



# Answering the Charge

## A study of the UK bank charge reclaim crisis

*Likely growth in bank charge reclaim volumes and the readiness of document systems to cope with statement requests within regulatory deadlines*

A research study from Anacomp UK, 2007

### Management Summary

#### Key Findings

- One in every fourteen requests for copy statements in pursuit of claims for a refund of bank charges is not being met within the regulatory 40 days period.
- If just half of the people who are potential claimants, but who have not yet processed a claim, do so, then this figure will rise to one in every nine requests not being answered within the designated timeline.
- Banks are investing to meet the peak in claims-based requests by either duplicating their microfilm archive and employing more people to handle claims, or digitising up to six years worth of statements for ultra-rapid retrieval.
- More strategically-minded banks, however, are not seeing the current reclaim peak as an isolated incident, and are investing in systems which allow a free-flow between microfilm archive and short-term digital systems, so that spikes in enquiry demand can be rapidly accommodated without massive tactical cost in the future.

## Introduction

In February 2007, the Office of Fair Trading stated that, “The Competition Commission's (CC's) remedies in relation to personal current accounts in Northern Ireland are likely to be relevant to the UK as a whole. The codes review should build on the CC's findings and incorporate its remedies. The OFT would welcome the opportunity to provide a supplementary submission on transparency issues in the light of the CC's proposed remedies, which are due to be published shortly<sup>1</sup>.”

Back in May 2005, the OFT referred the supply of personal current bank accounts services in Northern Ireland to the Competition Commission. As a result, in November 2006 the Competition Commission printed their findings. Their report makes it clear that banks are making substantial profits from bank charges. Appendix 4.6 makes it clear that charges from unauthorised overdrafts - which elsewhere in the report are said to include bank charges for refusing direct debits and returning cheques are an important source of profit – may be as high as 9%. An analysis by Credit Suisse has calculated that financial institutions make £1.2bn a year from penalty charges<sup>2</sup>.

In the February 2007 document, the OFT also said that, “There is a fundamental lack of transparency in retail banking, particularly in relation to prices. This encompasses the charging structure that firms use (in particular the reliance placed on hidden charges and the complexities that can arise when calculating interest)<sup>3</sup>, as well as the quality of information they give customers, both existing and prospective... The OFT therefore recommends that both the codes and guidance are amended so that at least 14 days notification is given before all charges and interest are taken from customers' accounts... The UCPD will be implemented on 12 December 2007 by the Unfair Trading (Consumer Protection) Regulations 2007 ('the UTCP Regulations'). These prohibit unfair commercial practices that harm consumers' economic interests... The UTCP Regulations will oblige all businesses not to mislead consumers through acts or omissions, or to subject them to aggressive commercial practices. Of these, the provisions relating to misleading omissions will represent the most significant change since the Banking Code was last reviewed.”

The point of quoting the Office of Fair Trading at such length is to demonstrate that it is not just the hysteria induced by journalistic or lobby group voices that have made the current consumer furore over allegedly unfair bank charges take off with such a head of steam during the end of 2006 and early 2007.

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<sup>1</sup> OFT *response to Banking Codes Review 2007*, February 2007

<sup>2</sup> The Independent, *Now banks are over-charging customers for information about their over-charging*, 3 March 2007

<sup>3</sup> OFT *Consumer Codes Approval Scheme Core Criteria and Guidance*, November 2006.

## **Bank charge reclaims – the current situation**

In layman's terms, if there is a breach of contract under English or Scottish law, any charge should not exceed the cost of the breach. Consumer lobbyists therefore claim that banks should only impose charges which are proportionate to the cost incurred by the bank.

However, when a customer goes over their overdraft limit, or has a cheque or direct debit payment bounce, the bank charges a penalty of up to £30 to £35 a time. The current – as yet unanswered question is - is a charge of this scale really proportionate? Especially since it could simply be a charge for going a few pence over the limit.

