CHAPTER 2

Current Accounts as a Tool for Bank and Customer Relationships Management

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SUMMARY: 2.1. Definition and Operational Characteristics. – 2.2. Economic Profile. – 2.3. Financial Profile. – 2.4. The Functioning of Current Accounts and Convenience Evaluation. – References.

2.1. *Definition and Operational Characteristics*

The bank current account is a contract by which the bank carries out a treasury service where it manages the collection of money and payments on behalf of the customer, using the customer's own funds or funds made available by the bank [1]. As this treasury service can only be carried out whether funds are available, the current account must be accompanied by a deposit (see paragraph 5.3) where the funds belong to the customer, or by an overdraft facility (see paragraph 4.2.2) where the bank has made funds available after granting a credit (see Chapter 3).

Bank current accounts are regulated by the Civil Code concerning banking transactions in current accounts (article 1852 and subsequent articles) and the associated Uniform banking regulations [2]. Furthermore, this contract is subject to transparency regulations (see Chapter 1).

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[1] This contract is different to an ordinary current account (regulated by the Italian Civil Code, article 1823 and subsequent articles) as it can only work per instructions given by the customer to the bank, and the balance is available and collectable in any moment, not only at the moment of closing the account.

[2] Uniform banking regulations are general contract conditions issued by the Italian Banking Association (ABI) with the aim of integrating and amending laws on banking transactions and services. It also aims at providing standard forms of contracts to regulate and standardize relations between banks and customers. These rules are not binding for its member banks, which can decide to use them if they wish or to modify them as they see fit (Bank of Italy Provision n. 12 of 3 December 1994).

From an operational point of view, a bank current account can be analysed taking into consideration:

– the ways of opening and closing the account; and,
– the documents that the bank must regularly send to customers informing them of any transactions, balances and costs regarding the account (interest, fees and any other expense).

The process of opening a current account includes:

– establishing which economic conditions to apply such as interest rates, value dates, fees and other expenses;
– producing by the customer the necessary documents to start the procedure with the bank. The documents needed will depend on the type of client which can be private, sole proprietorships or larger businesses. These are, in general, the customer's identification documents [3] and, in the case of a company, credentials documents;
– signing the contract and other documents (proxies, authorization forms to carry out specific transactions, signature specimen forms [4], etc.);
– attributing a current account number, which must abide by the definition of an IBAN (*International Bank Account Number* [5]); and,
– where appropriate, giving the customer a cheque book in the event of an initial deposit into that account or granting a credit.

Choosing the type of registration for the account is particularly important at this stage. The account can be registered:

– to one person: only the individual named on the account is authorized to carry out withdrawals and payments in this case; or
– to two or more people: if the account is registered with joint signatures (an "and" joint account), the signatures of all named individuals are needed to make withdrawals from the account; if the joint account is opened with separate signatures (an "or" joint account), each signatory is able to carry out all transactions with no limits.

When closing the current account, the client can withdraw from the contract without being charged a fee (article 120-*bis* of the Consolidated Law on Bank-

[3] The bank must verify the identity of those opening a current account (*duty of due diligence*) as provided for by article 17 of lgs.d. n. 231/ 2007, which implements the European Directives on Money Laundering.

[4] This document contains the signatures of individuals authorized to carry out transactions in the current account, thus allowing the bank to compare these signatures with those on cheques or any other signed document in order to verify its authenticity. The process of collecting a signature specimen can also take place via an electronic signature.

[5] These are international bank account numbers that allow an individual or a bank to identify the recipient of a bank transfer (see paragraph 6.4.2).

ing). It is also possible for customers to transfer all payment services to a current account in a different bank without any fees due (*account portability*) (see paragraph 6.2.1).

The account statement and the *interest account* are the informative documents that allow clients to track their current account. The account statement is a list of all transactions across a set period and recorded in the bank accounts. The sum of the transactions and costs constitutes the *account balance* at the end of the period. The interest account lists all transactions in relation to the value date and is used to determine the *numbers* to calculate interest (see paragraph 2.4). This balance (*value date balance*) may be different to the account balance as some transactions may have a value date after the closure date of the account statement.

