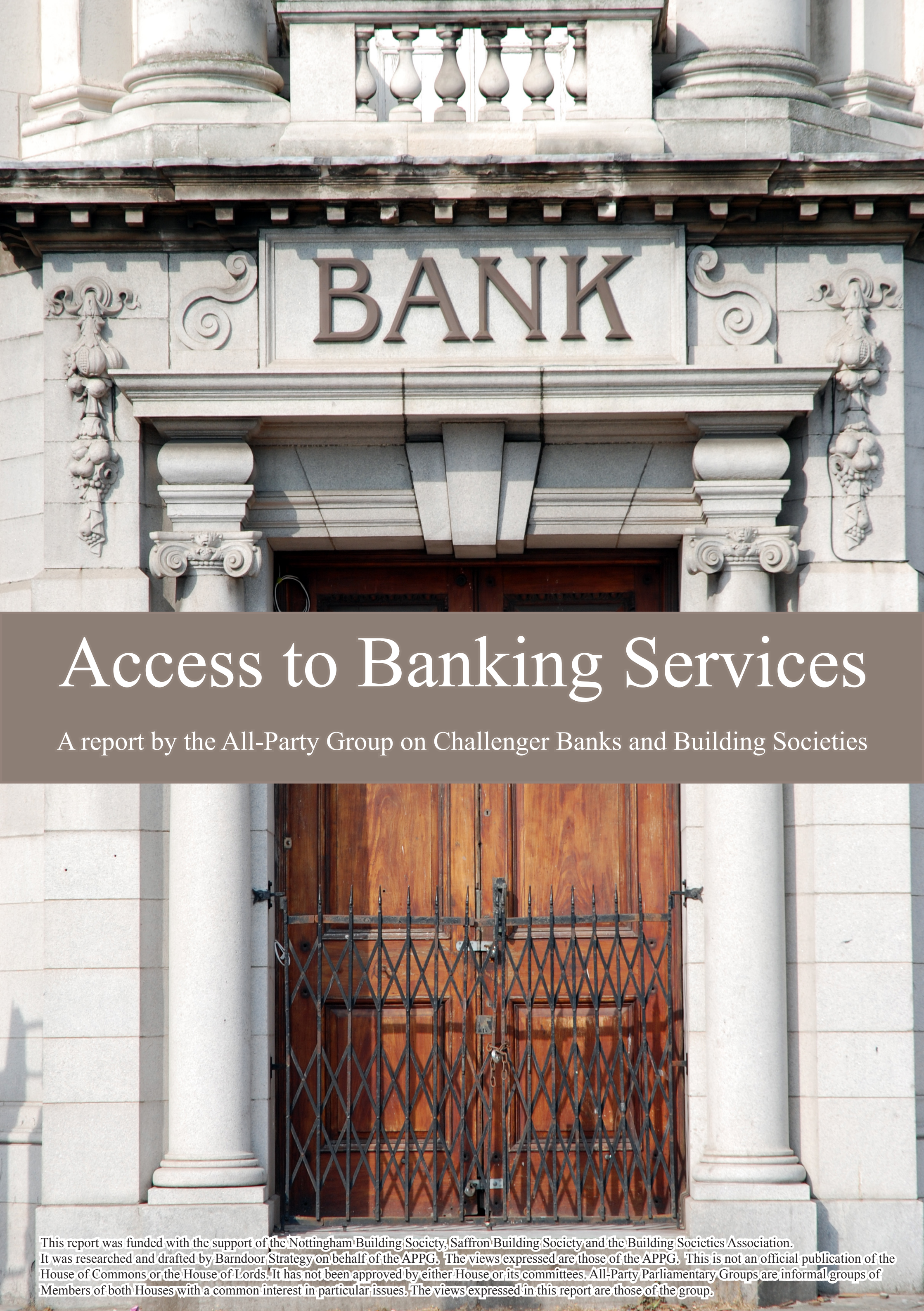



# Access to Banking Services

A report by the All-Party Group on Challenger Banks and Building Societies

This report was funded with the support of the Nottingham Building Society, Saffron Building Society and the Building Societies Association.
It was researched and drafted by Barndoor Strategy on behalf of the APPG. The views expressed are those of the APPG. This is not an official publication of the House of Commons or the House of Lords. It has not been approved by either House or its committees. All-Party Parliamentary Groups are informal groups of Members of both Houses with a common interest in particular issues. The views expressed in this report are those of the group.

**Foreword**

When we held our inaugural meeting, bank branch closures and the issue of access to financial services were hot topics for many of our APPG members across both Houses of Parliament. It should come as no surprise therefore that these issues feature in the first of our reports.

Many MPs have seen banks shut up shop in their constituencies. Therefore access to financial services is becoming a major issue for politicians of all parties, wherever they are based in the country. There are some simple and some more complicated reasons for this change. There are geographical variations and we also learned that it is not a one-way street.

We took evidence from a range of institutions into the issues around branch closures and access to financial services.

Underlying this all is a major revolution that is taking place in the UK in the way that people access retail financial services. Not only is the day of Mr Mainwaring gone, the very building in which the Mr Mainwarings of this world once worked are being erased from our high streets.

It is clear that whilst this change can bring many benefits, it can also throw up many issues for people and local communities. What is also clear is that we are not necessarily at the end of this process. The rationalisation of branch networks is continuing apace and many towns now lack a bank. If closures continue at the same pace, or accelerate, many more communities will be left without a financial hub.

This will clearly have implications not just for consumers, but other businesses. Worryingly, we received evidence of the detrimental effect this can have on the remaining business in the high street with figures suggesting a 20% drop in footfall. Clearly this could have a profound effect on many communities.

Therefore, we have proposed some suggestions as to what government and regulators could do to anticipate the challenges ahead and to empower challenger banks, communities and local politicians to step in.

