



Unite the Union response to the Independent Commission on Banking call for evidence

This response is submitted by Unite the Union. Unite is the UK's largest trade union with 1.5 million members across the private and public sectors. The union's members work in a range of industries including financial services, manufacturing, print, media, construction, transport, local government, education, health and not for profit sectors.

Unite is the largest trade union in the finance sector representing some 150,000 workers in all grades and all occupations, not only in the major English and Scottish banks, but also in investment banks, the Bank of England, insurance companies, building societies, finance houses and business services companies.

Executive Summary

- **Increased freedom of competition at the expense of freedom of choice;**
- **Risk must be controlled and monitored to alleviate destabilising effects;**
- **Require a banking model more closely aligned to wider stakeholder interests;**
- **Promotion of diversity and choice in the banking sector;**
- **Increased stakeholder engagement;**
- **Fundamental review of remuneration and reward systems;**
- **More robust and rigorous regulation;**
- **The creation of an independent financial products licensing authority;**
- **The introduction of a financial transaction tax.**

Introduction

1. Unite welcomes the opportunity to respond to this call for evidence and recognises that financial institutions will need to play a more effective role in maintaining stability in the financial system in order to rebuild consumer trust and re-instil confidence in the sector both domestically and globally. Unite believes that it is vital that the outcome of any reform is the creation of a financial system which is reconstructed around values which support a long-term outlook that is sustainable and fair and takes account of social justice principles.
2. This response will look specifically at options available which will reduce market concentration. Unite believes that the issue of choice in retail financial services is distinctly different from the issue of competition. It does not necessarily follow that increasing competition will increase the choice available to consumers. In fact it could be argued that we have seen greater freedom of competition at the expense of freedom of choice.
3. **Question 1.1** of the issues paper relates to whether financial stability and competition can work in harmony and if not, what proposals can be put in place to alleviate the tensions created.
4. The UK financial services market has grown significantly over the past decade, creating employment and highlighting the important role the sector played in building a successful economy. However the events of the past few years have shown that global economies relied too heavily on financial services which have led Governments around the world to take drastic action to stabilise financial markets. It is now apparent that the level of risk and growth within the finance sector was unsustainable and that action must take place to alleviate the possibility that such destabilisation could happen again.
5. Considerable debate, discussion and reflection have taken place to assess the damage done to and by the sector and to look at a new approach to financial services including reforms to regulation, remuneration, supervision, governance and competition to rebuild its reputation.
6. Unite recognises that growth and expansion can be positive aspects of business, creating employment and contributing positively to the economy and would not wish to curb this by recommending risk averse behaviour as the way forward. It is also recognised that a degree of risk is present in many business decisions which can create dynamic and innovative workplaces. However Unite would argue that it must be mitigated risk which is controlled and monitored closely to avoid the destructive results we have seen in the last few years.

7. Workers, consumers and taxpayers have paid a very high price for the irresponsible behaviour of a few. Unite would doubt whether any of these groups would have the appetite to bail out the banks in the future. Therefore 'business as usual' is not an option. Real changes are necessary to deliver a banking industry more aligned to wider stakeholder interests and Unite would argue this should be the model to move forward with.
8. Some of the proposals Unite would put forward to alleviate tensions between stability and competition would include:
 - Diversity in retail financial services with a consumer driven focus;
 - Expansion of providers;
 - Increasing choice in products, services, experiences and relationships;
 - Increased stakeholder engagement;
 - Transparency in remuneration systems including incentive structures;
 - Increased recognition of service delivery rather than volume of sales;
 - More intrusive regulation.

Promoting diversity and choice

9. Unite would argue that diversity should include increasing the choice of service providers, the products and services available, relationships and experiences as well as increasing the coverage on offer which serves the needs of all of society. A diverse finance sector is also better placed to serve the needs of a diverse population including those who are financially excluded.
10. Historically mutuals, cooperatives and building societies had an important stake in the local community in which they operated with many building societies and cooperatives built upon the principles of social justice. The Joseph Rowntree Foundation Paper: Community and mutual ownership: a historical review has clearly identified this. It states:

Co-operative societies, friendly societies, building societies and other mutual enterprises flourished in the 19th century. They met the basic needs relating to saving, insurance, food and housing for those affected by poverty and exploitation. Through collective self-help, members gained greater control over their lives. By the end of the 19th century, mutual organisations had grown into highly significant businesses based on democratic member control and federal structures. During the 20th century their role was to be undercut by the growth of state welfare, fierce commercial competition and a loss of purpose in a more affluent society.¹