The consumer lobby groups believe that, since the bank is fining customers for going over their overdraft limit, and these fines are disproportionate to the consequent costs incurred by the bank, then under the law of penalties this is 'extravagant'. Their argument is that banks' sophisticated systems simply send a computer-generated automatic letter with a franked stamp. A report by BBC2's The Money Programme put a group of former senior bank staff together and they estimated the real cost to be only somewhere between £2.50 and £4.50. However, the counter-argument is that their calculations ignored the major capital investment that British retail banks have sunk into these automated systems in the first place.

It is important to state that no firm legal precedent has yet been set to determine what 'fair' bank charges should be. Hence the OFT's statement that such a determination should be embarked upon by the expert but independent regulatory bodies with all haste. As far as we are aware, almost every claim made by a consumer has been settled in some fashion, and therefore no robust legal precedent has been formulated.

These serious voices – The Competition Commission and Office of Fair Trading – have been seized upon by journalists and consumer protection lobby groups and widely publicised, usually with the theme that consumers are being "ripped off" by the retail banks. This attitude conveniently ignores the fact that the vast majority of British banking profits (which have reached record levels) come from capital markets activities, as well as deftly setting aside the universal access to free banking in this country which is not the case in many other European countries. Nevertheless, UK retail banks are sufficiently keen not to add to the current consumer reaction and have generally refunded some or all of each bank charge reclaim that they have received.

## The publicity and the rise in reclaims

In late 2006, The Independent newspaper launched a campaign to publicise the availability of ready-made claim forms that consumers could download from a number of consumer financial websites, in order to make their claim more easily. The campaign took off meteorically, with downloads of these forms claimed to have reached 1.3 million to date on one website alone<sup>4</sup>, and to be running at a rate of 7,000 per hour. The overall number of people believed to be in the process of making a claim is thought to be around 1.9 million<sup>5</sup>.

This level of consumer activity has been corroborated by other sources. It was reported earlier this year<sup>6</sup> that consumers looking for advice on how to reclaim unfair bank charges have swamped the Financial Ombudsman Service. The independent public body said it is receiving up to 3,000 calls a day from bank customers – thirty times the amount of last year and ten times more than for any other issue.

With other recent estimates suggesting that more than a million customers are now attempting to reclaim fees, commentators such as Defaqto, the financial research firm, have said free banking is likely to end within two years as the banks react to the mounting consumer and regulatory pressure. Although none of the major high street banks have yet to start charging on current accounts, two 'branchless' banks have already announced plans to introduce charges on some accounts. And the incoming chief executive of Britain's biggest building society, said that he thought charges for running accounts was "fairer" than the current system. A secondary situation is also arising where banks have reacted to the customer reclaims by closing that person's account. Here it appears that some precedent (although not a legal one) is being set with, for instance, the Financial Ombudsman Service (FOS) in February mandating that one bank pay £125 to a former current account holder who had made a bank charges reclaim and then found their account closed<sup>7</sup>.

Whatever the legal and regulatory outcome of this situation – and it should be noted that many banks are now waiving charges in some instances – the clear and present need to administer this tidal wave remains with the UK banking system. Here again, we encounter a regulatory obligation on Britain's banks – namely, that any request for copy statements as part of a claim must be answered within forty days. Such a timeline does not seem too onerous, until one thinks of the

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<sup>4</sup> <http://www.moneysavingexpert.com>

<sup>5</sup> Telegraph, *Two million join bank charges fightback*, 2 March 2007

<sup>6</sup> The Times, 22 Feb 2007

<sup>7</sup> Daily Mail, *Ombudsman acts on bank fees*, 9 February 2007

sheer volume of claims, and the lack of readiness of document and information systems at some banks to cope with that volume of claims.