**Lee Rowley MP**
**July 2019**

# Contents

# 1 Executive Summary

When the APPG met in July 2018 it agreed to look at four main areas. The first of these was access to financial services, with several members of the APPG expressing concern over branch closures.

The APPG held an oral evidence session on the 15th November 2018. The following report is based on the submissions of witnesses at that session, on responses to our call to evidence and on information published by the House of Commons Library and the Financial Conduct Authority.

From our oral evidence sessions and the submissions we have received on access, it is clear that there are two severable but interrelated threads to the access debate.

There is the issue of access to financial services at branches, when many branches are being closed. There is also the issue of access to the underlying financial services products which consumers hitherto have accessed through branches, but which can now be made available by the use of the internet and apps.

Many consumers who formerly accessed their finances through branches are now doing the same thing using their mobile phone. However, real issues surround both those who are left behind by the changes and need to continue to access services in branch for a variety of reasons. When making major financial decisions there is clear evidence that consumers prefer to do this in person.

Moreover, the reasons behind branch closures are complex, opaque and have a relationship to the anti-competitive nature of the UK's banking system, which is heavily dominated by a small number of large established players. The presence of structures such as the free-if-in-credit bank account – once a game changing innovation, when pioneered by the Midland Bank – have ossified the market and act as a barrier to price transparency and competition.

The low propensity of consumers to switch banks means that the major players have a docile customer base prone to inertia. Many of these institutions have found that they can do almost anything they want to branches, safe in the knowledge that customers will not defect to competitors.

The present issues around access to finance may for many consumers be temporary, as FinTech innovations drive new routes to access services once found in a branch. Moreover, some firms, such as the Nottingham Building Society, are actively opening new branches as they are able to use them to deliver products their customers prefer to access in person.

However, given the way that the UK retail banking market has evolved in the past and the barriers to innovation that persist, it is unclear whether access to financial services will improve in the short term. The technological revolution that is gripping both the banking system, the payments system and the wider high street both have a long way to go before the final outcome becomes apparent.

At the end of this paper we make a series of recommendations about how government and regulators could tackle these issues including:

- legislation to allow challenger institutions to take over closing branches;
- a community scheme to allow towns and villages without a bank to tender for challengers to relocate there;
- a partnership scheme for challenger banks and building societies to open shared banking space in town centre locations;
- Clarification from the Government about the anticipated future role of the Post Office if it becomes the bank of last resort in towns and cities across the country.

We hope that these will provide stimulus for future action.

**APPG Challenger Banks and Building Societies**

**July 2019**

## 2 What are the issues around access to financial services?

*In our research we've tried to quantify whether perceptions about branch loss and reduced access to financial services represent the reality. Moreover, we've looked at whether there is an actual knock on effect for other services on the high street.*

Parliamentarians inevitably view the issues around access to financial services through the lens of their mailbox. Regular communication by members of the public on issues of reduced services has led to the perception of many MPs and Peers that the public are facing issues with branch closures and access to services.

Bank branch closures have become a commonplace occurrence across the country. With branches closing at unprecedented rates it isn't surprising that many customers are expressing exasperation at the loss of what they regard as vital community facilities.

The realities of bank branch closures and the effect this is having on access to financial services and cash needs to be kept under close scrutiny. What are the current state of bank closures? How does this actually effect consumers, vulnerable customers and communities? What is the at the root cause of the changes? How can problems arising be resolved?

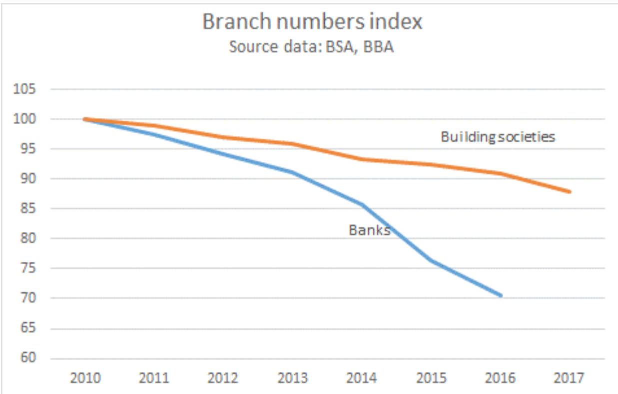
# 3 The current state of branch closures

In terms of the reality of closures, the House of Commons Library has figures suggesting 4,000 bank branches had closed over the last decade, with a continuing closure trend as the major banks rationalise their networks.

In terms of the rate of closures Reuters published an article on 23rd August 2017, which quoted 300 closures a year since 1989, with branches over that period going from 17,831 to fewer than 8,000.

their members and therefore could make different choices from firms that instead were required to prioritise the interests of their shareholders.

For instance, in recent years this had led to building societies reducing branch hours rather than closing branches. It has also led building societies such as the Nationwide to open in areas without a branch such as Glastonbury.




The Building Societies Association (BSA) was able to provide some detailed information on branch closures, including the above graphic, illustrating the decline in branches and how both the quantity and rate of change has been more pronounced in the banking sector than in the building society sector.

In explaining the difference, the BSA referred to its *Engaging Conversations* report, which explored the benefits of mutuality. All of these benefits were derived from the fact that building societies were owned by

The BSA was also able to point to other examples of branches being opened in the building society sector such as the Swansea Building Society's new branch in Cowbridge and the Nottingham Building Society's increased branch network which grew from 32 in 2013 to 67 in 2018.

Other developments included co-location of branches. The Newcastle Building Society's branch in Yarm was co-located with the local library. The co-location meant that the library was able to stay open.

# 4 The effect on consumers

Consumers have certainly been very vocal about the loss of branches. The corollary to this is the question as to whether consumers still need branches. There was a consensus amongst witnesses that this was very much the case for particular types of services.

In giving oral evidence, Joseph Lane of the Citizens Advice Bureau (CAB) referenced the FCA's Financial Life survey as a good source of information, as when run in 2017, it had surveyed 50,000 people. Of those surveyed, 40% used a branch regularly and of the remaining 60% who did not, 30% of those had used one until their branch had closed in the last twelve months. Together with other figures, it was clear that people were changing their habits due to closures.