2.2. *Economic profile*

The economic profile of a bank current account can be analysed by examining the main economic conditions applied by the bank. These are:

– interest rates: a debit rate is applied when the account balance goes into debt through the use of credit or of an overdraft (*overdrawn account*) [6]; a credit rate, on the other hand, may be applied when there is a credit balance on the account;

– account management fees and expenses: the bank may stipulate the payment of a variable cost related to the number and type of transactions carried out, or a fixed periodic fee (regardless of the number of transactions). For example, the *basic bank account* is a current account which has an all-inclusive annual fee that the bank must offer to consumers; this account allows a certain number of transactions and access to some payment services (article 126-*noviesdecies* and subsequent articles of the Consolidated Law on Banking) [7];

– arranged (or possible unarranged) overdraft fees: according to the Consolidated Law on Banking (article 117-*bis*), in the event of a customer using an arranged overdraft, the bank may apply an *overdraft fee* which is proportionate to the sum made available and the duration of the overdraft; it cannot be more than 0.5% of the arranged overdraft per quarter. In the event of the customer using an unarranged overdraft, the bank may instead apply a *fee for fast credit investigation*, which is expressed as absolute values [8]; and,

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[6] A current account is *overdrawn* when the balance is in debt without a credit, or it exceeds the credit arranged (*unarranged overdraft*).

[7] This initiative is aimed at facilitating access to bank services for the less wealthy population (*financial inclusion*) and to reduce the use of cash. To this end, the bank must identify clients from socially disadvantaged backgrounds and then offer them a basic account with no fees.

[8] The fee is calculated by using the available balance at the end of the day (see paragraph 2.3); if the unarranged overdraft is only on the value date balance, this fee is not applied. With

– the value dates: expressed in days, they determine a rise in interest in the event that the current account balance is in debt (see paragraph 2.3). The application of the value dates is regulated by article 120 of the Consolidated Law on Banking and article 23 of lgs.d. n. 11/2010 (see Table 2.1).

Table 2.1. – *Value dates and availability*

Payment instruments	*Value date*	*Availability*
Bank drafts issued by the same bank and bank cheques drawn on the same bank where the deposit was made	Date of deposit	Four working days
Other bank drafts	One working day	
Other bank cheques	Three working days	
Other instruments (e.g., bank transfers)	Crediting date	Crediting date

2.3. *Financial profile*

The financial profile of a bank current account can be analysed by examining the nature of the flows that define its handling. These are:

– income and expenditure and, that is, cash flows; and
– credit and debit, meaning financial flows.

These flows derive from:

– customer activities (e.g., payments from clients, payments to suppliers); and,
– transactions and services (e.g., granting and repayment of a loan, buying and selling financial instruments).

These are objective values which bring variations in customer credit and debit; the difference is that only monetary flows result in cash movements. Moreover, it must be emphasised that all flows are "cash", as they all result in a variation of the customer's purchasing power.

The flows change the current account balance and continuously show the customer's financial situation with respect to the bank. Naturally, this is a partial view of the customer's financial situation, as they can have various bank accounts both

consumer accounts, the fee for fast investigation is not applied if the unarranged overdraft is less than €500 and has a duration of no more than seven consecutive days (Interministerial Committee for Credit and Savings, Urgent Ministerial Decree – President 30 June 2012, n. 644 article 4).

in the same bank and across different banks. Furthermore, in order to determine the overall financial situation, it is necessary to consider transactions which have no effect on the balance of the current account; an example of this is the outstanding loan amount of a mortgage, which is not included in the current account balance.

Regarding the nature of flows through a current account, it can be seen that in most cases they are simple financial variations (credits and debits).

Issuing a bank cheque, for example, typically produces financial flows (a debit on the issuer's current account and a credit on the beneficiary's account); however, it is only when the cheque is collected that the bank detects a cash outflow. Bank transfers are a service by which the customer instructs the bank to pay a third party (beneficiary) on their behalf; it involves a debit on the current account of the payer and a credit on the current account of the beneficiary. Only when a customer carries out a transfer via cash deposit and/or the beneficiary withdraws the credited sum will the cash transactions be recorded.

The same situation can be found in lending and deposit transactions:

– granting a mortgage, for example, foresees an initial credit on the customer's current account and successively a series of debits to repay the capital and pay the interest, without any cash flows being recorded;

– issuing a certificate of deposit, for example, implicates an initial debit on the customer's current account; at the expiry of the certificate, the capital and accrued interest are added to the account with no cash movements.

However, to complete this analysis, it is necessary to consider that the customer's financial situation does not solely depend on the flows deriving from their business and banking transactions and services, but also on the way that costs are calculated; in this case, it consists of generally financial flows which change the balance of the current account.

The financial nature of these flows depends on the fact that interest, fees and other expenses are usually charged without determining movements of cash; these costs result in a deposit (although not necessarily of cash) only when the final balance exceeds the credit arranged and if that balance is not covered by an increase in credit. Quantifying these flows is not objective in nature, but is affected by the way the bank measures balances in current accounts in order to calculate the interest; this depends on the value date applied (see paragraph 2.4). In particular, the value dates:

– increase interest at the customer's expense, inasmuch as they increase the basis for calculation (*debit numbers*); and

– can also produce interest in absence of a debit balance; assuming a current account in which the customer periodically deposits the checks received and at the same time issues checks of the same amount, the account balances are zero, but the application of the value dates on deposits, against debits in the account with a value date corresponding to the date of issuance of checks, determines debit balances for interest calculation and the consequent calculation of interest on *value date overdrafts*.