¹ <http://www.jrf.org.uk/sites/files/jrf/community-mutual-ownership-summary.pdf>

11. Mutuols continue to be viewed as more customer focused and egalitarian. According to Mutuo, a campaigning organisation to promote mutuo, mutuo are regarded as democratic organisations in that they are owned by and run for the benefit of their members. They also add a competitive element to the sector, are more customer focused and their business model ensures they adopt risk-averse behaviours.
12. A Which? Publication survey of customer satisfaction for current accounts carried out in 2010 showed Cooperative bank at 86%, Nationwide 72%, HSBC 58%, RBS 55%, LTSB 54%, Barclays 53% Halifax 48% and Santander at 47%²
13. While remaining attractive to consumers mutuo are, however, facing increased financial pressures in the present economic climate as their business model means that they operate within tighter margins than other finance sector companies. They rely more heavily upon investing their deposits which, given the extremely low interest rates, means that returns are reduced with inevitable consequences for profit margins which could help to fund expansion opportunities and attract new customers with attractive deposit rates. This coupled with the present system of funding the Financial Services Compensation Scheme (FSCS) (see undernoted) has created a severe squeeze on the profitability of mutuo putting some of them at risk of take-over or even survival.
14. There is undoubtedly room for an expansion of mutuo in the UK market. Between 1910 and 2010 the number of building societies in the UK has reduced from 1700 with total assets of £76 billion, to just 55 building societies. Some of this can be attributed to demutualisation. However despite the reduction in societies the total assets held by building societies has increased significantly to £360 billion.³ By way of contrast, the assets of all banks in the UK stand at almost £8 trillion.⁴
15. Mutuo have 23 million members in the UK and remain a viable alternative to the dominance of banks in the high street.⁵

FSCS

16. As stated previously the building society business model differs greatly from that of banks. Building societies aim to provide the best interest rates to borrowers and savers, rather than maximising profit to pay dividends to external shareholders. The present system for calculating the Financial Services Compensation Scheme (FSCS) levy is based

² Which members survey of customer satisfaction 2010 (Sample size: 328 Coop, 1407 HSBC, 1451 Nationwide, 704 RBS, 2130 LTSB, 1844 Barclays, 749 Halifax, 465 Santander)

³ Figures from Building Societies Association

⁴ BBA Annual Abstract of Banking Statistics 2010

⁵ Mutuo: Facts about Mutuo

upon the size of retail deposits held which because of their need to retain larger retail deposit balances, has resulted in a detrimental impact to building societies

17. Unite would therefore wish to see a review of the method of calculating the levy which does not cause detriment to a particular business model. According to the Mutual Chief Executive Opinion Survey 2010, mutuals had to pay a disproportionate fee to the FSCS towards the rescue of several banking groups during the financial crisis, against the lowest Bank of England base rate in recent years, which squeezed their profits further. As a result of provisions for the FSCS levy, building society profits before tax in 2008/09 accounts were 64% lower than they otherwise would have been. Moreover 37% of respondents to the survey also said that they had cancelled or postponed projects, and 30% said that they had reduced their investment in staff.⁶
18. The Commission must therefore look at new methods of raising finance to subsidise the levy that does not compromise the mutual business model.
19. The financial crisis in the UK saw Northern Rock, Royal Bank of Scotland and Lloyds Banking Group receive Government assistance to survive and today they remain wholly or partly owned by the taxpayer. Further intervention through Government backed guarantees providing 100% reassurance on financial deposits in these companies resulted in a significant withdrawal of monies from those who were only guaranteed at 50%.⁷
20. It is therefore difficult to argue that the finance sector is operating in a completely 'free' market when organisations like the Building Societies Association see government intervention, in some of the biggest companies in the sector, as distorting competition.
21. Despite support for mutuals Unite recognises that banks serve a vital role in society. Banks provide a necessary function and offer a number of distinctive services required of an advanced economy in that they deliver facilities for the provision of payments and insurance services both retail and wholesale, payment clearing functions, conduct financial intermediation between organisations which pools risk thereby increasing choice and they are more likely to provide financial services to businesses. They operate a much broader remit than most mutual organisations.
22. It would however be disastrous for consumers if mutuals were pushed out of the market by constraints in funding or unfair competition which may limit their ability to expand and compete. It is incumbent on the

⁶ Building Societies Association Mutual Chief Executive Opinion Survey 2010

⁷ This guarantee was removed in May 2010

regulator and industry leaders to consider ways which will ensure the UK finance sector increases its diversity.

Increased stakeholder engagement

23. In response to **Question 2.1** Unite sees the need for greater public and employee engagement at a corporate level within the company to provide legitimacy to the decision-making process and to oversee corporate governance principles which take into account the interests of all stakeholders.
24. It is important that the stakeholder voice is heard among that of institutional investors and directors, and that the views of a more representative group of people are taken into account who can challenge the existing orthodoxy on corporate governance. This is equally true at an international level within the EU and beyond.
25. Unite commissioned a report by the Financial Inclusion Centre 'Reforming the Financial System' which looks at changing the financial system which presently exists. This report highlights the need for greater public interest representation and recommends a minimum number of seats specifically reserved for public interest groups. Unite would endorse this.
26. Unite has consistently argued for improved dialogue at boardroom level for trade unions and other stakeholders. This would provide a wider range of views, opinions, ideas and interests which more closely represent the society in which we live and in which the finance sector operates.