The CAB's view that it was necessary to take the perspective of consumers on what services were needed. A particularly problematic issue with bank accounts was that it was difficult to get to the bottom of the economics of what customers were paying for, given the way that banking services were cross-subsidised.

Additionally, the CAB had been involved in a large programme of work during the Post Offices' transformation as the Government had decided that the Post Office was one way of providing services where there was no bank. The problem here was that the Post Office was currently not set up for this and needed to build capacity. Only 2 in 5 people were aware that the Post Office provided access to banking services. Moreover 5% of customers who were using the Post Office in this way encountered problems such as difficulties with international transactions.

> **"Where banks closed, 90% were in poorer areas or where the income was below average. Scotland, Wales and the South-West were hot spots as were the suburbs of London."**
>
> **Joseph Lane, CAB**

The Nottingham Building Society also cited the growing demographic of ageing consumers who would seek to continue to manage their financial services in the way that they had done so traditionally for the next 30 years. However, this was not necessarily the case for younger demographics. Millennials, those born after 1994 and consumers in their early 30s had a very different approach to managing their finances.

The Nottingham had found that there was a difference between types of services that consumers sought to undertake in branch. Unsurprisingly, many of the straightforward simple transactions were going digital. This has meant that the traditional reasons for using branches, such as cashing cheques, have fallen into decline. Therefore, the way people were using branches was changing. Customers were using branches to discuss complex products or major financial decisions as many consumers prefer to make major decisions like this face-to-face as opposed to online or over the telephone.

Given the trend of moving responsibility for consumers' financial well-being from Government provided pension schemes, to self-sufficiency, through private provision, it was likely that more and more consumers would need advice on complex financial products. The Nottingham therefore believed that there was a growing market for institutions that could offer these services in branch.

**"The final branch closing resulted in a 20% fall in revenue"**

**Nottingham Building Society Research**

# 5 Vulnerable consumers

We found that there are still considerable issues of concern with regards to vulnerable customers. All our witnesses were able to point to the ability of face-to-face providers to assess the potential vulnerability of a consumer more accurately than, for example, an online provider. However, it is worth noting that technological solutions to some forms of vulnerability such as gambling do already exist for example, account features allowing gambling payments to be blocked.

The CAB in particular was concerned that there was a big risk of financial exclusion. The BSA provided further written evidence on vulnerability working from the FCA's definitions of "vulnerable customers" which include:

- people with physical or mental health problems
- Low financial resilience
- Low financial capability
- Impact of life events

The BSA evidence that withdrawal of branch services left all of these groups exposed was compelling. This was particularly so given the importance of face-to-face interaction for identifying vulnerability and providing support.

The BSA provided a number of examples:

- Customers who use the branch because they get help from branch staff to run their account e.g. customers under a Power of Attorney type arrangement has been made to give them limited access to cash.
- Customers who are unable or unwilling to use the alternate transaction options available, such as online transactions e.g. customers who cannot physically use a keyboard or smartphone; customers who do not have an internet connection; and customers who do not trust online banking.
- Customers pushed into using online services may become dependent on a third party to make the transactions for them and so are vulnerable to financial abuse.

However, the BSA did emphasise that not all vulnerable customers chose to use their local branch and that some managed their finances in different ways.

One further issue that the BSA also flagged was that although consumers were increasingly turning to post offices to access services once found in a branch the customer experience was not the same.

Witnesses made the point that in their view Post Offices frequently lacked the facilities or the training to offer customers the same sort of pastoral care that would be available, for example, in a building society branch.

According to the CAB's evidence, 90% of branch closures were in poorer areas or in those where the income was below average. This meant that Scotland, Wales and the South-West were hot spots, as were some London suburbs. This was due to the fact that areas with high rates of social exclusion were the least profitable parts of the market for banks, who predominately made their money from balances and savings accounts.

Additionally, the Nottingham had found that when the final branch closed other retailers reported a 20% fall in revenue. Survey work had revealed that 29% or respondents said that they would visit a town or village less if there were no financial services providers. Even with traditional branch based services, decline was not a universal trend.

> **"29% of people said that they would visit a town or village less when a branch closed."**
>
> **Nottingham Building Society**

# 7 Is a decline in access a universal trend?

The Nottingham Building Society is an interesting case study.

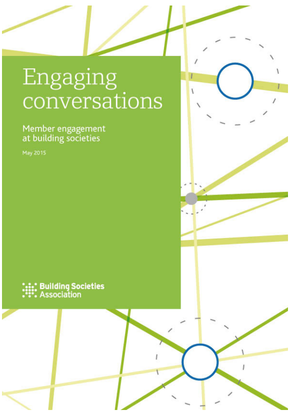
With a hybrid of digital and face-to-face advice, the Nottingham was opening branches where some of its rivals were closing theirs. The reason for this was that the Nottingham's proposition was different from many of its competitors. It offered whole-of-market financial planning, as well as the more traditional savings and mortgage products. While it might be prohibitive to offer advisers on different products in all its branches, the use of digital technology and video conferencing in branch meant that consumers could access the advice they needed from any branch.

Moreover, customers visiting a branch for a mortgage at the Nottingham Building Society had a 98% chance of walking out with a mortgage from a different provider. The Nottingham was not just about selling its products but ensuring that its customers secured the best financial product for them.

This has meant that the Nottingham had expanded from 32 branches in 2013 to 67 in 2018, extending its reach from four to eleven counties. The Nottingham had also been taking advantage of the departures of some of the other financial institutions, for example, Yorkshire Building Society's retirement of its Norwich & Peterborough brand in Norfolk. The opening of the Nottingham provided continuity for residents with seven new locations all opening in a month. Branches had been opened in towns such as Ashbourne, Uttoxeter, Buxton, Fakenham, Dereham and Stamford which were all traditional agricultural based market towns with a thriving mix of retail business and independent traders.

