Topic 4: Understand different types of bank account

After completing this topic, you will be able to:

- list the different types of bank account and compare them, including:
  - current accounts (including basic and packaged accounts);
  - savings accounts;
  - extra featured accounts;
  - loans accounts; and
  - mortgages (including offset and current account mortgages);
- understand how bank accounts work, including:
  - paying money into bank accounts;
  - deposit (paying-in) slips;
  - the different ways of taking money out of a bank account;
  - cheques;
  - the clearing cycle; and
  - cash cards and debit cards;
- understand the ways of accessing information about accounts, including:
  - statements;
  - automated teller machines (ATM);
  - online banking; and
  - telephone banking;
- understand special signing arrangements, including:
  - joint mandate;
  - joint and several liability; and
  - lasting power of attorney.

Current accounts

A current account is the most common type of bank account and it is suitable for everyday needs. It is the account into which your income (that is, your wages or salary) will be paid, usually by direct transfer, and out of which your monthly bills will be paid. A current account is where you would get money from in a hurry and where you would pay in any cheques that you receive.

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There are usually quite a few transactions on a current account every month and banks rarely pay interest on this type of account, so they are not meant for savings; rather, they are meant for everyday use.

A current account has two numbers:

- a **sort code** – that is, a six-digit number, such as '12–34–56', which identifies the bank and, in particular, the branch office at which the account is held; and
- the **account number** – that is, an eight-digit number that is unique to the account holder.

Whenever a payment is made into the account, these two numbers must be used to make sure that the money goes into the right person's account.

Sometimes, there are charges on current accounts: those that are used by businessmen, for example, may have a monthly charge imposed because there could be literally hundreds of transactions every month for the bank to process. There are other charges that apply to anyone, but they usually apply only if you do not manage your money and your account properly.

A current account usually has the following facilities.

- **Bank statements**

  These are lists of recent transactions that the bank sends to you.

- **Standing orders**

  These are payments that you can set up to be made from your account to another account on a regular basis (usually monthly) and for the same amount each time. An example would be a payment of £100 each month from your current account to your savings account.

- **Direct debits**

  These are instructions given to your bank to allow certain companies (such as an electricity company or telephone company) to take money from your account to pay bills. These are usually monthly and the amount taken each month is different depending on the amount of the bill.

- **A chequebook and a debit card**

  We will look at these in more detail later in this topic.

- **An overdraft**

  This is a facility through which the bank temporarily allows you to spend more than you have in your account. For example, if you were to write a cheque and there were not enough money in your account to pay the cheque, the bank might still pay it – but this will mean that it has temporarily lent you

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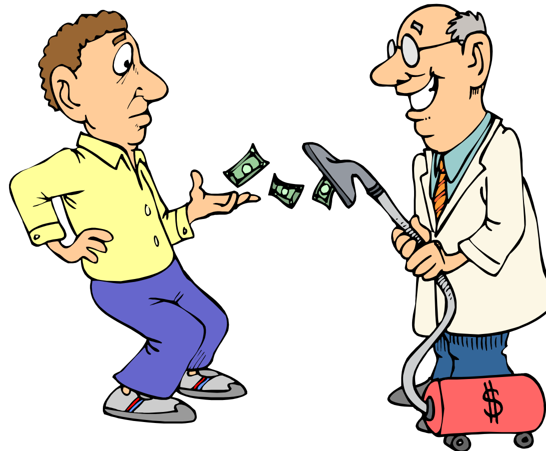
the money until you can put some more money into your account, or until you get paid.

– An 'arranged', or 'authorised', overdraft is an overdraft for which you have asked the bank first.

– An 'unauthorised' overdraft is an overdraft for which you have not asked its permission first, for which the bank will charge you.



Packaged accounts

Current accounts that offer extra benefits in return for a monthly fee – known as 'packaged' accounts – now make up almost a quarter of all of the current accounts available.

The benefits of a packaged bank account might include:

- a range of insurance products (for example annual travel insurance and mobile phone insurance);
- protection against the consequences of identity theft;
- preferential savings and loan rates;
- access to the VIP lounge at various airports;
- return lost keys schemes;
- will-writing; and
- music downloads.

Did you know?

The fees payable vary. Lloyds Bank has an account that has a fee of £5 per month, but the account can also be free to run, depending on how it is managed.

Source: www.lloydsbank.com

Activity 4a

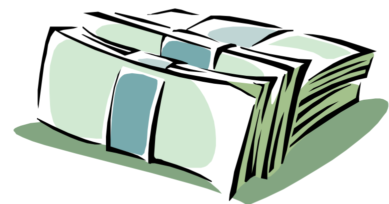
Visit www.lloydsbank.com and select 'Products and services', then click on 'Current accounts'. Examine the terms of the current accounts offered by Lloyds Bank.

a) What is the name of the Lloyds Bank account that has a monthly fee of £5?

b) Under what circumstances is this £5 monthly account fee waived?

c) On the same webpage, click on 'Continue to account details'. What other benefits are provided with this account? Are they worth the £5 fee, assuming it is charged?

Savings accounts



There are many different types of savings account, all of which are provided by the main banks and building societies. Unlike a current account, you would generally open a savings account to put money away that you do not expect to need in the short term.