### **The research – methodology and results**

The fieldwork for this report examined the state of document management systems at over 30 of the country's institutions that offer current account facilities. The research was conducted through telephone interviews and took place during February and March 2007. The conclusions of the research were that one in every fourteen requests for copy statements as part of a reclaim could not be met within the regulatory 40 day period. This equates to 7% of bank charge reclaim statement requests that are not being dealt with within the regulatory time period, and back up anecdotal claims in the press that, "On many occasions, [banks] have also failed to provide information within the 40 days set by the legislation<sup>8</sup>."

Under UK and Scottish law, claims may be made going back six years. All UK banks have archived records going back this far – in fact they have to keep records over a much longer period. However, having not expected that this situation would arise, the document management systems at some institutions are now thought to be unable to cope with this sudden volume of claims within the regulatory period.

Most banks use a combination of digital records and microfilm to store their customer records. Recent records are kept immediately available on the bank's computer system to answer queries about recent statements. After a period, however, decided by each individual bank, those records will be transferred to microfilm for long-term storage. Microfilm is the chosen medium for a number of reasons. It is simply a miniaturised image, so however computer formats may change; it will always be readable, avoiding inevitable future systems obsolescence. It costs far less over time than digital storage. Microfilm has been proven to be very stable as a long-term storage medium, not deteriorating across many decades. This is important, as many questions have been raised over the longevity of digital storage media such as CDs. Microfilm can be copied and physically removed to secure locations for disaster recovery insurance. Modern hybrid systems can now rapidly transfer the microfilm image back into a digital network for retrieval and reprinting, so that copy statements can be provided to the bank charge claimant.

Although these systems are available, either on a purchased or an outsourced basis, not all institutions have them in place. Nevertheless, in the short-term, some banks have managed to comply with the current volume of statement requests by duplicating their microfilm archive and

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<sup>8</sup> The Independent, *Now banks are over-charging customers for information about their over-charging*, 3 March 2007

then employing temporary staff to manually answer incoming queries. This has proved effective in the short-term, but will prove inadequate if volumes rise.

### **Rising claims volumes and their impact**

It would appear that volumes of reclaims will rise dramatically from this point onwards. A survey for Which? has revealed that two thirds of people charged excessive penalty fees by banks have yet to lodge a claim for a refund<sup>9</sup>. One in five (21%) of those said they had not asked for their money because they were worried how the bank would react. 22% felt the process would be too complicated, and a third said they did not know how to complain.

Therefore, if we accept that there are around 1.9 million reclaims currently being processed by consumers, the projected additional volume of reclaims would swamp any measures the banks have currently taken. If the current publicity from the media, lobby groups and official regulators encourages the larger part of currently reluctant claimants to overcome their reluctance and go ahead with a reclaim, then there could be another 3.8 million reclaims for the banks to process.

If this growth in reclaims occurs, which seems more likely than not, then banks whose systems can currently cope with reclaim statement requests within the regulatory 40 day period will start to transgress the deadline. The proprietary model constructed by this research project estimates that if just half of potential reclaimants overcome their reluctance and do process a claim, then by the end of this year, one in every eight claim requests will not be processed in the regulatory period, assuming that the banks make no further systems investment.

UK retail banks are, however, taking the situation seriously, and contemplate one of two areas of investment to cope with growing reclaim volumes. Some will invest in additional microfilm copies of archived records so that more people can be devoted to the task of manually answering reclaims within the regulatory period. Others will pay to digitise the last six years' records to speed up document retrieval rates. However, the more strategically-minded institutions are already regarding the bank charge reclaim phenomenon as just one manifestation of an as yet unforeseen series of banking reform situations, and are therefore investing in dual media document solutions. These allow free flow between short-term digital storage and long-term microfilm archiving, thereby avoiding being caught out by sudden peaks in enquiry volumes, but also taking advantage of the economies and proven longevity of microfilm storage.

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<sup>9</sup> Independent, *Fears of 'reprisals' stop bank customers reclaiming charges*,  
23 March 2007