Reward systems

27. Another initiative identified in **Question 2.1** which the Commission should consider is more robust and transparent regulation of pay structures.
28. Unite believes that remuneration and reward systems which are based upon performance and driven by targets, should be reviewed. Many companies within the finance sector favour rewarding sales figures which pay little or no regard to customer service. Remuneration must be transparent, accountable and open to independent scrutiny. Unite would argue that sales targets and rewards are not commercially sensitive therefore the industry should make their pricing policy publicly accessible with online access to the information.
29. The rise in comparison websites in the UK has given consumers unlimited access to compare products and services on everything from electrical products to utilities. In financial services this could be extended to compare the sales rewards and commission earnings on financial products. This would allow consumers to make choices based

on the increased information and knowledge on the incentives available to staff for product sales.

30. This scheme would be independent from the finance industry however the industry would pay to administer it. Finance sector companies would be reassured that they were truly transparent and willing to make available information that is presently obscured from public view but which may influence a financial decision made by consumers. This would enhance the FSA Treating Customers Fairly principles.
31. Furthermore, evidence shows that the target driven sales culture in which retail financial services operates does not provide real customer service or treat customer fairly. Customers are registering their dissatisfaction, which is evident in the level of consumer complaints reported to the Financial Services Ombudsmen which has increased significantly in the past few years and by 17% in 2010 to 925,000.
32. This included complaints regarding Lloyds Banking Group (22,420), Barclays (9,215), Santander (5,372), HSBC (4,031) and Royal Bank of Scotland Group (6,469). Nationwide Building Society had 1100 complaints against it and Cooperative Bank had 700. While acknowledging the difference between mutuals and retail banks in the number of customer accounts, 52% of the total number of cases the Ombudsman dealt with related to five of the UK's largest retail banks.
33. **Question 2.2** asks which specific measures to reduce market concentration should be developed further. Unite would suggest that greater scrutiny should be undertaken in mergers and acquisitions.
34. Unite has serious concerns about the fact that no one involved in determining the outcome of a takeover bid is required to take account of the long-term interest of the target company.
35. In addition, the interests of the long term stakeholder including the employees, suppliers, communities and the wider interest of society are not taken into account. The outcome of the bid is decided by shareholders alone, depending on the price of shares. Whilst shareholders want the highest price for shares, far from this meaning a takeover is in the long term interests of the company, the opposite is often the case, particularly if it means being saddled with more debt.⁸
36. Shareholders are not the only stakeholder in a business. Those working in the business have a very important interest in the outcome of a takeover. In a takeover, by selling their shares, shareholders can exit a company – but other stakeholders, especially employees cannot get out - they are the ones that stay. Employees in a company have at least an equal interest in the outcome of a takeover as shareholders.

⁸ These concerns are considered more fully in the Unite response to the Takeover Panel consultation at www.unitetheunion.com

37. A statement contained within the Coalition Agreement appeared to suggest support for more varied banking models which would increase competition as the way forward. It states:

We want the banking system to serve business, not the other way round. We will bring forward detailed proposals to foster diversity in financial services, promote mutuals and create a more competitive banking industry.

38. Unite would therefore question whether the sale of 318 RBS branches to the Santander Group, as a result of European Union obligations on competition, has in fact increased competition or promoted diversity in the sector.

39. According to the IBCs own document “the UK banking sector is especially concentrated in the retail & commercial banking sector, where the top six banks account for 88% of retail deposits”. Following the transfer of the RBS branches to Santander this figure will remain unchanged. This sale has not increased competition or choice but rather shifted ownership between the main players in the market.

40. Santander has more bank branches than any other bank in the world⁹ and through its purchase of other UK high street brands such as Abbey National, Alliance and Leicester and the savings arm of Bradford and Bingley, has captured a significant proportion of the banking market in the UK.

41. With Northern Rock likely to be sold off in the near future and LBG also being forced into selling off branches due to EU rules, Unite would wish to ensure any sale of Northern Rock, LTSB or Cheltenham and Gloucester branches are sold to a competitor which increases competition and choice in the market but also provides the workforce with a degree of job security.

42. One of the possible reform options listed in **Topic 2** includes the separation of retail and investment banking. Indeed there is much debate in the UK about the need to split banks into either retail banks or investment banks to reduce risk. Unite has made no policy decisions on the separation of investments and retail banking. To be clear we are not sure that the arguments have been made sufficiently one way or another. Big banks failed, small building societies failed. Lehman Brothers, who were mainly an investment bank failed, but Barclays a mainly retail bank, didn't.