Savings can be of small amounts (such as, £10, £20 or £30), or they can be of hundreds or thousands. Savings accounts are a safe place to put spare cash that you do not require for everyday expenditure; as well as being safe, your money earns interest, so it grows.

You can put money into savings accounts in many ways, including:

- by transfer from your current account;
- by paying straight into the account over the counter at the bank or building society; or

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- by making regular payments using a standing order.

The differences between the various savings accounts mainly relate to how often you put money into, or take money out of, the account.

Instant-access accounts

Instant-access accounts allow you to take your money out whenever you want it. Money can be taken from this type of savings account at a branch, or by transfer to a current account. Transfers can be organised at a branch office, by letter, by telephone call or online. The method that you will use will depend upon where your account is held.

The interest for instant-access accounts is usually very low.

Notice accounts

You must tell the bank or building society before you want to take money out of a notice account. Notice can vary between seven days, a month, three months or even a year. The usual types are seven-day and one-month notice accounts.

If you use a notice account, you might get a better rate of interest – but if you do not give the required notice before making a withdrawal, you will be charged a penalty.

Regular savers accounts

Regular savers accounts try to encourage you to put some money into the savings account on a regular basis. For many people, this is monthly – often when they get their pay. If you are paid weekly, you might put a bit into the account weekly. It is usual to set up a standing order from your current account to do this.

Sometimes, the interest rate is higher for regular savers. You can withdraw your money if you need it, but there might be restrictions as to how many times and how much you can withdraw – for example, two withdrawals a year.

Individual savings account (ISA)

An individual savings account (ISA) is a tax-free savings scheme offered by most banks and building societies, and some other organisations too. 'Tax-free' means that when you receive your interest, there will not be any tax deducted from it, unlike most other savings accounts.

There are limits on the amount that you can save in an ISA because of the tax advantages. The maximum amount of money that can be saved per tax year in an ISA is announced each year in the Budget. For the tax year 2016/17 the investment limit is £15,240, and

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from April 2017 it is £20,000. You can have only one ISA per year and since December 2015 it has been possible to reinvest any funds that are withdrawn from an ISA account (previously this was not allowed).

Help to Buy ISA

A Help to Buy ISA is a special ISA launched on 1 December 2015 to help first-time buyers save for a deposit for a house, with help from the government. The saver can save up to £200 per month, and the government adds 25 per cent tax-free to the amount in the ISA when it is used to buy a house, up to a maximum government bonus of £3,000.

Two people can both contribute funds from their respective Help to Buy ISA towards the same property, but they must both be first-time buyers.

Lifetime ISA

The Lifetime ISA was announced in the March 2016 Budget. It can be opened by individuals aged between 18 and 40, allowing them to save up to £4,000 a year (as part of the regular ISA limit). At the end of the tax year the government adds a 25 per cent bonus, so savings of £4,000 will receive a £1,000 bonus, plus interest or growth. The bonus is paid annually until the age of 50. Savers can use the Lifetime ISA to purchase their first home or save for retirement.

Child Trust Fund

The Child Trust Fund (CTF) is a long-term, tax-free savings account for children, but only children born between 1 September 2002 and 2 January 2011 qualify for this type of account. The government sent a voucher for each child who was entitled to CTF and this was used to open an account in the child's name. The annual investment limit is £4,080 for the tax year 2016/17, although the money cannot be accessed until the child reaches the age of 18. Children who do not qualify for the CTF can open a junior ISA.

Junior ISA

Junior ISAs are tax-free savings accounts for children under the age of 18 who do not qualify for the CTF. Anyone with parental responsibility for an eligible child can open a junior ISA. The annual contributions limit for junior ISAs for the tax year 2016/17 is £4,080. Anyone can contribute to a child's junior ISA, provided that the total contributions do not exceed this limit. The money in a junior ISA cannot be accessed until the child reaches the age of 18, at which time the junior ISA becomes simply an ISA and the contributions limits are increased accordingly.

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Interest rates

Banks and building societies use the money that people put into accounts to make loans to customers. They charge these customers interest for borrowing money. The banks pay some of this interest back to account holders to encourage them to keep money in their accounts.

Annual equivalent rate (AER)

Some savings accounts pay interest yearly and some pay monthly. So, when different savings providers advertise their interest rates, it makes it difficult for people with money to save to compare all of the accounts available and decide which one represents the best choice for them.

All savings providers must therefore quote the interest rate as an annual equivalent rate (AER). This means that the interest rate on all accounts, even those that pay monthly, is quoted as if interest were paid once a year, making it much easier to compare one account with another.

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Activity 4b

Visit a website such as www.halifax.co.uk and click on 'Savings' and then 'Compare savings accounts'.

There are lots of them and it can be hard to work out what makes them different. Completing the following table will help you to make a judgement.

Type of product	AER	Special terms
Regular Saver		
Fixed Saver		
ISA Saver Variable		
ISA Saver Fixed		

Activity 4c

From the accounts in the activity above, try to choose the best one for these people and give your reasons.