Taking over a branch revolutionised the economics. Whereas starting from scratch would entail a six to seven year lead time to break even. Working with an existing branch reduced this to two to three years.

Beyond bricks and mortar, the growing FinTech arena has seen the development of new and exciting ways for consumers




**Ipswich Building Society:**

' By helping members understand their status as owners of the business we can increase their engagement in the Society, bringing direct benefits to them and continual improvement to us.'

As quoted in the BSA's Engaging Conversations report p15

to both access financial services and to engage in new ways with financial providers.

Fintech has also created new services that were previously not on offer to many ordinary branch customers. Providers such as the Nottingham were part of this movement as they were not simply offering traditional transaction based services. Additionally, the Nottingham's Newark branch was offering community meeting facilities with iPads for community groups. The Nottingham was also only the second institution to offer Lifetime cash ISAs.

Technology also had a part in making financial services more useful to people. Professor Llewellyn of Loughborough University submitted substantial evidence, which will be dealt with in more detail in the APPG's forthcoming diversity report. Llewellyn set out how FinTech is eroding some of the traditional advantages of banks including financial intermediation, business and payments. Open banking and the second Payments Services Directive (PSD2) had lowered search and switching costs for consumers making it easier for new market entrants. However, much FinTech activity had so far concentrated on relatively narrow parts of the value chain in terms of the provision of financial products and services. The root causes of branch closure are in some aspects simply economic factors and in other ways complex results of wider societal changes and the growth of the internet.

# 8 What are the root causes of branch closures?

One aspect of banking that was repeatedly flagged by witnesses was the free-if-in credit banking model. While "free" current accounts might appear to be just that , the true cost of providing the complex set of transactional services was hidden through charges on customers who were not in credit. Some of these groups of customers with payed more than others. Moreover, it was suggested to the APPG by the CAB that the retail financial and misselling scandals over the last 20 years could all be traced back to banks seeking to make profits elsewhere as they offered current accounts for free.

Lack of competition with both banking customers highly unlikely to change bank and the market saturated by dominant players, meant that larger institutions could close branches with the knowledge that it would have little effect on their business, save for reducing their operating costs.
Added to this was the rapid move by high street banks to cut costs – partly brought about by the need to return to profitability post the 2008 crash. This was undoubtedly playing a part in accelerating branch closures.

In their oral evidence, the CAB cited the lack of transparency of pricing on the services that people needed as being problematic. The CAB assumed that transactional services and accessing cash were loss making for banks. However, debit card and overdraft usage were presumably profit making and used to cross-subsidise other services. The CAB's view was that the current account market was so uncompetitive at present there was no compulsion for firms to open marginal branches to acquire customers. This lead directly to a disincentive for alternative firms to enter the market, as the costs of opening branches were so high.

# 9 How can access to banking services be addressed?

## 9.1 Competition

At our oral evidence session the CAB's view was that banks were merely acting as rational players in a free market. Voluntarily banks would not choose to operate less profitably. It was their duty to make the best use of their capital.

Only regulation could mandate banks to perform a social function. This has been seen elsewhere, for example in the United States, as a key driver behind the US Community Reinvestment Act.

In his evidence Professor Llewellyn did provide cogent examples about how the reformed regulatory regime and Open Banking could also lead to greater competition. This is detailed more fully below.

What was clear from the evidence submitted, was that unless there was regulatory intervention, the current market arrangements acted as a major disincentive not so much to new market entrants, but to those who wished to expand in terms of the provision of traditional bricks and mortar banking services.

**"87% of banks funding for lending was sourced from domestic deposits."**

## 9.2 Regulation

During oral evidence the question was raised as to whether regulators were doing enough to respond to the challenges of branch closures. The CAB's view was that there were wider questions as to what the universal service obligation should be and at what geographical distance to consumers.

As a corollary to this, one aspect to regulation touched upon by several witnesses, was the need for greater transparency over costs. There was a need for regulators to delve deeper into the true costs of branch networks. Although we recognise the challenge of doing this.

A second related issue was the distorting effect of retail deposits. 87% of banks funding for lending was sourced from domestic deposits. These were known as NIBLES (non-interest bearing liabilities). They gave the larger banks a significant competitive advantage over their rivals.

Whether the financial or competition regulators needed to take a closer look at this situation is beyond the scope of this paper, but the APPG hopes to return to it later in our work.

There was a suggestion from several witnesses that better regulation was needed for the whole of the market. The regulator was too focused on the bigger players and needed a greater risk appetite for different types of institution and to allow for the possibility of failure.

The CAB was of the view that the reason banks could continue to operate with big margins was that the barriers to entry for competitors were too high. The CAB was of the view that one of these barriers was clearly the free-if-in-credit current account. However, a greater issue seems to be the scalability of institutions.

## 9.3 Technological change

Technology, while cited as one of the root causes of branch closures, was one of the solutions to the access conundrum.

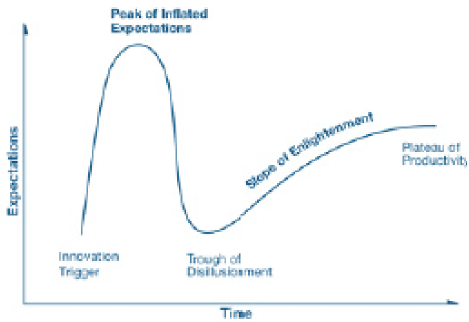
In their oral evidence, the CAB outlined how they themselves had traditionally been a face-to-face provider. However, now the CAB was itself growing its online proposition using digital chat and other tools. It had been able to expand the number of people it helped to some 8 million online compared to 400,000 face-to-face.

They were also confident that the free market would drive solutions for the majority of customers.

The CAB set out how they were developing a digital "sandbox" to allow providers to test their digital services with 500 vulnerable consumers. This would, the CAB hoped, help providers develop solutions for these groups.

