Issue 1 | March 2020

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Welcome to the FinCoNet newsletter

Dear FinCoNet members,

I hope this edition of the FinCoNet newsletter finds you safe and well at this difficult time. Most of us are dealing with the challenges of Covid-19, both at work and at home, and working under various constraints.

As you will have seen, in order to support information sharing between members, the OECD Secretariat has circulated a questionnaire to which FinCoNet members are invited to participate on financial consumer protection measures that jurisdictions may be implementing or considering. It is optional to do so, but obviously at this time, information sharing can be helpful to everyone. The aim is to collate responses into a table for members, for those members who agree. The Secretariat will also be in touch about a possibly organising a virtual meeting at some point as well, so watch this space.

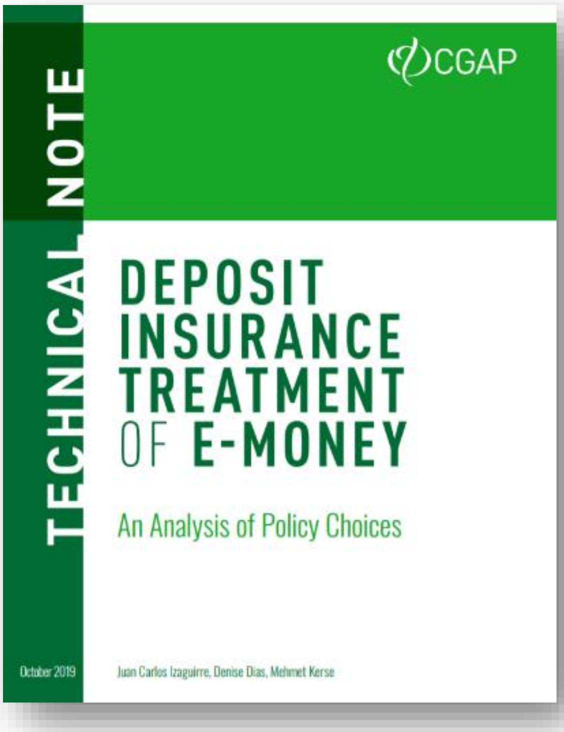
Please continue to take care of yourself, your families and your colleagues. I look forward to seeing you again soon.

Best regards

Maria Lucia Leitão,
Chair, FinCoNet

In focus

CGAP Technical Note: *Deposit Insurance Treatment of E-Money: An Analysis of Policy Choices*



The expansion of digital financial accounts among poor customers has raised the question of whether e-money should be covered by deposit insurance and if so, how. This recent Technical Note from the Consultative Group to Assist the Poor (CGAP) argues that deposit insurance should not be the first line of defence for two primary reasons: In many emerging markets where authorities have limited resources, their first area of focus should be on strong prudential regulation and supervision to ensure safe and sound institutions. Second, electronic money issuers are engaged in a narrow set of activities and in most cases pose limited or no systemic risk compared with financial institutions that intermediate deposits and issue credit.

The Technical Note can be downloaded full here.

Current issues forum

Tabular form and credit insurance withdrawal

Contributor: Bank of Russia

Terms of mortgage contracts to be presented in table format

The most important terms of mortgage-backed consumer loans, which must be approved by borrowers before they sign the agreement, will now be presented in a table format. The corresponding Bank of Russia Ordinance No. 5350-U, dated 10 December 2019, took effect on 30 January 2020.

These terms include the loan amount, due date, interest rate, methods of repayment (including free-of-charge options), paid services provided by the lender and information on whether the lender is ready to assign claims under the loan agreement to third parties.

Mortgage contract terms not listed in the table may be specified either outside the table or below it.

The table format is already used in concluding consumer loan agreements and makes it easier for borrowers to understand the main terms of the agreements they sign. This approach provides an efficient way to inform consumers and helps them to assess their risks while deciding whether to accept a loan.

This regulatory document will address all organisations engaged in mortgage consumer lending.