Background information	Type of saving
Bettina is a new graduate and has just started working for a computer company. She has spare money each month, but the amount can change. She wants to save for a holiday in 12 months' time.	
Jimmy and Louise are approaching retirement. They have £10,000, which they want to keep for their dream trip to Australia in two years' time. They are worried that interest rates may fall and that the money they can get on their savings will be less.	

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Mandy is in her 30s and has a very well-paid job. She pays tax at 45 per cent on some of her earnings. She gets an annual bonus of around £5,000, which she never spends. Mandy would like a savings account that is as tax-efficient as possible. She likes to know what interest she is going to receive each year.	
Amy has just inherited £13,500. She is not sure what to spend it on yet or when; it has all been a bit of a surprise. She believes that interest rates will increase in the near future. She has a high level of earnings and pays tax at 40 per cent.	

Loans

Loan accounts are an arrangement with the bank. The bank lends money for a period of time and the customer makes regular repayments to reduce the amount borrowed.

Loans tend to be made for larger sums of money than overdrafts. Overdrafts are designed to be used for short periods of time (such as a few days a month) and for smaller sums of money (for example, a few hundred pounds). Loans are for larger sums of money (such as several thousand pounds) and for longer periods of time – for example, 12 months, three years, five years, seven years, or 15 years.

There are two types of loan:

- personal loans; and
- mortgages.

Personal loans

People can borrow by getting a loan from a bank or building society. Loans can be made for a specific purpose, such as a car loan. A personal loan is a way of borrowing a sum of money for a period of time. For example, someone could borrow £10,000 over three years, or £2,000 over two years, etc. It is up to the borrower to look for the repayment period that will suit them best.

The monthly repayments will be the same each month and the interest rate will not change.

When you look at the cost of a personal loan, the lender will tell you the monthly repayments, which will be the same each month.

Why do you think it is a good idea for the repayments to be the same each month?

Mortgages

Mortgages are loans that are used to buy a home, such as a house or a flat.

Mortgages are secured on the home that they are used to buy. This means that if the borrower does not repay the mortgage, the lender can take the borrower's home (that is, 'repossess' it) and sell it to get its money back.

Mortgages are available from banks, building societies and specialist mortgage companies. The most usual repayment period for a mortgage is 25 years, although mortgages can be for a shorter or longer period of time.

A mortgage is the largest loan that most of us ever get. Because they are secured loans and the repayment period is so long, the interest rates on mortgages are almost always lower than for other forms of borrowing.

What do you think happens when someone with a mortgage sells their home and buys another one?

The Financial Conduct Authority (FCA) gives the following advice:

> There are many mortgages available on the market, with different interest rates and different charges. When you are looking for a mortgage, it is important to shop around, not just for the best interest rates, but also for the best type of mortgage to suit your circumstances. There are specialist mortgage advisers that help you to do this.

Source: FCA, *Money Advice Service: Mortgages*

Another thing to consider when borrowing such a large amount of money over such a long period of time is how you are going to pay it back. There are different types of repayment method from which you can choose, as follows.

Repayment mortgage

With a repayment mortgage, you make monthly repayments for an agreed period (called the 'term') until you have paid back the loan, including the interest. The interest rate is likely to vary over the period of the mortgage and so you will be quoted a variable APR at the beginning. When interest rates change, so does the amount of your repayment each month – but by the end of the term, you will have paid off the mortgage in full.

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Interest-only mortgage

With an interest-only mortgage, you make monthly payments to the lender for an agreed period, but these will cover only the interest on your loan. The payments to the lender are therefore lower than those of a repayment mortgage. During the term of the mortgage, interest rates may change, and so will your payments to the lender.

At the end of the term, you will still owe the lender the same amount as you borrowed, so, in order to build up enough money to pay it back, you need to save into some sort of savings plan or investment over the term of the mortgage.

Loan to value (LTV)

Once the mortgage provider has worked out whether the customer can afford the mortgage, another thing that it takes into account is the value of the property that the customer wants to buy. This is because if that customer were to stop making repayments, the lender would have the right to take the property from them and sell it to get its money back. The property is the lender's 'security'.

So that the property will always be worth enough to sell and get the loan money back, the lender will lend only a certain percentage of the property's value to begin with. This is called the 'loan to value' (LTV) rate.

Case study

Jamie applies for a mortgage and the house that he wants to buy is valued at £300,000.

The building society states that its LTV rate is 75 per cent. So the maximum mortgage that Jamie can have is £225,000.

If he wants to buy the house, he will have to find £75,000 from his savings, or from somewhere else.

Activity 4d

Visit www.moneysupermarket.com/mortgages. Click on 'Fixed rate mortgages', change the tab category to 'Home purchase' and then click on 'Find mortgages'. Complete the following table with the top six lenders' deals on offer.

Provider	Mortgage fixed rate	Fixed until (date)	Fees	Maximum LTV

a) Which one offers the lowest fixed mortgage interest rate?

b) Which one has the cheapest arrangement fee?

c) Which one is prepared to lend with the highest LTV?

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Special types of mortgage account

Offset mortgages

An offset mortgage is a way of reducing the interest payable on a mortgage. A bank current account and savings account can be linked to the mortgage.