Professor Llewellyn of Loughborough University also submitted evidence regarding the prospects for Open Banking and FinTech to revolutionise the provision of financial services. He also cautioned over the effects of the Gartner hype cycle which had been seen in tech before, notably in the 2000s dot com bubble.

Past innovations in financial services, such as MiData, have proved disappointing and consumers are reluctant to take the risk of new technology and approaches when they have seen problems emerge.




*Gartner hype cycle, Llewellyn, Loughborough University*

## 10. Likely future developments

Future developments are something the APPG will turn to more broadly in its forthcoming paper on diversity of providers. However, for the purpose of this paper, it does seem likely that if present trends are continued there will be a substantial reduction in the high street presence of the Big Six.

The Nottingham Building Society was able to provide some evidence on the knock-on effect on high streets from branch departure of up to a 20% fall in footfall.

The evidence supplied by Professor Llewellyn emphasised the scale of the transition banking services are going through currently. With the introduction of FinTech, sometimes new technological approaches to traditional demands, sometimes in the form of price comparison and supermarket tools, entirely new products are entering the market.

Professor Llewellyn also set out some potential consumer benefits and also potential risks from these changes which include enhanced competition and lower prices, easier access to services, more switching, enhanced information, lower entry barriers and increased access to products due to lower costs.

On the risks front there are issues around data and cyber security, new scams such as authorised push payment fraud, making use of automated systems, and civil liberties issues arising from the amount of granular data that organisations hold on individuals and their spending habits.

However, according to estimates cited by Llewellyn, the peak value customer in banking is 58 years of age compared to say 29 in the telecoms sector. It is against this rather inconvenient backdrop that many firms in the banking sector looking to move to a lean online based business model. It does therefore appear that there is a potential gap in the market opening for challenger institutions who are targeting these profitable customers who have a preference for a physical branch.

# 11 Conclusion

There can be no doubt that at present a channel to access to financial services for UK consumers is declining.

As to whether this is a temporary blip as new technologies and players enter the retail banking space it is too early to tell.

Government and regulators will need to keep the retail banking market under close scrutiny as the industry is not so much going through a change, but a fundamental revolution in the way that banking services are being delivered. This technological and payments revolution has barely begun and there will be further profound changes before it reaches its conclusion.

The access report is the first in a series where we will look at the issues developing in the high street banking arena. It is difficult to separate it from the other related issues, such as the relative lack of diversity of players in the UK retail banking space compared to other jurisdictions.

Moreover, underlying the economics of the whole sector is the regulatory backdrop, which influences, not only the economics of the whole sector, but also governs the barriers to entry for potential new competitors. Both these issues will be matters that the APPG seeks to return to at a later date.

# 12 Recommendations

Having considered the evidence and the issues, we would like to make the following recommendations.

## Recommendation 1

We would like to consider legislation to give challenger banks and building societies the right to take over Big Six branches that have been earmarked for closure.

Banks and financial institutions are not being very transparent about the criteria for branch closures or indeed the their "end-game". This leaves challengers and communities in the dark. Legislation allowing new entrants or other institutions first refusal would mean that there is an opportunity to save a banking presence and ensure that there isn't institutional group think leading to every branch in a town closing before other organisations, local authorities or communities are consulted.

## Recommendation 2

We would like to see regulators challenge the major banks over closures with a view to giving competitors a faster route to building competing branch networks. We would like to see a scheme set up, funded by the major banks, to enable towns and villages without a bank to tender challengers for the opportunity to open a branch there. We would like to see HM Treasury make provision for this through tax relief on the taxes paid by the major banks in an effort to support communities and councils to undertake this work.

## Recommendation 3

We would like HM Treasury to investigate a scheme to partner challenger banks with existing retailers to open a desk within existing retail outlets and other public buildings in town centre locations such as council offices, libraries and leisure centres etc.).

## Recommendation 4

We believe that Government should outline with more clarity how much support it is willing to give the Post Office if it should become the bank of last resort in towns and cities across the country, assuming that many "high-street" banks continue to run down their networks to zero. This has widespread implications for access to financial services and access to cash in particular.

## Appendix 1 - Minutes of Oral Evidence Session on Access to Services

15th November 2018

David Marlow, Chief Executive of the Nottingham Building Society
David Marlow thanked those in attendance and outlined the importance and role of face to face and branch networks, now and in the future.

He set out how the Nottingham had approached changing times, the themes and the drivers of change. There were two sides to this demographic split.

The first of these was demographic change in the country. There was a great deal of discussion of the ageing population with the number those over 60 increasing all the time. There was a group, therefore, that needed help managing their financial affairs based on how they had experienced financial services historically. This would remain an important demographic for financial services for the next 30 years. Their financial background was set in a different context to the younger generation. There was an older generation, who had benefited from a golden era of strong pensions support from government, employers and advice specialists. The portion of national income that pensions covered today was much larger than it would be in 10 – 15 years.

There was also an emerging demographic that would need to be served in a different way Generation K and Z, teenagers and those in their early 30s would have to take a very different approach to how they managed their financial affairs in years ahead. They would not benefit from the same level of employer and government support that their parents and grandparents had enjoyed.

This was coming at a time when the rise of digital was making the straightforward simple transactions of financial services simpler and quicker. Traditional reasons for visiting a branch were in decline and being confined to history. The way that people used their branches was changing with fewer people visiting their branch to pay in a cheque, for example. Therefore, the reasons people are visiting branches are radically different as the profile of transactions is reduced.

These demographic and digital elements needed to be considered accordingly.
There were new requirements and solutions that financial services organisations would be required to provide. There would be a requirement for the change in nature of services provided that would not be transaction based, but it would be advice based. The requirement for advice and support would increase quite dramatically and the Nottingham were looking at how they used their physical presence to combine digital accessibility with advice and support. In the next 20 to 30 years people would need to take greater responsibility for self-sufficiency in terms of how they arranged their financial services. The role of the Nottingham was therefore changing to reflect this and this had been the strategy over the last three to four years.

