

Rt Hon Mel Stride MP
Chair, Treasury Select Committee
House of Commons
London
SW1A 0AA

CC:
Rt Hon John Glen MP
HM Treasury
1 Horse Guards Road
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By email

14 May 2020

Dear Mel Stride MP

Banking Competition Remedies update

BCR has regularly kept TSC informed of Banking Competition Remedies' (BCR) plans and activities and the purpose of this letter is to share some background with you and your committee about BCR and update you on the latest developments.

Background to BCR

BCR was established in 2018, to implement the £775 million Royal Bank of Scotland (RBS) State Aid Alternative Remedies Package, following the 2008 financial crash which led to recapitalising RBS. The European Commission placed a number of State Aid measures on RBS to limit the distortions in competition that resulted from state support. HM Government, RBS and the European Commission worked together to find a way to resolve RBS' State Aid commitments and increase competition and expand competition among challenger entities in the SME banking market.

One of those commitments was for RBS to divest the business formerly known as Williams & Glyn with the objective to mitigate the distortion of competition in the UK SME banking market. However, by late 2016 RBS were unable to divest Williams and Glyn and HM Government sought to replace the commitment with an alternative package of measures aimed at increasing banking competition in the SME market. In September 2017, the Alternative Remedies Package was agreed with the European Commission as a resolution of RBS' final State Aid commitment. Subsequent to that, Banking Competition Remedies was established as the delivery mechanism.

BCR's purpose is to implement the Alternative Remedies Package. It has had no involvement in the design of the eligibility criteria for applicants, the timelines for delivery, the legal agreements to be entered into, the sums to be disbursed or the associated processes for those engaging with the two workstreams. These details were worked out and agreed between HM Government and the European Commission. As underlined from the outset, the ability of BCR to alter or revise these details is extremely limited.

The **Alternative Remedies Package** comprises two RBS funded measures amounting to £775m:

The Incentivised Switching Scheme – to which up to £275m is allocated to assist SME customers within the Williams & Glyn business to move to ‘challenger banks’. A further maximum sum of £75m has been set aside within RBS to cover customers’ switching costs.

The Capability and Innovation Fund – to which £425m is allocated to support the development of wider capabilities and competition in the SME banking market essentially through grants to eligible challenger institutions across 4 “pools”.

BCR’s remit includes:

- Providing information to applicants in respect of the Capability and Innovation Fund and Incentivised Switching Scheme.
- Managing and disbursing the Capability and Innovation Fund to Eligible Bodies.
- Administering dowry payments to Eligible Bodies and overseeing the delivery of the Incentivised Switching Scheme.
- Monitoring compliance by Eligible Bodies with the terms of the agreements governing the use of funds.
- Reporting publicly on the Alternative Remedies Package each quarter and meeting with awardees to discuss progress

Corporate Governance

HM Treasury established BCR as a limited company and appointed two directors by an independent Nominations Committee (Brendan Peilow and myself), and we were joined by Aidene Walsh some months later. While BCR is not required by its Articles of Association to appoint Non-Executive Directors (NED), the board has chosen to appoint two NEDs as part of ensuring enhanced governance and decision-making.

HM Treasury appointed Mazars as the official Monitor for the project. The Monitor has been kept closely informed and attended BCR board meetings and other decision meetings in addition to regular meetings with BCR. We also regularly update HM Treasury directly.

Activity and achievements so far

Throughout this project, BCR has sought to fund initiatives which, if successful, will ‘move the dial’ on competition in the SME banking services sector. It was always intended that the Incentivised Switching Scheme would have a more immediate impact, while funds deployed under the Capability and Innovation Fund will take longer to deliver fundamental change.

The Capability and Innovation Fund

In 2019, 15 grants under the Capability and Innovation fund were awarded across four Pools (A, B, C and D). The process attracted 165 applications and from this we chose a diversity of awardee strategies to optimise the choice for UK SMEs across a breadth of financial services. BCR retains a robust focus on monitoring and compliance of all funding recipients. Each awardee has – at BCR initiative - made a series of public commitments against which they report quarterly and this is made available on our website. Awardees are also required to report and/or meet at such other times as the BCR may request.