Each month, the mortgage lender looks at the amount that you owe on your mortgage, and also looks at how much you have in your savings and current accounts with the same organisation. So, if you were to have a mortgage of £100,000 and savings of £20,000, instead of charging you mortgage interest on £100,000 and paying you savings interest on £20,000, the organisation would offset one against the other and you would pay mortgage interest only on £80,000. This means that you have to give up your savings interest, but it can be worth it because it will reduce the amount charged on your mortgage. Because interest rates are always lower on savings accounts than on mortgage accounts, you save more than you lose.

By offsetting the savings against the mortgage to reduce the amount of interest charged, this can result in either lower mortgage repayments or, if you continue to make the full mortgage repayment (that is, the amount that you would have had to repay had you not offset your savings), it can result in the mortgage being repaid more quickly instead, as the following table illustrates.

Savings account balance	Monthly mortgage saving, causing an 'overpayment'	Time by which mortgage would be paid off earlier
£1,000	£57.74	4 years 0 months
£2,000	£61.88	4 years 3 months
£6,000	£77.40	5 years 2 months
£8,000	£86.46	5 years 6 months
£25,000	£152.80	8 years 2 months
£50,000	£235.75	10 years 6 months

Current-account mortgages

Current-account mortgages also work by combining your savings accounts and current accounts with your mortgage account with the aim of paying less interest. This time, instead of the mortgage being shown as a separate account, the mortgage is shown as though it were one very large bank overdraft on your current account.

The maximum overdraft is calculated using income and LTV; the bank produces a schedule of by how much the overdraft must reduce each month and will show this on your statement.

These are very flexible and are likely to be suitable only for people who can manage their money very well.

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Interest

Banks make money by charging interest on their lending. To work out the cost of borrowing, you will need to work out the interest costs. Interest is stated as a cost for each year.

Case study

Petra borrows £2,500 at an interest rate of 10 per cent.

The interest cost each year will be:

10% x £2,500 = £250

The APR and AER

Banks do not expect you always to have your calculator with you when you are trying to choose the best way of borrowing and the best provider.

As we saw above, AER is a method of comparing interest rates on savings. It works similarly for loans, except that the rate that all lenders must quote for loans is instead called the annual percentage rate (APR).

The APR is worked is worked out using a complicated formula, which includes:

- the interest rate;
- for how long you want the loan (known as its 'term'); and
- any fees.

Because the APR includes any fees that have to be paid, as well as the interest charges, it represents the *true* cost of the loan. If lenders were allowed simply to quote the interest rate, they would advertise their loans at really low interest rates to attract customers and tell them about the other charges later. Even if they were to tell the customers up front what all of the other charges were, it would be difficult for the customers to compare one loan with another. Comparing loans by means of their APR means that the customer can see at a glance which loan is the cheapest for them.

There are two types of APR, depending upon whether your loan has a fixed interest rate or whether it is variable (that is, the rate and the repayments can fluctuate over time).

Fixed APR

The APR on a personal loan is fixed, meaning that it does not change over the life of the loan. To work out your monthly repayments, the bank or building society will show you a table like the one overleaf.

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12.9% APR								
Months		12	24	36	48	60	72	84
		£	£	£	£	£	£	£
£1,000	*Monthly repayment*	89	47	33	26	22	20	18
	Total to repay	1,068	1,128	1,188	1,248	1,320	1,440	1,512
£2,000	*Monthly repayment*	178	94	67	53	45	39	36
	Total to repay	2,136	2,256	2,412	2,544	2,700	2,808	3,024
£4,000	*Monthly repayment*	356	189	133	106	89	79	71
	Total to repay	4,272	4,536	4,788	5,088	5,340	5,688	5,964

Activity 4e

Using the table above, find out the following.

a) ***The monthly cost of a loan of £2,000 for 48 months***

b) ***The monthly cost of a loan of £4,000 for 72 months***

c) ***The monthly cost of a loan of £1,000 for three years***

The table also shows the total cost of repaying the loan in full. For example, if you look at a loan of £2,000 over two years, you will see that the total that you will repay is £2,256.

What do you think the difference of £256 represents? Why do you think knowing the total to be repaid is useful?

Variable APR

If the interest rate on your borrowing can change, the APR is said to be 'variable'. Variable APR means that your interest payments can go up or down each month.

How bank accounts work

We have looked at the beginning of this topic at the different features of a current account. We are now going to look at these in a bit more detail.

How to pay money into a bank account

When money is paid into a bank account, we say that the bank account has been 'credited' with the sum of £45.

Can you think of the ways in which money can be paid into a bank account?

Case study

Johann goes on holiday and runs out of money. He calls his friend Abigail and asks her to transfer £100 to his account, giving him some money to spend for the rest of his holiday.

Johann then makes another bank transfer when he gets home, to pay Abigail back.

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The paying-in slip

'Paying-in slips' are paper forms that account holders fill in with details about their bank account and the amount being paid in. An example is shown below.

Paying-in slip

Date

Cashier's Stamp

Bank **ABC Bank plc**

Account Holding Branch

Customer's Name

Name and address of person paying in (if not the customer)

£50 Notes
£20 Notes
£10 Notes
£5 Notes
S & I Notes
£2 Coin
£1 Coin
50p
20p
Silver
Bronze
Total Cash
Cheques, P.O.s etc

Number of cheques

Sorting Code Number

Account Number

£

Please do not write or mark below this line or fold this voucher

Paying-in slips can be used to pay money into any account. An account holder hands this slip of paper to the bank cashier, along with the money that they want to pay in. The cashier types the account details into the counter terminal and checks the amount of money against the quantity written on the slip.

