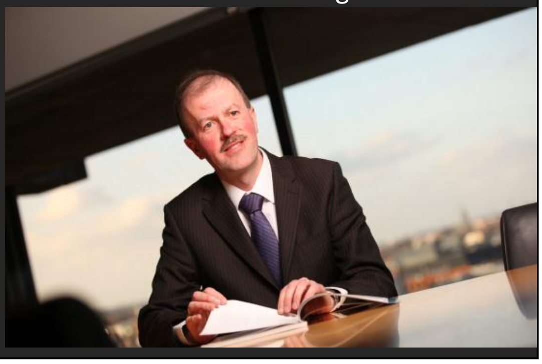
Issue 1 | February 2014

Welcome to the FinCoNet Newsletter

Welcome to the first edition of our newsletter. The purpose of this newsletter is to help share best practice and effective approaches across our members and also act as a channel of communications on current topics. We would encourage all members to contribute to future newsletters and to provide any feedback to us.

Chair

Bernard Sheridan
Chair of the Governing Council



FinCoNet: Advancing the Financial Consumer Protection Agenda

Please click on the link to view an article published in the January edition of the International Banker, on the establishment and background to the International Financial Consumer Protection Organisation.

http://internationalbanker.com/banking/finconet-advancing-financial-consumer-protection-agenda/

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In Focus: Banking and Credit

Secured Credit	**Code of Conduct on Mortgage Arrears** The Central Bank of Ireland published a revised Code of Conduct on Mortgage Arrears in 2013, which sets out rules for lenders when dealing with borrowers who are in arrears with their mortgage payments. An Industry Letter issued subsequently outlining transitional arrangement and required implementation of the Code. To accompany the Code, a guide for consumers has also been published here:
Un-Secured Credit	**Research on the Licensed Moneylending Industry in Ireland** The Central Bank of Ireland published a report on the licensed moneylending industry in Ireland in November 2013, which was undertaken to inform the regulatory approach to the licensed moneylending industry and to see how the firms are treating their customers.
Payment Issues	In December 2013, the **Financial Consumer Agency of Canada** released a research paper, Mobile Payments and Consumer Protection in Canada, which examines risks associated with the emergence of this new payment method and assesses the extent to which financial consumers in Canada are protected when making mobile payments.
Credit and Mortgage Intermediaries	The Central Bank of Ireland's newsletter for Retail Intermediaries recently issued a special edition providing details of our recent themed inspection on the financial position of retail intermediaries. Intermediary Times

In Focus: Other Areas of Interest

Information request on Business Lending to Small and Medium Enterprises

In Ireland, the Code of Conduct for Business Lending to Small and Medium Enterprises (SME Code) applies to business lending by regulated entities, excluding credit unions, to small and medium enterprises (SMEs).

The objectives of the SME Code are:

- to facilitate access to credit for sustainable and productive business propositions,
- to promote fairness and transparency in the treatment of SMEs by regulated entities, and
- to ensure that when dealing with financial difficulties cases, the aim of a regulated entity will be to assist borrowers to meet their obligations, or otherwise deal with the situation in an orderly and appropriate manner.

The SME Code applies to regulated entities when providing the following credit products within the State to SMEs operating within the State: overdrafts, loans, term loans, leasing, hire purchase, and invoice discounting.

A review of the SME Code will be undertaken during 2014. In advance of that review, we are seeking information on requirements relating to business lending to SMEs in other jurisdictions. In particular, we are seeking information relating to:

- the type of issues arising in relation to lending to SMEs in that jurisdiction; and
- any requirements that jurisdiction has imposed on lenders in relation to:
  - access to credit;
  - provision of information to SMEs;
  - withdrawing or declining credit;
  - dealing with financial difficulties.

Please send responses to finconet@centralbank.ie

Information request on class action law suits taken by consumer organisations against banks

A Central American Non-Member Country has made contact with FinCoNet reporting on recent rulings in their country in favour of consumer organisations taking class action law suits against banks even without individual claims.

They are requesting FinCoNet members to share their experiences in relation to class action cases by consumer organisations against Banks. They are particularly interested in current or existing class action type cases against banks by consumer organisations, claiming lack of information for consumers; alleged unfair terms in contracts or in interest rates; the extent of the damage caused to banks or the general financial system due to such claims or lawsuits.

Responses can be sent to finconet@centralbank.ie for onward transmission.