Credit insurance may be rejected with premium refund

Federal Law No. 483-FZ, issued on 27 December 2019 and developed with the active participation of the Bank of Russia, implies that a borrower will be entitled to receive a refund for the premium paid to the creditor for joining a group insurance programme. This insurance scheme will provide for a cooling-off period similarly to individual insurance contracts: a borrower will have the right to cancel the contract within 14 calendar days by applying in writing to be excluded from those insured. The creditor will be obliged to refund, within seven days, all money paid by the borrower for joining the programme , provided there is no insured event.

The law also reflects the Bank of Russia's suggestions on a partial refund of the insurance cost paid by the borrower in cases of early loan repayment and non-insurance. The law implies that in such cases, the insurance premium paid shall be refunded to the borrower, less the part thereof proportionate to the expired insurance period, provided there was no insured event.

In addition, a creditor will be obliged to inform the borrower about the specifics of joining a group insurance contract, withdrawing options from such a contract and amounts of the insurance premium and other payments (e.g., fees) making up the cost of this service, or about the maximum possible payment including the insurance premium and other payments. The law also takes into account credit institutions' suggestions in terms of whether a consumer loan contract and an insurance contract are interrelated.

The law stipulates that the above approaches also apply to mortgage contracts.

That said, the approved amendments preserve the approach under which a creditor is entitled to raise the interest rate on a loan when a borrower withdraws from the insurance contract.

The law will become effective on 1 September 2020 and will cover legal relations arising under insurance contracts signed after that date.

Fee disclosure through digital channels

Contributors: João E. Rodrigues, Madalena Leitão, Jorge Cunha and Filipa Alves (Bank of Portugal)

Banking fees were identified as the most relevant topic for EU consumers in the *Consumer Trends Report 2018-19*, published by the European Banking Authority.[1] Nowadays, there is an increase in the offer and customisation of banking products and services, which hampers customers' choices. At the same time, the price structures of this wider range of products and services have become more complex, increasing misunderstandings and decreasing comparability.

In Portugal since 2015, credit institutions have been obliged to provide all customers (consumers and other clients) with a free-of-charge document (the "invoice/receipt") in January of each year that identifies the fees and charges incurred in the previous calendar year for services provided through the current account.[2]

In 2019, with the implementation of the Payment Accounts Directive[3] transposed into the Portuguese legal framework by Decree-Law No 107/2017 of 30 August,[4] additional steps were taken to promote the comparability of fees linked to current accounts and other payment accounts.

The Portuguese legislator amended the rules applicable to the former invoice/receipt. Now, payment service providers shall provide the information on fees charged for services linked to current accounts and other payment accounts by means of the "statement of fees", a very similar document to the one in force since 2015. The statement of fees also includes information on interest charged and earned by customers on their current account balance.

To ensure the statement of fees provides customers with all relevant information in a way that enhances comparison and transparency, it has a standardised format and a common symbol, defined by the European Commission.[5] Where applicable, the statement of fees includes the standardised terms defined for the most representative services linked to a payment account in Portugal.[6]

With a mandate to oversee the implementation of this new legal and regulatory framework, Banco de Portugal conducted a remote inspection to assess whether credit institutions were providing

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[1] EBA *Consumer Trends Report 2018/19*, page 46. Available at: https://clientebancario.bportugal.pt/pt-pt/publicacao/eba-consumer-trends-report-20182019.

2 No 8 of the Article 77 of the Legal Framework of Credit Institutions and Financial Companies. Available at (in English): https://www.bportugal.pt/sites/default/files/anexos/legislacoes/rgicsf_en.pdf.

[3] Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014.

[4] Available in Portuguese at https://www.bportugal.pt/legislacao/decreto-lei-no-1072017-de-30-de-agosto.

[5] Commission Implementing Regulation (EU) 2018/33 of 28 September 2017.