The Nottingham's proposition as a building society was quite different from others which consisted mostly of passbook savings and mortgages. The social purpose of the sector as established 170 years ago, was predominately around improving the quality of housing and putting a roof over members' heads. While this was still a very important role, today the Nottingham was extending its role to help people to organise and protect their future and their family's future.

The Nottingham offered whole of market advice for mortgages so that consumers coming to the Nottingham had a 98% chance of walking out with a mortgage from a different provider. It was not just about selling a Nottingham Mortgage, rather the best product for them.

The Nottingham also offered whole of market financial planning. Advice was available for pensions and long-term saving. The Nottingham also offered financial advice services and estate planning services from the provision of wills to estate planning advice as well as the setting up of trusts for future generations. The Nottingham was putting effort into its proposition in non-traditional areas for building societies. But there was a tightening focus on providing services that the older and younger demographics valued in terms of advice.

There was still a very strong demand from consumers to receive this more complex advice on a face to face basis rather than over the phone or through an app. The Nottingham had been taking advantage of the departures of other providers over the last three to four years from certain locations. Careful selection of locations had led to opening new branches from 32 in 2013 to 67 in 2018. The Nottingham had extended its footprint from 4 counties to 11 counties. If you looked at the savings balances and new membership serviced by this network the new branches open by The Nottingham in the past four years would be a top 20 building society.

There was strong evidence for an advice and service based proposition amongst the British public. Nottingham were not offering branches in a traditional way as a transaction hub. They were establishing branches as an advice and service centres. You could buy a home through an estate agency, get whole of market mortgage advice and financial planning advice to protect your family's future.

The stance had been to step back and not look simply at physical access on the high street but also to look at the pressures that different demographics had, and to design a proposition that met those needs. The future was about combining face to face advice and digital. Around 10% of the Society's capital was being invested in a digital transformation programme at the moment.

A hybrid of this digital and face-to-face for advice and services to customers was the future. For example, video terminals had been installed in all 67 branches so that face to face mortgage advice could be given and customers could be interviewed to give appropriate whole of market mortgage advice. It would be prohibitive to have 67 advisers sat in 67 branches. This had proved very popular and had demonstrated that this form of digital technology was the future. The setup allowed the customer to see the adviser as if they were in the room. Irrespective of where the adviser was sat in the Nottingham network they could press a button and print out documents where the customers was seated.

Over time the plan was to offer these services to people in their homes and over computer tablets. The Nottingham was not a Luddite organisation which was wedded to a physical presence. However, it believed that an appropriate number of branches and access points was necessary to provide services and grow the membership.

1. How has the Nottingham bucked the trend in terms of branches?

Nottingham's proposition was different and relevant. This gave the confidence that customers would be interested in the Society's products. Using sophisticated data modelling the Nottingham had identified the best areas for people who were open to the proposition and where that customer profile over-indexed in the population of that town. The Nottingham waited for one of the large incumbents to leave and then would move in. For example, the Yorkshire Building Society decided to retire the Norwich & Peterborough Brand and close branches in Norfolk. The Nottingham had been looking at some locations in Norfolk for quite some time and entered swift discussions with colleagues at the Yorkshire. The opening of the Nottingham provided continuity of service in 7 new locations all of which were opened within one month.

2. What have been the driving factors behind your moves to open branches?

If a branch was set up from scratch without any other supporting factors a bank could look at a period of 6 – 7 years to break even. However, taking over a branch meant that the economics were revolutionised with a break-even at 2 – 3 years which was much more acceptable. Nottingham would not have been able to open 30 odd branches with a break-even of 6 – 7 years.

3. How does your business model compare to others on the high street?

We don't view ourselves as a transaction based organisation. People save with us and we see saving as the fundamental underlying platform for future protection. The Nottingham sees itself as an advice and service proposition. There were other means for self-service and this represented only 20% of the UK population.

As our purpose we are focused around how to help our members to help protect themselves for the future. We have an advice proposition that is as relevant to one of our 60 + customers as well as our younger members. For example The Nottingham was the second institution to offer LISAs which is a fundamental product to allow younger people to save for a home.

4. What do you think is the likely future of the branch?

There is a strong future for the Nottingham in the way it offered branches. There is a strong future depending on the way that people were drawn to the branch. The Nottingham was just about to launch its new concept branch in Newark in December which for the first time would have a community area. This will offer meeting type facilities for local groups with digital tools such as iPads available. We will be encouraging local groups to use the branch on the high street if they want to gather for community purposes. The Nottingham sees its role in making the branch as relevant to the community in which it operates as possible, coupled with our advice proposition. Transaction based branches were in a dwindling market.

5. Is technology a solution? Are there alternative providers or ways of providing services once catered for in branches?

Yes, undoubtedly. Technology was part of the solution and there are lots of ways we can use technology to provide advice effectively. We see this as important part of how we develop our offering.

The way we save in the UK has not changed in 100 years. You save in a savings account or in an ISA. We see technology giving us the opportunity to change the way in which we save. It can be delivered in branch on tablet too. We need to create more objective based saving plans for members which identify the right goals and ways of saving for these. It allows people to start their own dashboard. This was a very different way of going about saving. This was enabled by technology. A number of us went to a global technology conference in San Francisco last year and saw technologies that enabled an objective based savings approach. This could be enabled with the support of an adviser in branch or at home. Technology will absolutely play a part in making financial services more useful for people. Expert advice can be made available and accessible through technology.