The bank provides *blank* paying-in slips for you to fill in at the branch, but it also gives you a supply of paying-in slips at the back of your chequebook. You might also get a separate 'paying-in book' full of paying-in slips. These will be already printed with your account details (name, sort code and account number) for convenience.

Case study

Sarah has a current account with XYZ Bank. There are paying-in slips at the back of her chequebook that look as follows.

Date

	£	p
Cash		
Cheques		
Total		

Date

Cashier's Stamp

XYZ Bank plc
30 High Street, Seaville S021 6TH

Account MS. SARAH HOLMES

Paid in by

£50 Notes
£20 Notes
£10 Notes
£5 Notes
S & I Notes
£2 Coin
£1 Coin
50p
20p
Silver
Bronze
Total Cash
Cheques, P.O.s etc

Number of cheques

Sorting Code Number 76 - 54 - 32

Account Number 12345678

£

Please do not write or mark below this line or fold this voucher

000000 765432 12345678

What the items on a paying-in slip mean

Stub (also known as a 'counterfoil')	The stub is the part of the paying-in slip to the left of the perforations. This part of the slip stays in the chequebook when the account holder tears out the slip. In this case, Sarah will complete the stub so that she has a record of what she has paid into her account. The bank cashier uses a rubber stamp to put the bank's name and date on this stub. The cashier also initials the stub. The cashier's stamp and initials prove that the bank has accepted the deposit on a certain day.
Date	There are two places in which the account holder writes the date on which they pay in the money: one is on the top of the stub and the other is on top of the paying-in slip.
Bank and branch name	In this case, Sarah banks at 'XYZ Bank plc', at '30 High Street, Seaville, SO21 6TH'. This address is already printed on the paying-in slip, so the bank knows where Sarah's account is held.
Account	This is the name on the account and helps to make sure that the money is paid into the right account. In this case, this is shown as 'Ms Sarah Holmes'.
Paid in by	When the account holder pays money into their account, they should sign their name in this box. Someone else can use this form to pay the money in for the account holder; this person should then sign in this box.
Number of cheques	The account holder will write the number of cheques that they are depositing in this box.
Sort (or sorting) code	This is a six-digit number that is unique to the bank branch that holds the account. The sort code (or sorting code) appears twice on the paying-in slip: in the box labelled 'Sorting Code Number' and at the bottom of the slip written in digits that a computer can read. In this case, the sort code is shown as '76–54–32'.
Account number	This is a number that is unique to the account at the relevant bank branch. In Sarah's case, this is shown as '12345678'.
Cash denominations	The table on the right side of the paying-in slip is for the amounts of cash and the total value of cheques being paid into the account. Denominations of cash greater in value than 10p are listed separately on this paying-in slip. The account holder needs to fill in the total value of each denomination that they are paying in. For example, if Sarah has two £5 notes, she will need to write '10' (ie £5 x 2 = £10) in the box for '£5 Notes'. The bank cashier will count the cash and tick off each entry in this

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	table to confirm that it is correct. If the account holder has made a mistake, the bank cashier will be able to find it and ask them to correct it.
Total cash	The account holder writes the total value of the cash that they are paying into their account in this box. The total figure should be the same as all of the cash denomination values added together.
Cheques, POs, etc	The account holder writes the total value of the cheques and postal orders that they are paying in here. They should also list the cheque numbers on the back of the paying-in slip.
Box at bottom of table	This is where the account holder writes the total amount that they are paying in – that is, the value of all of the cash plus the value of all of the cheques, etc.
'Please do not write or mark below this line or fold this voucher'	The numbers below this line are written in a way that computers can read. Banks ask customers not to write in this area because such marks could make it difficult for the computer to read the information provided by the bank. The preprinted slip has the account holder's account number and sorting code already written in this area. To process the payment, a computer operator adds the amount of the payment in digits that the computer can read. This gives the computer all of the information that it needs to process the payment correctly.

How to take money out of a bank account

Banks call money taken out of a bank account a 'debit'.

There are several ways in which money can be taken out of a bank account, including the following.

- **Over the counter**

  You can go into the branch office and withdraw money from your account by signing a withdrawal slip.

- **Standing order or bank transfer**

  Just as money can be paid into an account using a standing order or bank transfer, this obviously works the opposite way around – that is, you can arrange for money to be paid from an account using these two methods.

- **Automated teller machine (ATM)**

  You can take money out of an account using an ATM, sometimes called a 'cash machine', 'cash dispenser', 'cash point', or 'hole in the wall'. To do this, you need a personal identification number (PIN), which is your own secret four-digit number that works almost like a signature.

- **Online or telephone banking**

  You can arrange transactions online or by telephone. Of course, for this, you will need secret numbers and passwords, so that the bank knows that it is you making the request.

- **Writing cheques**

  We will look into this in more detail below.

- **Cash cards and debit cards**

  We will also explore these in more detail below.