Moreover, it can be seen that value dates are only important to measure value date balances; in particular, value dates on deposits determine the date from which the interest is calculated, without allowing the customer to use the money deposited in their current account.

In order to measure the monetary resources available to the customer, it is therefore necessary to calculate a different balance (*available balance*). To this effect, to allow the customer to know when the deposited money can be used, banks have established *availability dates* which, like value dates, are subject to specific regulations (see Table 2.1).

However, measuring an account's available balance must take into account both unavailable transactions, such as cheque deposits and other securities, as well as transactions that, while appearing on the customer's account on a future date, immediately change the account balance, for example purchasing or selling financial instruments. Furthermore, to determine the monetary resources which can be effectively spent by the customer, it is necessary to take any arranged overdraft into consideration. The relationship between account balance and available balance can be seen in Table 2.2.

Table 2.2. – *Measuring available balance*

± *Account balance*	Algebraic sum of all transactions recorded in current account.
– Unavailable transactions	e.g., deposits of cheques from other banks where the availability has not yet expired.
– Transactions carried out but charged on the account the following days	e.g., the purchase of financial instruments recorded on the settlement date, following the date of execution, or ATM withdrawals recorded after the date of execution.
+ Transactions carried out but credited to the account the following days	e.g., the sale of financial instruments recorded on the settlement date, following the date of execution.
+ Arranged overdraft	Current account credit
= *Available balance*	Customer's expendable amount

To understand the relationship between the account balance and available balance, look at data regarding a hypothetical current account. Take, for example:

– an account balance at 100;

– a cheques deposit for 50 on date x, with availability three days; and,

– the purchase of financial instruments for 80 on date x + 1, settlement in two days.

The balances vary according to what is indicated in the following table:

Date	*Account balance*	*Available balance*
x	150	100
x + 1	150	20
x + 2	150	20
x + 3	70	70

It can be seen that on date x + 3, the two balances coincide as at that date all transactions have been accounted for and availability have passed.

2.4. *The functioning of current accounts and convenience evaluation*

Consider a current account (arranged overdraft €400,000) under the following economic conditions [9]:

– an interest rate of 7%;
– a value date on cheque deposits from other branches of one working day;
– a value date on cheque deposits from other banks of two working days;
- an overdraft fee of 0.1% on arranged overdraft; and,
- a monthly fee of €8.

Transactions from the first quarter are shown in the account statement below [10]; debits are written as *withdrawals* whereas credits are written as *deposits*.

Account statement on 31 March 20XX

Date	*Value date*	*Withdrawals*	*Deposits*	*Description of the transaction*
		75,000		Opening balance
11/01	11/01	20,000		Bank transfer to...
16/01	16/01		90,000	Bank transfer from...

continues

[9] Stamp duty of €34.20 for physical individuals and €100 for other parties is also applied. If the account holder is a physical person, this tax is not applicable if the total deposits are not over €5,000.

[10] Here we assume that the bank sends out the account statement every quarter (see paragraph 1.6).

11/02	11/02		30,000	Bank transfer from...
14/02	13/02	350,000		Cheque no. ...
15/03	16/03		200,000	Cheque deposit from other branches
17/03	19/03		70,000	Cheque deposit from other banks
21/03	20/03	38,000		Bill payments
23/03	23/03	25,000		Cash withdrawal
25/03	25/03	40,000		Tax payment
29/03	31/03	100,000		Payment of the installment, loan no. ...
31/03	31/03	400		Overdraft fee
31/03	31/03	24		Other expenses
		258,424		**Closing balance**

To calculate debit interest, quarterly transactions are listed by value date in the interest account. This way, it is possible to get the daily value date balances to calculate the *numbers* (value date balances × days in debt / 100):

Interest Account

Value date	*Value date balances*	*Days in debt*	*Days in credit*	*Debit numbers*	*Credit numbers*
31/12	-75,000	11		8,250	
11/01	-20,000				
	-95,000	5		4,750	
16/01	+90,000				
	-5,000	26		1,300	
11/02	+30,000				
	25,000		2		500
13/02	-350,000				
	-325,000	31		100,750	
16/03	+200,000				
	-125,000	3		3,750	
19/03	+70,000				
	-55,000	1		550	

continued

20/03	-38,000				
	-93,000	3		2,790	
23/03	-25,000				
	-118,000	2		2,360	
25/03	-40,000				
	-158,000	6		9,480	
		88	**2**	**133,980**	**500**

Using these numbers, it is possible to calculate the debit interest[11] and other costs reported on the account statements, where:

– the debit interest = (debit numbers × interest rate) / 365;
– the overdraft fee = 0.1% on arranged overdraft; and,
– other expenses = monthly fee × no. months.