6. What does the Nottingham do for vulnerable consumers?

We look after them. Vulnerability can exist in so many different guises. Face to face service gives you a much greater ability to assess vulnerability. Most of the best examples from a vulnerability perspective are where our staff in branch know a customer really well see a change in behaviour. They have an ability recognise and understand this. They also have the strength of ability to handle this to take the customer into an office and offer them a cup of coffee and ask them questions about unusually large sums of money they may be trying to withdraw for example. Vulnerability was an emerging theme across financial services and there are things you could do as a building society to address this. The complexity of vulnerability in an individual can ebb and flow. When you are a member based organisation it is a lot easier to ensure people are helped to project themselves.

7. How do consumers view banking services in the experience of the Nottingham?

As we don’t offer a current account we don’t see ourselves as offering a banking service. However, being blunt the nature of the UK current account market is broken and has been for some time. All of us would recognise that current accounts are not free. The complexity and digital accessibly that people expect is impossible to be free. It is delivered in a way that makes it free at the point of use and this creates enormous barriers to entry. The amount of investment being put into deliver a competitive current account offering when the income side of this is nothing would be huge. Hence the market being broken. Technology wise, with the advent of open banking the Nottingham will be able to serve members equally well whether they are banking with us or not as well will be able to see where members are spending money and help them to spend it more wisely.

8. Are there any unintended consequences of the changes? For example such as:

- issues around disproportionate burdens being placed on alternative providers;
- unintended consequences for consumers and the wider environment;

- changes to travel plans; and,
- increased competition.

When you are undergoing any period of seismic shift, such as the demographic and digital shifts we are seeing there are always a higher risk of unintended consequences. There will be people who are disadvantaged by this shift who just happen to live in the wrong town and the chances of another institution coming in are low to zero. The unintended consequences of free banking are significant. The Nottingham's technology journey is still relatively new. You go through a period of transition where the full technology solutions are not there yet. The technology journey of the Nottingham was still relatively young and there would not be a full services level in terms of technology for four to five years. We are going through a period where there are unintended consequences for a whole range of consumers as the technological solutions are not yet present.

9 Are the regulators and authorities doing enough to respond to the challenges of branch closures?

Not sure what the regulator and authorities can do in a free market. There has to be an economic model that works to deliver. It was for institutions to come up with an economic model that worked for them. It wasn't the role of the regulator to opine on where institutions should or should not offer services. Developing a close dialogue with local authorities when entering towns is important and we have seen this in a number of instances. Locally things could be done to encourage but it wasn't the role of regulators to respond to this. At the heart of this inquiry is how to encourage smaller organisations to move quicker. A different topic but one which was worth of some attention even though this was a difficult balance for regulators to strike.

10 Are there any regional variations in terms of how changes to branch networks are taking place?

Yes, this is interwoven into a number of responses given. With the Nottingham's footprint across 11 counties, its heartland stretched from the Humber to 15 miles west of the M1 to the M25. Within the Nottingham's plan there are 80 locations within these 11 counties where it would be right for the Nottingham to be. The Nottingham was pursuing this plan and therefore not anticipating opening branches in other locations as clearly there were hundreds of towns in this part of the world. There were going to be regional variations and this is reflected as well when you walk up to a high street.

If you look at some of the towns Nottingham has entered over the last few years. They are places like Ashbourne, Uttoxeter, Buxton, Fakenham, Dereham, Stamford. These were strong traditional agricultural based market towns with a thriving mix of retail business and independent traders. The footfall in these towns was therefore very high.

However, there was a range of towns, of a similar size, perhaps more focused on industrial strength in the past where the pattern was different. There are therefore some quite strong demographic variations into how towns were going to evolve over the coming years and not just in a financial services context.

The Chair thanked David Marlow and introduced the next witness.

**Joseph Lane - Senior Policy Researcher at the Citizen Advice Bureau**

CAB was a general advice charity. It helped just under three million people in person and on the phone each year. It worked through 300 independent charities operating from 2500 locations which meant that something like 95% of the population was within three miles of an advice office. It has a large web presence with 20 million visitors a year seeking advice on debt issues, employment and housing. Lane outlines how his role was to examine policy trends in terms of the issues that the CAB was asked to look at.

In terms financial inclusion and banking and access to branches, the CAB was primarily concerned with most of the severe problems in the sector. The CAB fully agreed that the market was best placed to provide the services that people wanted and that this should not be for Government or regulators. However, where the market wasn't providing he services that as a society people should be able to access then there a governmental or regulatory response was needed for this. The problem that the question was addressing was unclear. It was necessary to start from the position of what services people needed.

The way we pay for services such as transactional banking was hidden and this made it difficult. The way that loss making services were paid for was hidden in a fudge. What people needed access to could be divided into three.

This needed to be broken down into transactional accounts, access to a branch and access to cash. All of these could be loss making. In terms of transactions this was dealt with by the basic bank account under the payments account regulations. These were loss making for banks but they have been told to provide them by government. Therefore, they were cross-subsidised by other customers. In terms of access to branches, in areas where branches were loss making they were cross subsidised. The post office was filling the gap allowing customers to access to 95% of banking services through its network. The Link financial inclusion programme ensured access to cash which was funded by a 10p supplement on the interchange fee.

In terms of savings, debit card usage, overdraft usage – these were all areas where banks made money and were used to subsidise other customers. At the moment there was not a good settlement to provide services in most areas.

There were two responses to this: the first was regulatory to compel cross-subsidy through a levy model to provide unviable services; the other was a competition route. Currently the current account market was so uncompetitive the incumbents didn't need to open marginal branches for customer acquisition. There were such high margins in some of the areas of their business which meant that the opportunity cost of opening branches was high. This meant that because of the lack of competition there was no incentive for others to enter the market.

The CAB was also a statutory advocate on post and mail services. The CAB had a large programme of work during the Post Office's transformation. The Government had decided that the Post Office was one way of providing services where there was no bank. The problem was that the Post Office was not currently set up for this and capacity needed to be built. Only 2 in 5 people were aware of this so awareness was low and only half of these would use the Post Office service. The 5% of banking customers who did use the Post Office found difficulty using the service they went in for such as international transfers. This was one way of servicing people's needs but was yet to be properly implemented.