Current Issues Forum

New rules proposed on payment services to benefit consumers and retailers

Philippe Pellé, European Commission

On 24 July 2013, the European Commission adopted a proposal for a legislative package on retail payments which will further improve and modernise the European legal framework for payments and which will bring more competition in the card payments market.

Together with the SEPA Regulations, the current Payment Services Directive of 2007 has brought substantial benefits to the European market for payments. It has facilitated the entry of new actors (so-called payment institutions), allowing for more competition and better choice for consumers and retailers in payment solutions. The Directive also has achieved that payments are much more quickly executed and that there is much more transparency on the conditions and fees for making use of payment services.

However, since 2007, the landscape of electronic payments has changed considerably. Now almost every account holder in the European Union possesses a debit card and 40% also own a credit card. Around 34% of the citizens shop on internet and e-commerce is growing exponentially. 50% of the citizens also own a smart-phone which allows for making mobile payments. New players have found their way to the online payments market, allowing consumers to pay for their online purchases without the use of a credit card, by conducting a simple online credit transfer through his bank to the bank of the retailer.

One of the main innovations of the proposed package is to expand the scope of the Payment Service Directive to also include the third party payment service providers and make them subject to the same rights and obligations as the incumbent players. Furthermore the obligation for payment service providers regarding information on payment services will be expanded to international payment transactions, where only one of the payment service providers is located in the European Union. This will very much benefit consumers that make use of remittance services for sending money abroad or paying in non-EU currency.

Consumers will also be better protected by providing them with an unconditional refund right even in case of disputed payments. Furthermore, consumers in principle can only be held liable in case of a payment incident up to maximum 50 euro (versus 150 euro currently). Equally important, the security for online payments will be increased substantially. Consumers only feel comfortable to make payments through Internet, if they are confident that these payments are safe and secure. The current security measures already guarantee a good level of security, but further improvements are needed to make the security of payments also future proof. Payment service providers will be obliged to apply strong customer authentication to severely limit the risk against fraud and other possible abuses. The overall security requirements for payment service providers will be considerably improved.

The payment package also includes a proposal for a new Regulation to regulate the interchange fees for card-based payments with flanking measures to combat anti-competitive practices in this field. Interchange fees are fees that are applied in card schemes which operate through banks, such as Visa and MasterCard. For each card payment, the retailer's bank must pay an interchange fee to the consumer banks (or card issuing bank). The proposal puts a cap on these interchange fees for transactions on consumer debit and credit cards and bans possible extra charges that retailers may impose on consumers when paying with these cards. These caps would apply immediately for cross-border transactions. A transitional period of 22 months after adoption is foreseen for domestic transactions.

Changes to the UK Consumer Credit Regime

Karen Northey, Manager, International Department, Financial Conduct Authority

At the UK Financial Conduct Authority (FCA), we expect to double the number of firms we regulate when we take over responsibility for consumer credit regulation in April this year.

The move is part of the UK's continuing reform of financial regulation. Last year saw the creation of the FCA and the Prudential Regulation Authority (PRA), a subsidiary of the Bank of England.

Around 35,000 new firms will fall under our oversight for the first time. Many are specialist credit lenders or brokers, or others who offer credit services, like debt collection or debt advice. But we will also be responsible for small businesses offering credit alongside other goods they sell, such as furniture or electrical retailers. Added to these are the credit activities of around 15,000 firms that we already regulate in other areas – such as banks' personal loan and credit card lending.

The change will mean that the UK will have only one regulator for consumer-facing financial services, and will be a huge change for the credit industry and the FCA. It is probably the biggest challenge that we face as a regulator.

We are progressing well with the preparations to get ready – from training our staff, to updating our IT systems. In the past year we have been doing new things – such as our first direct marketing and advertising campaign to try and reach the thousands of small businesses who have low awareness of the changes and the action they need to take.

The consumer credit market in the UK is large, complex, and important to the UK – with 176 billion pounds (213 billion euros) lent in 2011/12. People will always need credit – so our simple goal is for the consumer credit market to work well for the people that use it. Consumers should be able to get products and services that meet their needs, from firms they can trust.

We have been clear that meeting this objective will be done through a proportionate approach that recognises the important role that credit plays to our economy.

In February 2014 we will finalise the policy changes that support our regime, following two consultation papers last year, that set the way we will bring consumer credit firms into our regulatory system.

Our regime will build on what the current regulator the Office of Fair Trading (OFT) has in place, combining the existing protections with the FCA's high-level rules, like treating customers fairly, and being clear, fair and not misleading.