[6] The standardised terms were published by Instruction no. 11/2018 of Banco de Portugal. Available at (in Portuguese only): https://www.bportugal.pt/sites/default/files/anexos/instrucoes/304342895_1.docx.pdf

the statement of fees to customers according to the legal and regulatory framework in force.

Banco de Portugal developed a specific and comprehensive approach for this purpose. All credit institutions were required to send copies of the statement of fees provided to a selected sample of customers. The sample was defined according to a set of requirements, such as customers' profiles (consumers and other clients); account characteristics (plain vanilla accounts and packaged accounts); inclusion of specific payment services provided to customers (payment cards, credit transfers or overdrafts) and channels used to provide the statement of fees. All credit institutions were required to prove the statement of fees had been sent to all customers.

Institutions are required to send the statement of fees to all current account holders, including dormant accounts or those where no interest or fees were charged in the preceding year. To assess whether all customers received the statement of fees, Banco de Portugal requested specific information on the number of customers who received the statement. It compared this with the data (made available by credit institutions under reporting requirements) on the number of current accounts and other payment accounts held at each specific institution.

The statement of fees must be provided to customers on paper or another durable medium. Bearing in mind that institutions provide information through digital channels (online, mobile and e-mail) on a major scale, Banco de Portugal also decided to assess how credit institutions provided their statement of fees through these channels. It requested detailed information on how customers accessed their statement of fees through digital channels by asking institutions for screen captures and copies of the statement of fees provided through digital channels.

According to Banco de Portugal's assessment, when the information on the statement of fees was provided through digital channels, it was not easily identifiable. This was the case, for instance, when the statement of fees was sent by e-mail and the subject line did not explicitly mention its content. Banco de Portugal also found that the location of the statement of fees on the app often made it very difficult to find.

Considering the importance assigned to the statement of fees in increasing disclosure and transparency, rising customer reliance on digital channels and the findings of these inspections, Banco de Portugal decided to publish a set of best practices to be observed by institutions when providing the statement of fees through digital channels and by e-mail. Those recommendations were published in a Circular Letter issued in December 2019.[7]

This Circular Letter states that institutions shall ensure that when the statement of fees is provided through digital channels or by e-mail, it will be in an easily identifiable manner. Moreover, when the document is made available by the institution, the customer must be informed through a specific notification, namely by e-mail or short text message (SMS), identifying the Internet address or the app location of the statement of fees.

Through this initiative, Banco de Portugal aims to foster technological neutrality by ensuring compliance with information requirements regardless of the channel used by credit institutions to disclose the statement of fees. This is in accordance with the mandate received from the Portuguese legislator and considers the challenges

[7] Circular Letter No. CC/2019/00000083. https://clientebancario.bportugal.pt/sites/default/files/relacionados/generica/CircularLetter83_2019.pdf

posed by the new digital ecosystem to the commercialisation of retail banking products,

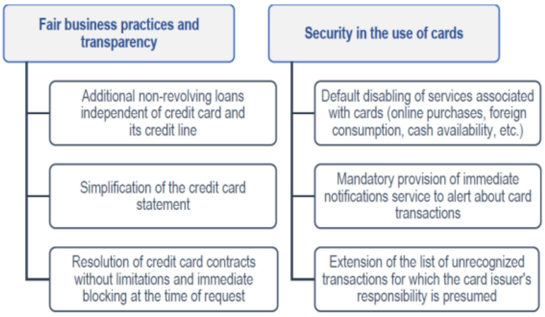
Amendment of credit and debit card regulations

Contributor: Superintendence of Banking, Insurance and Private Pension Fund Administrators (SBS-Peru)

With additional financial products and services available in the credit and debit card market, SBS has remained committed to requiring that card issuers and financial entities step up protection and security measures for their customers. In the past few years, SBS has issued several safety and protection measures for consumers, such as mandatory embedded chips in all debit and credit cards, the use of monitoring and fraud systems across all financial entities, definition of fraud liability policies for consumers, payment allocation fair practices, and electronic and physical billing options.