In this case, the interest account also shows a credit value date balance (two days in credit, credit numbers 500). However, interest on these is not calculated in favour of the customer as the terms and conditions of the account do not foresee a credit rate.

Calculation of costs

Debit interest	(133,980 × 7) / 365	2,569
Overdraft fee	400,000 × 0.001	400
Other expenses	8 × 3	24
Total		**2,993**

Analysing the account statement and interest account allows the customer to check the ongoing performance of their current account and the ways the bank calculates costs. This information can also be used to carry out economic assessments aimed at measuring the actual cost of the current account. These assessments are useful to analyse the effect of different economic conditions on the total cost, and to compare the cost of a current account with accounts from other banks. In this way, it is possible to identify the economic conditions which affect the total cost of each current account the most which should be focused on in case of contractual renegotiations with the bank.

[11] The debit interest is not reported on the account statement and therefore does not change the quarterly current account balance (see paragraph 1.7).

The actual cost of a current account is a rate which takes into account all applied economic conditions (interest rate, value date, overdraft fees, other expenses). These conditions have a different effect on the actual cost of the current account, where:

– the interest rate produces interest relative to the debit capital, shown by debit numbers;
– the value dates contribute to higher debit numbers and therefore a rise in interest, in relation to the total of the transactions to which they are applied and the interest rate; and,
– the overdraft fee and other expenses are fixed costs as they do not depend on the debit capital or the number of transactions carried out; their effect on the actual cost rises the smaller the debit capital.

Assuming that:

$$I = (N \times i) / 365,$$

where:

I = interest
N = debit numbers
i = nominal interest rate

it can be seen that:

$$i = (I \times 365) / N.$$

To go from a nominal interest rate to the actual cost of the current account, it is necessary:

– to consider all costs (debit interest, overdraft fee, other expenses), with regards to the numerator; and,
–to subtract the numbers adjusted given the application of the value dates from the debit numbers indicated in the interest account, with reference to the denominator; value dates, in fact, determine an increase in debit numbers which does not depend on a greater use of the arranged overdraft.

At this point, the actual cost of the current account can be calculated as follows:

$$i_e = (CO \times 365) / (N - NV),$$

where:

i_e = effective interest rate
CO = total costs
N = debit numbers
NV = numbers adjusted given the application of the value dates.

Taking the data from the example, higher debit numbers are calculated due to the application of the value dates on the deposit of the two cheques as follows:

– higher amounts on cheque deposits from other branches: 200,000 × 1 day / 100 = 2,000; and
– higher amounts on cheque deposits from other banks: 70,000 × 2 days / 100 = 1,400.

The actual cost of the current account is therefore:

$$(2{,}993 \times 365) / 130{,}580 = 8.4\%,$$

where 2,993 is the total cost and 130,580 are debit numbers corrected to take into account the value dates (133,980 – 2,000 – 1,400).

Once the actual cost of the current account has been determined, it is possible to analyse its composition measuring the effect of each economic condition on the total cost.

The effect of value dates is expressed using the difference between the recalculated rate, which takes into account the higher debit numbers deriving from the application of the value dates and interest rate. The first is measured by simply stating the interest as the numerator of the following formula for the actual cost:

$$i = (I \times 365) / (N - NV).$$

Consider the example:

$$(2{,}569 \times 365) / 130{,}580 = 7.2\%$$

where the effect of value dates is 0.2% (7.2% – 7%).

The effect of value dates can also be measured in absolute terms, calculating the interest that comes from their application in the following manner:

$$I = (N \times i) / 365 = (3{,}400 \times 7) / 365 = 65,$$

where 3,400 (2,000 + 1,400) are the higher debit numbers deriving from the application of value dates. This means that, if there is no value date on cheque deposits, the interest that the customer should pay is 2,504 (2,569 – 65).

The effect of the other economic conditions is calculated using the formula for actual cost, stating the related absolute value as the numerator. Here:

– overdraft fee: (400 × 365) / 130,580 = 1.1%
– other expenses: (24 × 365) / 130,580 = 0.1%.

The actual cost of a current account is summarized as follows:

Interest rate	7.0%
Value dates on cheque deposits	0.2%

Overdraft fee	1.1%
Other expenses	0.1%
Actual cost	**8.4%**

In conclusion, the actual cost of a current account is higher than the nominal interest rate as other economic conditions are applied by the bank such as the value dates, the overdraft fee and other expenses.

Finally, it can be seen that the actual cost is calculated *ex post* as it depends on both the previously agreed upon economic conditions and the number and type of transactions carried out; these determine the account handling and influence the overall effect of the value dates.

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