We have highlighted two key areas where we have proposed significant policy changes. In high-cost short term credit lending (known in the UK as payday lending) and debt management we think there are gaps in the existing protections and so we have set out new rules.

Payday lending has hit the headlines in the UK in the past few years as reduced household income has combined with a contraction in lending by banks to offer high-cost short term lenders increased demand for their products among people on lower incomes.

Politicians and consumer rights advocates have highlighted the high costs and harmful practices of some lenders. The OFT in its own compliance review has found widespread failings and the UK Competition Commission has begun its own investigation.

We agree that conduct needs to improve, and have put the spotlight on payday lending because we must take action to help those consumers most at risk, where too many get loans they can never afford to repay.

These loans are often used by people in financial difficulty, so we are proposing to apply tighter rules than before to make sure payday lenders treat their customers fairly.

When customers do not pay off their loans, it is common for payday lenders to refinance, or 'roll them over', to the following month. This is a simple process that can be useful to customers, as it means they will not default on the loan, or incur additional charges and their credit score will not be affected.

However, if lenders use it too much, it can mean that the cost of interest on the loan accumulates. Sometimes charges can be higher than the original loan. A number of rollovers may indicate that a customer is in financial difficulty, rather than experiencing a temporary change in circumstances.

To protect consumers, we want to stop payday loans spiralling endlessly by capping the number of times each loan can be rolled over to two. For consumers in this position, lenders will also have to give them information about where they can find free debt advice.

Many lenders do not have the incentive to carry out proper affordability assessments because they have unrestricted access to borrowers' accounts through 'continuous payment authorities' (CPAs). A CPA allows a lender to take a series of payments from a customer's bank account without the customer having to authorise it every time.

Typical problems with these include firms trying to take payments unexpectedly, or repeatedly trying to take payments when the customer has already explained that they do not have the money.

We propose restricting the use of this kind of payment. Lenders will only be able to make two unsuccessful attempts, and will only be able to take the full payment, rather than attempt lots of small payments. We believe that this allows customers some flexibility, while giving them more control to manage their way out of financial difficulty.

Advertising often makes borrowing look easy. We propose applying a clear risk warning for payday loan adverts, highlighting the potential risks of taking out a loan to consumers, and directing consumers to free, independent debt advice. This warning could help those consumers who are not aware of the costs of not paying back a loan on time.

In addition, the UK Government has recently asked us to introduce a limit on the total cost for high-cost short term credit, and we will follow a separate consultation process to work out how this should apply.

Debt advice is another high-risk area, where the work of the OFT and others has found that consumers need increased protection.

We are introducing new requirements for firms to have minimum capital and more detailed rules for firms that hold client money. We also propose rules that signpost potential customers to free debt advice and spread set-up costs so that they start paying off their debts as soon as possible.

Added to this will be robust scrutiny of all firms when they apply to be authorised by us. Our authorisation process is a gateway that firms must pass through to enter the financial markets. By guarding this gateway, we will check that a firm meets the standards required and conducts itself in a way that puts consumers at the heart of its business.

Consumer credit firms will have to follow a similar authorisation process to other financial firms. This means they will have to comply with certain conduct standards depending on whether they pose a higher or lower risk to consumers. For example, we may check how much money a firm holds, its internal processes and controls and its management structure.

When we agree to authorise a firm, we will decide how we are going to supervise it and the intensity of our monitoring. Consumer credit firms will go through the same supervisory process as other financial services firms, with proactive supervision that aims to spot and deal with issues before they build up in to problems for consumers.

Our teams will have more contact with higher-risk firms that have a significant impact on the market. These firms will meet with a dedicated supervisor regularly and provide us with a wide range of information about their business.

Lower-risk firms that have less of an impact will be supervised in a way that is appropriate to the size of their business – so for example, they may not need to send us as much information.

We have far wider enforcement powers than the OFT, which we will use to show there are meaningful consequences for wrongdoing. When firms break our rules, we have the power to punish them in a range of ways – for example fining them, banning them from carrying out certain activities or making them do the right thing.

Our enforcement teams are already working with the OFT so that we can take action where existing rules are not being followed and where we believe that firms are continuing to harm consumers. We will also be considering how competition in consumer credit is working in the interests of consumers.

In all, we think we are on track to introduce meaningful changes that will allow UK consumers to get better outcomes from the credit market.