1. Is consumer behaviour altered due to the sparsity of branches and does this influence the way that consumers use financial services?

The FCA's financial life survey was a good source of information. This was run in 2017 and surveyed 50,000 people with some OK questions on branches. The CAB volunteered to do some work for the APPG on this. 40% of people said that they use a bank branch regularly i.e. once a month or more. Of the 60% who did not, 30% used to use one but their bank branch had closed in the last 12 months. This was a clear message that where banks were closing people were not doing something they used to do.

The demographics of this were not as stark as one would imagine. Over 55s it was 17% but for rural areas it was 13% the same as the average and in Scotland 20% of people said they didn't use a branch regularly as a result of closure. The simple answer was that yes people were changing their behaviour.

2. What are the risks to consumers generated by declining networks and to particular groups of consumers including vulnerable ones?

The big risk was financial exclusion. This could be defined within a range of not being able to access a necessary service or need. Or not able to access services through a branch, digitally or on the phone. The CAB had not done an analysis on this area so it was difficult to see who had been most affected.

The CAB believed that people had an equal right to have a bank account and have access to some sort of physical bank infrastructure and also access to cash bar some extreme living choices. If this wasn't available, then this was a failure of the financial services system.

3. How do branch closures relate to access to cash, both as a means of payment and as a reservoir of wealth?

The CAB would be interested to know the direct impact of this. The only analysis the CAB had come across was that in areas where there were no bank branches the investment in borrowing and small businesses relatively to similar postcodes and characteristics fell. The CAB was not particularly bothered about the medium people used to spend money in it was whether they were spending less.

The access to cash questions had an indirect and direct relationships in terms of access to branches. Access to cash had a similar question around financial inclusion. Recent changes in the interchange fee from 30p to 20p was forecast to lead to closures restricting access to cash. There were questions about how much access to cash people deserved and who would pay for it.

4. Do reduced networks have an effect on an institutions' access to capital?

There was third party research on this but not CAB research. There were other ways that businesses could get capital. Lots of small businesses used credit cards and overdrafts as sources of capital instead of loans.

5. What do consumers think about dwindling branch networks?

The CAB did not know as it had not done any direct research amongst its customers. Lots of people still used branches. 40% used branches once a month and two thirds or people had used a branch in the last 12 months, as well as 70% of people who opened a current account, of those depositing cash and cheques 75% did this face to face in a branch. Lots of people were directly affected when a branch closed.

The CAB did not know the underlying economics of branch closures. When banks choose to close branches the presumption was that it was because they were loss making. There was something around the high entry barriers and lack of competition due to capital requirements or other institutions holding customers' cash balances, there was no free market. In an actual free market there would be more openings; however, there was a policy point that Government didn't want to see banks going bust.

6. Do branch closures represent an off-balance sheet transfer of cost?

Yes – there were situations where banks looked at ways to make better use of their capital. This is something that free market organisations would do. Regulation needed to mandate that institutions performed a social function. Voluntarily banks would not choose to operate less profitably.

7. Do you have any intelligence on innovative providers or on how consumers use alternative services?

Not really. It was not the role of the CAB to look at how businesses could be more competitive. Where the CAB would be involved was in issues around policy. It was pretty clear that the current account market was not competitive. The FCA and the CMA were looking at competition in the sector. If there was the view that competition was an issue, there were things that could be done to make the market more competitive.

8. Is technology a solution? Are there alternative providers or ways of providing services once catered for in branches?

Yes, this was happening. Traditionally the CAB was a face-to-face provider. Even the CAB was growing its online proposition. There was direct help available via web chat. The CAB helped a lot more people on digital platforms, 8 million compared to 400,000 face to face. The CAB wanted to play a role in helping people at the margins. The free market would drive solutions for the majority of customers. The CAB was developing a 'sandbox' to allow providers to test their digital services with 500 vulnerable consumers who were at the margins. This would help providers develop solutions for these groups.

9. Are there any unintended

consequences of the changes? For example such as:

- issues around disproportionate burdens being placed on alternative providers;
- unintended consequences for consumers and the wider environment;
- changes to travel plans; and,
- increased competition.

Instinct said that if the last bank closed this would have an effect. This was something that was problematic. If the last bank in town closed then there were impacts. Where banks closed, 90% were in poorer areas or where the income was below average. Scotland, Wales and the South-West were hot spots as were the suburbs of London. Areas where there was social exclusion were the least profitable bits of the market. Banks made profits from balances and savings accounts and people in these areas were not doing these things.

10 Are the regulators and authorities doing enough to respond to the challenges of branch closures?

There were two questions here. What should the universal service obligation be as in other markets. What access should people have to banking services and at what distance. Where this wasn't a normal call for a business who and how should it be paid for. This was currently being done through fudges product by product rather than by looking at the whole cost of banking.

Speakers thanked and formal meeting closed.

As an aside in closing discussion:

Nottingham Building Society research showing that shopkeepers had found a 20% fall in revenue when the final branch closed. 29% of people said that they would visit a town or village less when a branch closed. The sample size was not massive.

The CAB felt that there were issues where banks operating with big margins were able to exist due to how uncompetitive the market was. The entry barriers for competitors were high. The free current account was part of the problem.

From the resolution or financial stability side a highly volatile market was not desirable as firms went out of business.

The financial scandals of the last 20 years could be traced back to the free current account as banks had to make a profit elsewhere. 87% of banks funding for lending was coming from domestic deposits. These were known in the sector as NIBLES – non-interest bearing liabilities. These institutions were making a fortune from lending deposits. Customers were paying for their account, but the cost was hidden with some customer cohorts paying more than others.

## Appendix 2

Sources of evidence submitted in response to our call for evidence are to be found on the APPG website:

- Evidence submitted by the BSA;
- Nottingham Building Society work on Access;
- FCA Financial Lives Survey;
- Evidence from Professor Llewellyn of Loughborough University.

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