- **Direct debit**

  Money can be taken out of an account using a direct debit, usually to pay regular bills for which the amount due is not the same each month. A direct debit differs from a standing order in that the payee 'collects' the amount of the bill from the account, rather than the account holder setting up a fixed amount to be transferred each month.

Cheques

A cheque is a written instruction to a bank or building society to pay a specific sum of money to a person or organisation.

Here is an example cheque, belonging to Sarah Holmes.

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76 - 54 - 32

XYZ Bank plc
Current Account

30 High Street
Seaville
S021 6TH

Date__________ 20___

Pay

£

A/C PAYEE

MS SARAH HOLMES

Date | To | Amount £

300061

Cheque Number 300061 | Sorting Code 765432 | Account Number 12345678

As you can see, a cheque is a printed form showing the bank and branch name and sort code where Sarah holds her account. The cheque also shows her account number and gives a unique number for this cheque.

The information on the bottom line of the cheque is printed in a way that can be read by computer. This makes processing cheques faster than keying in all of the information by hand. It is these computer numbers that are processed by the equipment used for clearing cheques.

Case study

If Sarah Holmes were to write a cheque payable to her friend, Mark Wright, she would write Mark's full name on the 'pay' line, insert the correct date, and then write the amount that she wanted to pay him in words and in figures.

Mark would then pay the cheque into his bank and the amount would show as a credit on his account.

The clearing cycle

The 'clearing cycle' is the name given to the process by which the money is transferred from the account of the payer (that is, the person writing the cheque) to the account of the payee (that is, the person to whom the cheque is paid). The payee will take the cheque to their bank and pay it into their account. Through the clearing cycle, the payee's bank will 'claim' that money from the payer's account, even though the cheque might be drawn on a totally different bank or branch.

This process is called 'clearing the cheque'. There are thousands of cheques paid into all of the different banks every day. So each bank adds up the amounts owed to it by the other banks at the end of each day, and vice versa, and they settle up at the end of each day.

The Cheques and Clearing Company has set up a '2–4–6' system, which is used by all UK banks and which works in the following way.

- **Day 1** – The cheque is paid into the bank account.
- **Day 2** – A cheque is cleared for interest payments. This means that, from Day 2, you will start to earn interest on the money paid in by cheque.
- **Day 4** – Your bank will allow you to withdraw the money (except from a savings account). The reason why there is a delay is that the bank has to make sure that the person who wrote the cheque has enough money in their account to cover it.
- **Day 6** – You can be certain that the cheque has been paid. (The bank now allows withdrawals from savings accounts.)

Did you know?

In December 2009, the Payments Council Board agreed to set a target date of 31 October 2018 to close central cheque clearing

However, despite the fact that cheque use has been in decline since 1990, there are still plenty of situations in which cheques continue to be used, so in July 2011 this decision was reversed and it was announced that banks and building societies will continue to issue cheques for as long as customers need them.

The Cheque and Credit Clearing Company (C&CCC) has been looking at a number of possible ways to improve the cheque clearing process – potentially moving away from paper to 'cheque imaging' – allowing payments to be made by mobile device

Source: http://www.paymentsuk.org.uk/project-delivery/cheque-imaging

Can you think of the sort of payments that you might get or make by cheque that would be hard to make using another method?

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Cash cards and debit cards

With a current account, you will normally be issued with a debit card or a cash card. A cash card can be used only to get cash, either over the counter or using an ATM. Young people, such as students or those under the age of 18, are usually given only a cash card.

A debit card is much more flexible because, as well as being able to use it in an ATM, it can be used to buy things in shops or online. When a purchase is made using a debit card, your card is swiped through a machine, which reads the information stored in the magnetic strip on the back. Your account is checked to see if you have enough money to pay for your shopping and, if there are sufficient funds, an electronic debit is made to your account – although it sometimes takes a day or two actually to be deducted.

Balance enquiries and access to account information

Bank customers will need to check the balance of their bank current accounts frequently, because this will help them to plan and manage their money.

The main methods of doing so include using:

- bank statements;
- ATM balance enquiries;
- online banking; and
- telephone banking.

Bank statements

Bank statements list all of the transactions that put money into and take money out of a bank account. The types of transaction that appear on a statement depend on the type of bank account to which it refers – for example, a current account or a savings account.

The account holder should check their bank statement to make sure that they agree with all of the transactions that it lists – that is, payments into and out of the account – and report any discrepancies to the bank. The statement can also help the account holder to budget for the days and weeks ahead. By looking at the balance at the end of the statement (not forgetting to take account of any transactions into or out of the account that are not yet showing) and deducting enough to cover any bills that they may still have to pay, the account holder can work out how much they have left to spend.

Some account holders arrange for an overdraft on their account. This is where the account holder can spend more than the amount that they actually have in their account – borrowing temporarily from the bank. If, for example, an account holder has only £100 of their own money in their account, but they have a £500 overdraft facility, they can actually spend up to £600. They have to pay interest on the overdraft while they owe this money to the bank and it is a very expensive way of borrowing money, but it is useful if the person needs to make an essential purchase before they get paid.

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ATM balance enquiries

Bank statements are usually issued only once a month (or even less frequently than that if you do not have many transactions), but you can get a balance enquiry from an ATM at any time, which will give you a more up-to-date balance. Also, you can get the ATM to print out a 'mini-statement' showing the last few entries on your account.