If you have any questions regarding the new regime, you can find information on our website http://www.fca.org.uk/firms/firm-types/consumer-credit

Banco de Portugal's mystery shopping activities

Sara Areia, Banking Conduct Supervision Department, Banco de Portugal

Banco de Portugal is the entity responsible for banking supervision in Portugal. In 2008, Banco de Portugal was given a clear and comprehensive mandate to undertake banking conduct supervision (through the Decree-Law No 1/2008 of 3 January, which amended the Legal Framework of Credit Institutions and Financial Companies ("LFCIFC")). In 2011, the Board of Banco de Portugal took the decision to create the Banking Conduct Supervision Department – separating this task from the previous Banking Supervision Department – acknowledging the importance assigned to the supervision of conduct of business in retail banking.

The strategy followed by Banco de Portugal's Banking Conduct Supervision Department is based on three pillars: rule-making, oversight and enforcement. Banco de Portugal, in the use of its regulatory powers, complements the existing legal framework with a set of specific provisions on disclosure rules and codes of conduct. However, regulation is not sufficient and needs to be complemented by adequate oversight and enforcement.

Mystery shopping initiatives play a significant role in Banco de Portugal's banking conduct oversight strategy, being a very important complement tool to other inspection activities, such as the on-site and off-site inspections.

Allowing for an effective assessment of how products and services are sold to banking customers, mystery shopping inspections are a valuable instrument for assessing compliance with the legal and regulatory framework applicable to banking activities. Mystery shopping allows evaluating the market conduct of institutions with regard to selling practices, information disclosure, duty of assistance, creditworthiness assessment, etc. But this is not the appropriate tool to assess compliance with other market conduct rules; compliance with specific contractual obligations cannot be covered. It is also worth mentioning that mystery shopping is a tool adequate for market conduct inspections but not for prudential purposes.

One important feature of Banco de Portugal's mystery shopping inspections is that these are conducted solely by dedicated staff: inspectors from the Banking Conduct Supervision Department. This is the only way to ensure these inspections are performed with adequate technical standards. In addition, this also allows these inspections to evolve from "pure mystery shopping" to a combination of mystery shopping with on-site identified inspections.

In these initiatives, Banco de Portugal's inspectors initially present themselves as customers (mystery shopping), and assess how the financial institution's staff complies with a pre-defined set of issues for each banking product or service. For this purpose, the Banking Conduct Supervision Department at Banco de Portugal developed Inspection Guides with evaluation grids containing the detailed description of each theme.

Afterwards, in case irregularities are found, Banco de Portugal's inspectors show their own credentials and require the manager of the branch where the inspection is being conducted to sign a form with the identification of every non-compliant situation or irregularity detected. This document becomes a formal instrument for the enforcement of the legal and regulatory framework, allowing Banco de Portugal to initiate administrative proceedings to impose fines and additional penalties, when applicable.

The detection of irregularities at a mystery shopping initiative is also immediately followed by a "training session" conducted by the inspectors for the staff of that financial services provider's branch.

As a result from these inspection activities conducted by Banco de Portugal, credit institutions started themselves to implement internal mystery shopping initiatives, to ensure that employees at their own branches are complying with the applicable rules.

The use of mystery shopping activities has to take into account the heavy human resources requirements involved, and the difficulty of ensuring an adequate territorial coverage. Therefore, when defining inspection activities Banco de Portugal applies a risk weighted approach and mystery shopping inspections are planned taking into consideration the potential reduction in consumer detriment.

As Banco de Portugal places great importance in accountability, the Banking Conduct Supervision Department publishes half-yearly reports on its activities. These reports describe the mystery shopping inspections performed in the period and its results.

Although not universal, mystery shopping activities remain one of the most adequate tools for the supervision of how financial institutions comply with some specific duties towards customers. In our view, the cost-benefit analysis of mystery shopping oversight is undoubtedly positive.

New rules on mortgage credit lending

A Europe-wide mortgage credit market with a high degree of consumer protection could be a reality soon

Emilie Truchet and Adrian Steiner, European Commission

The European Union's Mortgage Credit Directive (MCD)[1] will enter into force at the beginning of March 2014. Member States will have 24 months to transpose the Directive into national law. You will find below a summary of its most important provisions.

Why this legislation?

The financial crisis has had a big impact on the public. Many have lost confidence in the financial sector and irresponsible lending is now having an impact. These problems are not confined to one or two countries, and will not fade away with an upturn in the economy. As we have seen all too clearly, the effects of irresponsible lending in one country can quickly spread to others.