As part of these efforts, during 2019, SBS approved Resolution SBS No 5570-2019. It was designed to promote innovation in financial products and services and fair business practices for consumers, which would minimize potential impulse buying, reduce over-indebtedness and maximize the customer experience. To increase the transparency of the contract process, SBS required all financial entities to provide separate contracts (terms and conditions) for any additional lines of credits or loans. Also, billing information on credit card statements has become more user-friendly by keeping the necessary information to a minimum.

Main improvements in Peru's credit and debit card regulations



The new regulation also requires that banks offering additional services have the customer's consent prior to activation and the option to change or customize any of them at any given point during the length of the agreement.

Another element of the new regulation is that financial entities can no longer place limits on consumers who want to pay out their card contracts, allowing the customer to fulfill their obligations while any additional charge is pending. The card can be blocked to prevent further usage and accrual of finance charges.

Algorithm bias in credit scoring: what's inside the black box?

Contributors: Maria Fernandez Vidal, Jacobo Menajovsky, Consultative Group to Assist the Poor (CGAP)

This blog was originally published on the CGAP website.

Digital financial services (DFS) are expanding around the world, with the promise of improving financially excluded customers' access to affordable products and services. The growing use of algorithms in DFS opens opportunities as well as the possibility of unfair bias and discrimination in the treatment of customers and would-be customers.

Using artificial intelligence, regression analysis and machine learning, IT developers and financial service providers are tapping into predictive algorithms that can make decisions better and faster than humans can. The predictions of well-developed algorithms can be more accurate than those of people because of the former's ability to analyze multiple variables and the relationships between them. However, poorly developed algorithms or those based on insufficient or incomplete data can easily make worsen decision-making. Providers generally consider their algorithms to be confidential for competitive reasons, which makes it difficult to assess how the algorithms are making decisions.

(Photo: Jay Bendixen)

Regardless of the methodology used to develop them, algorithms are basically a set of rules assembled to solve a problem using a series of mathematical calculations. In financial services, algorithms are most commonly used to predict credit risk and accept or reject prospective borrowers. These algorithms can make decisions in seconds without any human interaction, so they are particularly relevant in issuing small value loans for which low operation costs are critical to profitability.

These algorithms estimate the probability that an applicant will default by comparing their current and historical data with data on borrowers who have taken similar loans in the past. An applicant is considered risky if people who share their characteristics and behaviours have paid late or defaulted.

Credit scoring algorithms are not new, but there are three reasons why it is becoming increasingly important to take a critical look at them:

1. The range of characteristics and behaviours that financial service providers can use in their algorithms is growing, thanks to the increased availability of consumer data.

2. Credit scoring models are becoming more complex and automated, and there is less human oversight of the roles that various characteristics are playing in applicants' final scores.

3. Algorithms are becoming more common in emerging markets, where there is often less regulation and oversight of what data are used and how they are used.

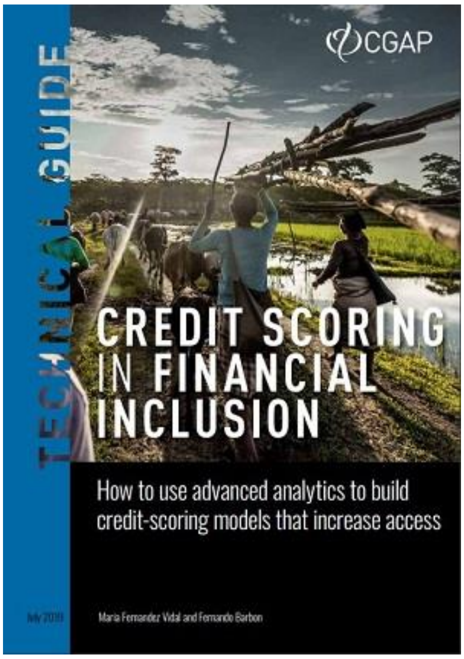
Algorithms and automation don't necessarily imply a bigger risk of discrimination than do traditional types of credit scoring. In the absence of algorithms and data-driven models, decisions on creditworthiness are made by loan officers. Consciously or unconsciously, people tend to have biased views based on the limited information at their disposal, and it's hard for a company to ensure all its employees make unbiased assessments of applicants. One of the advantages of algorithms is that they can be developed, reviewed and monitored to avoid certain forms of discrimination. For example, you can tell your employees not to consider an applicant's gender when making a loan decision, but can you be sure that they aren't exhibiting a gender bias even at an unconscious level? With an algorithm, you can simply ensure a gender variable, and closely correlated variables are not included when computing a score.