43. Unite recognises that no matter which system is in place, it is the risks associated with reckless behaviour that needs tackled. It is about

⁹ About Santander www.santander.co.uk

ensuring that sufficient safeguards are put in place to protect against undue risks. The regulatory structures must be robust enough to ensure that no organisation can be in a position to take a risk which is bigger than the company itself. The regulator must be more challenging by introducing better and more rigorous investigations and be prepared to ask difficult questions.

44. To this end Unite therefore believes that there should be greater integration of the FSA into the business functions, applying a more inquisitive element which is embedded within the strategic role of the company. Just as the risk function has become integral to the company, so too must the supervisory and regulatory function; perhaps the ability to second individuals to the company working independently and autonomously from within the firm providing robust oversight.
45. To reduce risk Unite believes that consideration should be given to a new, independent financial products licensing authority, based on an industrial patent structure. Products should be stress tested to ensure no product or combination of products is so risky that the potential could exist for bringing down the institution or the economy. This could be done within tight parameters where risk could be measured prior to going to market. Products should also be completely transparent.

Regulation

46. **Question 3.3** relates to the shadow banking sector. Unite would wish to see improved transparency and regulation in this particular part of the sector. It was evident that significant risk from within the shadow banking sector also contributed to the financial crisis.
47. Unite would see a role for a UK version of the Volker rule to restrict speculative investment if companies do not deliver benefit on behalf of their customers. The Volker rule restricts proprietary trading that is not for the benefit of customers. Financial transactions carried out purely on the basis of gambling on making a profit but serving no real function would appear to be a wasteful exercise. Indeed it is this type of speculative transaction that Adair Turner, Chairman of the FSA referred to during a Mansion House speech in September 2009 when he commented that some financial activities were 'socially useless'. In the same speech he made reference to Stephen Green, Chairman of the BBA who said that 'in recent years, banks have chased short-term profits by introducing complex products of no real use to humanity'.¹⁰
48. Both Turner and Green are respected individuals in the industry. Both men know how banks are regulated and managed. If they believe this to be the case it is somewhat disconcerting that transactions are concluded and products sold which are not, in the long run, in the best interests of consumers or society but are purely speculative.

¹⁰ http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0922_at.shtml

49. Unite has supported calls for a financial transaction tax to be introduced to generate an income from this very complex industry. According to the Robin Hood Tax campaign it is estimated such a tax, charged at 0.05% could raise as much as £20 billion per annum based on current transactions levels within the UK alone. Such a tax would include taxing transactions on foreign exchange dealing, hedge funds and trading in bonds, gilts and derivatives. Even given significant reductions in the level of transactions should a European Volker rule be introduced, the receipts from the tax would still be significant and could be used to fund public sector projects and to combat issues such as climate change.
50. The introduction of such a tax on speculative practices should also help to reduce casino style gambling in financial transactions and curb the short term, quick gain model which has damaged the sector irrevocably. It would also help at a domestic level, to repay a debt owed to society and taxpayers for the financial support which helped stabilise the sector.
51. By comparison Unite believes that the recent announcement by the Coalition Government in the Comprehensive Spending Review to introduce a financial levy will do little to alter behaviours and will not deliver the financial benefits to the economy that the sector could afford or come close to the potential financial benefits of a transaction tax. It is estimated that this levy could raise around £2.5 billion per annum. The rate as yet is undetermined however an HM Treasury paper in June 2010 suggested that a rate of between 0.04% and 0.07% could be likely.¹¹ This would generate a surmountable sum, yet far short of what could be raised by the introduction of a transaction tax even given possible future restrictions in speculative transactions.

Conclusion

52. Unite believes that a re-evaluation of the banking business model which incorporates a moral and ethical dimension to the business is required; one which regards good customer service as equal to good sales techniques and rewards accordingly; one which gives regard to fairness in employee relations as well as treating customers fairly. This should be a prerequisite in expanding competition and choice in the UK banking sector and should be supported by the IBC.
53. Unite believes that the industry needs to put its house in order and restore trust and confidence to demonstrate, without doubt, that the sector has done enough to ensure a more positive outcome should we be in the unfortunate situation should these circumstances happen again in the future. The sector appeared ill-prepared last time around

¹¹ http://www.hm-treasury.gov.uk/d/junebudget_bank_levy.pdf

with little contingency in place to resolve the situation internally and instead sought help from the Government.

54. The industry could do itself a favour by ensuring checks and balances of key functions are in place and are robust enough to deal with any eventuality should it arrive.

55. Unite is not advocating increasing and restrictive regulation. Indeed would support the innovation, vitality and dynamism that come from allowing companies to manage their businesses without over-intrusive or restrictive regulatory practices, provided that the business is conducted in a manner which does not jeopardise jobs and takes accounts of fairness, reasonableness and social justice.

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