Online banking

Provided that you have access to a computer, this is the easiest way of looking at your balance and the items that have gone through your account. Some banks make online banking easy through mobile phones.

When using online banking, account holders have to input their user name and password or security information. Some banks also issue account holders with a device that looks a bit like a calculator, which is used to produce a unique number for each online transaction. The account holder inputs their PIN into the device, which then produces the unique number, which the account holder must then input on-screen before completing the transaction. This ensures that even if a fraudster were to find out a person's user name and security information, they would not be able to carry out online transactions without also being in possession of the device and knowing the PIN for it.

Telephone banking

If you phone your telephone bank, you will be asked to give some security information; you will then hear your balance and the computerised voice will tell you the last five entries on your account. You can also talk to an operator.

Some banks will also send you a text if money comes into your account or if your balance has fallen below a figure that you have pre-programmed.

Mobile banking – phone banking apps

Mobile banking is a system that allows customers to conduct banking transactions using a mobile device, such as a mobile phone or tablet. Until around 2010, mobile banking services were performed via SMS, but advances in technology and the widespread use of smart phones and tablets have led to the increasing use of apps. These are covered in more detail in Unit 2 (MMS).

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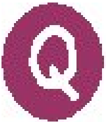
Special signing arrangements for bank accounts

When you open a current account, the bank will ask for a specimen of your signature. This specimen will be compared with any other items that you sign at a later date to ensure that it is the account holder who is giving the instructions.

Joint accounts



Can you think of times when the finances of two people might be closely linked?

Joint current accounts are simple to set up with any bank. All of the people who want to open the account together have to provide suitable evidence of identity to prove to the bank who they are. This is a legal requirement. We call the people who are part of a joint account the 'parties'.

The main decision that the parties have to make is how many people need to sign instructions such as direct debits or cheques. They might agree that any *one* of them can sign these instructions, or that *both* of them must sign (or *all* of them if there are more than two account holders). It could be that if four people have a joint account, any two of them can sign to make decisions about the money in the account.

Activity 4f

You are going to open a joint account with a friend, with whom you share a flat. The account is to be used to pay shared household bills. You will each put an equal amount in the account each month.

a) What would be an advantage of only one person being able to sign instructions?

b) What would be an advantage of both parties signing?

The British Bankers' Association suggests:

It can sometimes be convenient for more than one person to be able to sign cheques alone to pay, for instance, household bills. An example of this would be where one of the joint account holders is away from home for extended periods of time. In this case you would need to instruct your bank to accept the signature of any one account holder alone.

It can also be useful to ensure that funds are only paid from the account provided both or all account holders have signed the instructions to the bank. In this case you would need to tell your bank that it could only accept instructions to pay money away (including cheques) if all the account holders have signed.

The most convenient way in which to operate a joint account is to require only one signature. This means that both parties can have a debit card, and use this for payments and ATM withdrawals. Imagine how difficult it would be do the week's shopping if both parties were always to have to be at the shop to put their own PIN into the debit card machine? It would be almost impossible to arrange and it is for this reason that many banks ask for joint accounts to be managed on one signature only.

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In its leaflet called 'Keeping you informed', NatWest said:

With an 'either to sign' joint account, both account holders:

- have full access to funds
- can set up an arranged or unarranged overdraft without the other party's consent
- are responsible for the whole debt, even if they did not agree to it.

If one account holder dies, an 'either to sign' account can usually continue to be operated as normal by the remaining account holder.

In some circumstances, it may be necessary to freeze a joint account, for example:

- where we receive a request to convert the joint account to a sole account without both parties' agreement
- where we receive notification of bankruptcy of any party to the joint account
- where we know of a dispute between account holders
- if we are informed that the relationship between the parties has ended.

Activity 4g

Discuss and try to explain what NatWest means by the following.

a) ***'Full access to funds'***

b) ***'Are responsible for the whole debt even if they did not agree to it'***

c) ***'Freeze a joint account'***

d) ***'Dispute between account holders'***

e) ***Why do you think NatWest would want to freeze the account in this case?***

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The joint account mandate

A mandate is an instruction given to a bank. To open a joint account, all of the parties must sign a mandate, which gives the bank clear instructions about the number of people who can sign.

Joint and several liability

'Joint and several liability' is a legal way of saying that all parties are liable for the whole debt on a joint account even if they did not agree to it. Joint and several liability is included in every joint account mandate.

Case study

Alex and Sandra set up a joint account to pay bills on their rental flat. They each put in £100 a month. After a year, Sandra decides to travel to Australia and leaves the flat.

The next month, Alex receives a bank statement for the joint account, showing an overdraft of £1,200. It also shows that Sandra drew out this money at an ATM.

Horrified, Alex goes to see his bank – but is informed that he will have to pay back the £1,200 himself.

Each party to an account is liable for the full amount of any debt.

Power of attorney

Sometimes, a person may not be able to look after their own affairs themselves and will appoint an 'attorney' to have control over their finances. An attorney can be appointed only by someone who has full mental capacity at the time that the forms are signed.

There are two types of power of attorney, as follows.

