or technical development to the prejudice of consumers
>
> (c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage
>
> (d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of the contracts.[43]

For further information about abuses of a dominant position, see the OFT's guide *Understanding Competition Law: Abuse of a Dominant Position*, 2004.

The range of remedies available to the OFT will depend upon which anti-competitive provisions have been broken. In general, if the OFT considers that a law has been infringed, it will write to those concerned to explain the case against them and give them a chance to respond, both in writing and by meeting with OFT officials. If it is subsequently decided that there has been a breach of competition law, it will notify the infringing businesses and publish the decision in the Register on the OFT website. It may issue directions (e.g. ordering the business to change or terminate the offending agreement or stop the offending conduct) and if a business fails to comply, it may seek a court order to enforce them. Alternatively, it can conclude that there are no grounds for action. In this case the OFT will notify those concerned and may publish a decision to this effect on its website.[44] More details about the

---

[41] Office of Fair Trading, *Powers of investigation* [on 12 January 2010]
[42] Office of Fair Trading, *Abuse of a dominant position*, 2004
[43] Office of Fair Trading, *Abuse of a dominant position*, 2004, para 2.5
[44] Office of Fair Trading, *Enforcement* [on 12 January 2010]

OFT's enforcement powers are provided in the OFT's guide *Understanding Competition Law Guide: Enforcement*, 2004.

Under section 131 of the *2002 Act*, the OFT may make a market investigation reference to the Competition Commission (CC). The reference can be made where the OFT has reasonable grounds for suspecting that any feature, or combination of features, of a market in the United Kingdom for goods or services prevents, restricts, or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK. Under section 132 of the 2002 Act the Secretary of State for Business, Innovation and Skills can also make a reference. The OFT would generally make a reference to the CC when:

- when it has reasonable grounds to suspect that there are market features, which prevent, restrict or distort competition, but not to establish a breach of the CA98 [*Competition Act 1998*] prohibitions;
- when action under CA98 has been or is likely to be ineffective for dealing with the adverse effect on competition identified.[45]

The CC then has a duty to prepare and publish a report into a market investigation which must be done within two years.[46] If it concludes that there is an adverse effect on competition, section 138(2) of the *Enterprise Act 2002* requires it to take such action as it considers "reasonable and practicable" to prevent these effects on competition and any consequential effects on customers. CC guidance describes some of the remedies available:

> (a) remedies designed to make a significant and direct change to the structure of a market by a requirement, for example, to divest a business or assets to a newcomer to the market or to an existing, perhaps smaller, competitor;
>
> (b) remedies designed to change the structure of a market less directly by reducing entry barriers or switching costs, for example, by requiring the licensing of know-how or intellectual property rights or by extending the compatibility of products through industry-wide technical standards;
>
> (c) as a particular category of (b), recommendations for changes to regulations found to have adverse effects on competition or detrimental effects on customers, for example, by limiting entry to a market;
>
> (d) remedies directing firms (whether sellers or buyers) to discontinue certain behaviour (for example, giving advance notice of price changes) or to adopt certain behaviour (for example, more prominently displaying prices and other terms and conditions of sale)
>
> (e) remedies designed to restrain the way in which firms would otherwise behave, for example, the imposition of a price cap;
>
> (f) monitoring remedies, for example, a requirement to provide the OFT with information on prices or profits.
>
> Most of the examples above are remedies that would fall to the Commission itself to impose. Examples of remedies that would require action by other persons or bodies

---

[45] Office of Fair Trading, *Market investigation references*, March 2006, section 2.3

[46] Section 137(1) Enterprise Act 2002

such as government, regulators and other public bodies include changes to regulations and measures to increase market transparency.[47]

Further information about enforcement powers of the CC is given in part 7 of the CC's guidance document *CC4:General Advice and Information*.

4.2 Changes to bank branches

Industry guidance for banks about what they should do for consumers in the event of a branch closure, is published by the British Bankers' Association:

> **5.5 Branch availability or closure**
>
> If a firm plans to close or move a branch, customers should be notified at least 12 weeks beforehand and told about how the firm will continue to provide retail banking services. This includes providing micro-enterprise customers with information on any inter-bank agency agreements that exist.
>
> This relates to permanent closure, not temporary closures (e.g., due to branch refits). This does not apply where branches merge and are very close together (e.g. in the same or adjacent streets) or where a branch relocates to a very close location, providing customers do not experience the service reductions outlined in the three Guidance bullets below.
>
> If a customer is formally attached to a particular branch (i.e., they have an individual account number and branch, rather than a central or universal, sort code), and that branch is to close, the customer should be given personal notification of at least 12 weeks.
>
> In all cases (i.e. whether customers are formally attached to a branch or not) a prominent notice should be placed in the branch for all customers to see and consideration given to other local advertising and notifying local councils and community groups.
>
> Notifications should provide information on alternative facilities offered by the firm in the locality including, its nearest alternative branch and its nearest free ATM(s). Notifications should also include generic information about other channels through which banking services are provided.
>
> In exceptional circumstances, such as where there have been life-threatening raids, the notification periods may be reduced or waived by the firm although notification should still be given to customers.
>
> Customer notification of at least 12 weeks should also be given where:
>
> - all counter services in a branch are replaced with automated provision; or
> - branch opening hours, are reduced by 30% or more; or
> - access to a branch becomes restricted to a particular group or groups of customer(s).
>
> The 30% reduction in opening hours should usually be measured by reference to the branch's previous opening hours over a working week, but alternative measures in line with the local market are acceptable.

---

[47] Competition Commission, *Market Investigation References: Competition Commission Guidelines*, June 2003, p41

> This section also applies to branch agencies, where it is the firm who chooses to bring the agency agreement to an end (placing notices in the agency may still be dependent on the goodwill of the agent, and may not therefore be possible – although arrangements and agreements made with agents should have been designed to ensure as far as possible their co-operation in complying with this requirement). If the agent defaults or withdraws from the agreement at short notice, it may not be possible for the firm to give the required notice to customers.[48]

It should be noted that the industry guidance is not mandatory. However, it is reviewed by the Financial Services Authority (FSA), which regulates retail banking conduct. The FSA explains the authority of the guidance as essentially one step below that of a rule:

> As now, a firm's defence against us is in essence the same whether they follow FSA guidance or FSA confirmed Industry Guidance –our rules say 'The FSA will not take action against a person for behaviour that it considers to be in line with guidance, other materials published by the FSA in support of the Handbook or FSA-confirmed Industry Guidance, which were current at the time of the behaviour in question.' (DEPP 6.2.1(4)G). Similarly, as Industry Guidance is not mandatory (and is one way, but not the only way, to comply with requirements), we do not presume that because firms are not complying with it they are not meeting our requirements.
>
> However, where a breach has been established, Industry Guidance is potentially relevant to an enforcement case.[49]

The Campaign for Community Banking Services (CCBS) website contains advice and further information for customers who are concerned about the closure of a local bank branch, particularly for those in remote areas: www.communitybanking.org.uk/community.htm

---

[48] British Bankers' Association, *Industry Guidance for FSA Banking Conduct of Business Sourcebook*, December 2009

[49] FSA website, *Confirmed Industry Guidance* [on 12 January 2010]