The awards made were as follows:

Pool A

£120m – Metro Bank Plc
£100m – Starling Bank Limited
£60m – ClearBank Ltd

Pool B

£50m – Nationwide Building Society
£15m – Investec Bank plc
£15m – The Co-operative Bank Plc

Pool C

£10m – Atom Bank Plc
£10m – The Currency Cloud Group Ltd
£10m – iwoca Ltd
£10m – Modulr Finance Limited

Pool D

£5m – Codat Limited
£5m – Fluidly Limited
£5m – Form3 Ltd
£5m – Funding Options Limited
£5m – Swoop Finance Limited

What has been achieved in a period of profound economic and business uncertainty, has been remarkable. 13 of the 15 awardees are making traction on delivering against their public commitments; as one would expect some initiatives are making an impact more quickly, while others will take longer to come good and may at times need revision along the way.

So far, we are seeing that smaller and more digital awardees have generally been more agile in taking advantage of BCR funding in current circumstances.

Pool E will launch in the next few days (please see below) and at the same time we will be producing a table setting out the main achievements of every current awardee. I will ensure that a copy is provided to you as soon as it is available.

The Incentivised Switching Scheme

ISS has already made a difference in achieving switching rates above historic levels accounting for 32,773 SME customers moving from RBS to challenger banks in the 13-month period (beginning of March 2019 to end March 2020). That is some 50% of all non-personal switches.

This is a significant achievement given that it was widely expected that very few SMEs would even consider moving banks.

Switching is a matter of customer choice and in the current environment we are understandably seeing that switching is not presently a priority for SMEs.

Nevertheless, BCR continues to do everything possible within its terms of reference to streamline and support customer switching as well as exploring activity with RBS and HMT to enhance the scheme for those that do wish to switch.

Metro Bank and Nationwide

The design of the Alternative Remedies Package allows for any CIF awardee to approach BCR with an updated or revised business case. BCR may then approve or reject those changes. If a business case is rejected, the awardee would be required to continue with their original strategy. In such circumstances, it would be very likely that they would fail to achieve their commitments, which would not be a good use of BCR funds.

As you will have seen, in 2020, Metro Bank and Nationwide, have, following their own internal strategic reviews which indicated a change in business direction, each returned £50m to BCR. Both revised business cases were independent and honest recognitions that their respective strategies had changed and that they were no longer in a position to deliver some (Metro) or all (Nationwide) of what was originally proposed. Nationwide's decision to return funds was a result of Covid-19 impacting the interest rate environment and, being a liability led business, this caused specific issues for them.

As a board, BCR agreed that accepting the revised business cases, as foreseen in BCR's design, is a better outcome than the alternative: insisting to the boards of awardees that they continue with a strategy that is no longer appropriate and BCR possibly later seek to engage in a drawn out and expensive process of audit, with uncertain outcomes. It is a shame that Metro and Nationwide are not able to deliver their original Business Cases but we appreciate their transparency around being unable to meet the obligations under CIF.

The funds have swiftly been returned to BCR and this means that £100m is available to redeploy as 'Pool E'. With HMT and RBS' agreement, BCR is now moving forward with this next round of grants given the pressing need for support to financial challenger organisations working with SMEs.

Pool E consultation and process

BCR has consulted on the size of grants that should be awarded under Pool E.

The design of BCR limits us to consulting only on this specific issue and also to awarding no more than 20% of Pool E to the smaller organisations ("Pool D" eligible in previous round) and therefore up to 80% to bodies eligible under (former) Pools A, B and C.

We have recently completed a process of consultation with a wide range of organisations as to their views on the sizes of grants that should be awarded under Pool E. We contacted 238 organisations directly, while also publicising via relevant industry trade bodies, associations and the media; we have received some 100 responses.

Responses for Pool D bodies (£20m available) are very consistently in favour of grants in the £2.5m-£5m range. Responses from Pool A, B and C bodies (£80m available) show larger challengers advocating awards above £20m and smaller challengers advocating for awards £20m or less.

Based on these responses, the BCR board will decide on the grant sizes available under Pool E next week and we will then open the application and evaluation processes within the tight timetable required by BCR design. As always, the Monitor will attend that meeting next week and will maintain close scrutiny on the process on behalf of Treasury.

We will keep you updated as Pool E progresses. I hope this provides a helpful overview to you and the Committee of BCR and the work so far. If you would like any further information, please do let me know.

Yours sincerely

A handwritten signature in blue ink, appearing to be 'GC', enclosed in a light blue rectangular border.

Godfrey Cromwell
Chair: Banking Competition Remedies Ltd