> "
> The responsible use of algorithms requires providers to know which variables are being considered in their credit scoring models and how they are affecting people's scores.

The problem is that algorithms require people to ensure their impartiality. In developed markets, where credit bureaus exist and are widely used for scoring purposes, there are norms and regulations in place that prohibit the inclusion of specific data in algorithms. The main purpose of these regulations is to avoid the risk of algorithms being unfairly biased toward certain groups of people. In the United States, for example, data on an applicant's race, ethnicity and closely correlated factors such as ZIP code cannot be used to make a credit decision.

Other markets lack such safeguards. In the absence of regulation, it is difficult for financial services providers to agree on a universally accepted answer as to what types of data should be included in credit scoring algorithms. Models can be developed in-house by financial service providers or outsourced to a developer under different types of arrangements. Either way, the provider is incentivized to maximize the predictive power of its model, regardless of what type of information the model uses to make predictions. This is especially true in cases where algorithm development is outsourced and presented to DFS providers (and ultimately their customers) as black boxes. It also holds true in countries that don't require providers to disclose the types of information used to determine an applicant's score.

CGAP recently released a [guide on credit scoring in emerging markets](), focusing on how lenders can use data analytics responsibly to develop new and better credit products.



The responsible use of algorithms requires that providers know which variables their credit scoring models consider and how the variables are affecting people's scores. Algorithms will reflect the data used to build them. For example, immigrants may have low repayment rates due to their limited access to local networks, restrictions on their business activities and other factors. If this is the case and providers are allowed to use data that identifies applicants as immigrants, the algorithm may reinforce these applicants' financial exclusion. Another example is variables pointing to stability, such as how long an applicant has been with their current employer or living at their current residence. Stability generally helps a customer achieve a better score. However, this factor may put forcibly displaced people at a disadvantage. A provider could easily correct for this by not considering time at current residence for this segment, but this would require a developer to check and adjust for the bias. In the context of developing financial markets, where regulations are limited and norms are not established, self-regulation would be a step in the right direction. Investors and supervisors can provide incentives for self-regulation by asking for information on the variables that providers are using in their algorithms and how often-excluded groups are being treated. Even in absence of clear rules, financial services providers might think twice if they have to report to their supervisor or a potential impact investor that they reject 30 percent of male applicants and 60 percent of females. Can different stakeholders in the financial inclusion space work together to identify algorithm bias and introduce fixes when certain groups are being treated unfairly? Should standards be put in place to require greater transparency among algorithm developers and to create mechanisms for understanding and monitoring biases? Let us know what you think in the comment section at the end of the original post.

FinCoNet

Established in 2013, FinCoNet is an international organisation of supervisory authorities responsible for financial consumer protection. It is a member-based organisation set up as a not-for-profit association under French law.

FinCoNet promotes sound market conduct and strong consumer protection through efficient and effective financial market conduct supervision.

Each member of FinCoNet has responsibility for and an interest in protecting the interests of consumers of financial services. FinCoNet seeks to enhance the protection of consumers, and to strengthen consumer confidence by promoting robust and effective supervisory standards and practices, and sharing best practices among supervisors. It also seeks to promote fair and transparent market practices and clear disclosure to consumers of financial services.

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