The Commission has been taking a close look at EU residential mortgages markets and has pinpointed the obstacles restricting the opportunities for a borrower to take a loan in another country.

Who will benefit from the Directive?

The Directive will encourage responsible lending practices.

Consumers should get better protection at the pre-contractual stage against risks associated with mortgage credits.

Lenders and credit intermediaries, who play a key role in the economy, will benefit from a framework for a Europe-wide mortgage market that will enable them to finally take full advantage of the Single Market and over 500 million consumers.

What will change?

Consumers will be better informed, so they can choose the mortgage product which best meets their needs. Lenders will have to provide them with a standardised information sheet (ESIS) which will allow them to shop around to identify the right credit. Borrowers will benefit from a guaranteed period of time before being bound by an agreement for a mortgage (through a period of reflection, a right of withdrawal, or both). The MCD will introduce Europe-wide standards for assessing the credit worthiness of mortgage applicants.

In addition, lenders and credit intermediaries will be obliged to respect high-level principles in their direct contacts with clients. This means ensuring that the way they are paid does not prevent them from taking account of the consumer's best interests or disclosing any links between the credit intermediary and the creditor.

Performance quality standards for staff will apply. That means staff will have to have the appropriate knowledge and competence in fields identified, and be obliged to provide adequate explanation at the pre-contractual stage. There will also be standards for advisory services.

Consumers will benefit from more competition through a general ban on tying practices. Tied mortgage products that have proved to be beneficial to consumers in the past (e.g. some insurance or savings products) or future products that pass an assessment will still be allowed.

The Directive will grant consumers a general right to repay their loans early, thereby benefiting from a reduction in the total remaining cost of the credit. However, Member States may decide that in such cases, creditors are entitled to fair compensation for costs directly and exclusively linked to early repayment.

Last but not least, creditors will be encouraged to apply reasonable forbearance when being confronted with consumers in serious payment difficulties.

The Directive also establishes principles for the authorisation and registration of credit intermediaries and establishes a passport regime for those intermediaries. This means that once authorised in a Member State, a credit intermediary will be allowed to provide services throughout the Single Market. This process is based on a number of conditions: credit intermediaries have to possess and keep updating to maintain an appropriate level of knowledge and skills, to hold professional indemnity insurance and to be of good repute.

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[1] *Directive on credit agreements relating to residential immovable property[1] also colloquially referred to as Mortgage Credit Directive ('MCD').*

FinCoNet Activities

1. **AGM held on 14 November in Lisbon, Portugal, hosted by the Banco de Portugal. Issues discussed included:-**
   - Bank bundling and tying clauses,
   - Distorting incentives paid to intermediaries in the credit market,
   - Regulation of and consumer safeguards in electronic banking and electronic payments.
2. **Governing Council Call 5th December 2013**
3. **Meeting with the OECD 17th December 2013**
4. **Governing Council Call 20th December 2013**
5. **Meeting with the OECD 10 February 2014**

FinCoNet - Who We Are

FinCoNet is a new international organisation of financial consumer protection supervisory authorities was formally established on 14 November 2013 at its AGM, hosted by the Central Bank of Portugal. The new organisation (to be known as FinCoNet) replaces the informal network of supervisory authorities which has existed for a number of years and builds on the work already started by that network.

The overall aim of FinCoNet is to promote sound market conduct and strong consumer protection through efficient and effective financial market conduct supervision. FinCoNet will be focusing on banking and credit consumer protection issues. FinCoNet aims to enhance the protection of consumers of financial services, strengthen consumer confidence and reduce systemic consumer risk by promoting strong and effective supervisory practices by sharing best practice and by promoting fair and transparent market practices.

FinCoNet also intends to collaborate with other international bodies and contribute to advancing the G20's financial consumer protection agenda.

Members of the Governing Council

Country	Representative	Organisation
Australia	Greg Kirk	Australian Securities and Investments Commission
Canada	Lucie M. A. Tedesco (Vice Chair)	Financial Consumer Agency Canada
China	Jiao Jinpu	People's Bank of China
Ireland	Bernard Sheridan (Chair)	Central Bank of Ireland
Japan	Kenji Okamura	Financial Services Agency
Portugal	Maria Lucia Leitão	Banco de Portugal (Central Bank of Portugal)
South Africa	Caroline da Silva	Financial Services Board
Spain	Fernando Tejada	Banco de España (Central Bank of Spain)