- An attorney is appointed for a fixed period of time.

Case study

Jackie owns four flats and plans to be abroad for six months. She will appoint an attorney to manage the flats and to sign any necessary documents while she is away.

- An attorney is appointed who will look after a person's finances at some time in the future should that person become sick or mentally incapacitated. Known as a 'lasting power of attorney', this type has to be registered before it takes effect.

Case study

Craig is worried what might happen if, when he gets old, he cannot make sensible financial decisions for himself. He decides to give power of attorney to Alison, his niece. Because she is very knowledgeable about money, Craig is confident that Alison will make good financial decisions for him if he is too old or too unwell to make them for himself.

When (several years later) Alison thinks that Craig is unable to look after his finances, she can register the lasting power of attorney and then she can look after Craig's affairs.

Lasting powers of attorney are very useful for anyone who is worried that they may become mentally incapable through illness, an accident or old age.

People can use a solicitor to set up a lasting power of attorney, or they can fill in a form available online from the Office of the Public Guardian (via the Ministry of Justice at www.justice.gov.uk/about/opg.htm).

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Review questions

1. List the features of a current account.

2. Why do you think a current account is sometimes called a 'transactions account'?

3. For what is a mortgage used?

4. How long is the typical repayment period for a mortgage?

5. What is 'AER'?

6. What is 'APR'?

7. What is 'EAR'?

8. What sort of person is likely to want the following types of product?
   a) An offset mortgage
   b) A packaged current account
   c) A loan account
   d) A personal loan

9. How can someone give another person the authority to look after their finances while they are still alive?

10. Mark is 15 years old. He has £100 that he was given on his birthday. He wants to put the money into a bank or building society account to keep it safe and to earn interest. He is unsure when he will be spending the money.

    Mark visits some banks and building societies to find out what they offer.

ABC Bank Limited	• Offers a savings account with an AER of 2.55%. • Mark can take his money out of the account whenever he likes. • He can open the savings account with £1. • The bank will give Mark a free mouse mat when he opens the account.
Big Bank Limited	• Offers a savings account with an AER of 2.75%. • Mark must give three months' notice if he wants to take his money out of the account. • He can open the account with £10. • The bank will give Mark a free music CD when he opens the account.
Local Building Society	• Offers a savings account with an AER of 3.01%. • Mark can take his money out of the account whenever he likes. • He can open the account with £1. • The building society does not offer free gifts.

Country Building Society	• Offers a savings account with an AER of 2.75%. • Mark can take his money out of the account whenever he likes. • He can open the account with £1. • The building society will give Mark a free 'Savers' ringbinder when he opens the account into which he can put his statements when he receives them.

Which account should Mark open if he:

a) wants to earn the most interest?

b) wants to take his money out with no notice?

c) wants the best free gift?

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Learning activities

Internet

- Visit www.ukpayments.org.uk and look at the icons on the homepage. Find out about the mobile payments system that was launched in 2014. What is it called? What types of payment does it process?
- Visit www.chequeandcredit.co.uk and, under 'Cheque users', click on 'The cheque clearing cycle'. Look at the animations and the text, which tell you more about cheque clearing.
- Visit http://www.rbs.co.uk/personal/mortgages/g1/offset-flexible.ashx and see about how a borrower can pay off their mortgage early using this product. Visit https://www.bba.org.uk/publication/leaflets/you-and-your-joint-account/ and download the PDF file called 'Joint Account'. Read the FAQs.

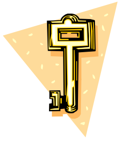
Group

- Visit the websites of three banks and two building societies. Look up the interest rates for an interest-rate tracker mortgage for 25 years.
- Use the mortgage calculator that is to be found on all of these websites. Find out how much it would cost each month to repay a mortgage of £150,000 borrowed over 25 years.
- Discuss why every website carries a warning saying: 'Your home may be repossessed if you do not keep up repayments on your mortgage.'

Individual

Visit www.moneysupermarket.com and look under 'Money' at the savings section.

- If you were to have £50,000 to invest over the next three years, which bank and which account would you choose?
- Would there be any penalties if you were to need to withdraw £2,500 after the first year?
- If you were to have £5,000 to save for only one year and want an account that paid tax-free interest, which one would you choose this time?



Key points for Topic 4

You should now understand:

- ❑ what a 'current account' is, and be able to list and explain all of the methods of payment available to a current account holder;
- ❑ what a 'joint account' is;
- ❑ the advantages and disadvantages of having a joint account;
- ❑ what a 'mandate' is;
- ❑ the problems of joint and several liability;
- ❑ what a 'lasting power of attorney' is;
- ❑ methods of getting information about the balance of your account;
- ❑ what a 'bank statement' is, and the meaning of the words 'debit' and 'credit';
- ❑ what a 'paying-in slip' is and be able to list the main parts;
- ❑ what a 'cheque' is and the main features of a cheque;
- ❑ the 2–4–6 clearing cycle;
- ❑ types of bank account, including savings accounts, loan accounts, mortgage accounts, offset accounts, packaged current accounts and extra feature accounts;
- ❑ the advantages and disadvantages of these types of account, so that you can make comparisons;
- ❑ the features of debit cards and cash cards.

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