

**For information on
20 March 2003**

**LegCo Panel on Financial Affairs
Consumer Protection in the Banking Sector**

I. PURPOSE

This paper aims to update the Panel on the initiatives undertaken by the Hong Kong Monetary Authority (HKMA) and the banking industry to strengthen the self-regulation of market conduct and enhance the mechanism for handling customer complaints. The paper covers developments since the Administration last reported to the Panel in June 2002.

II. BACKGROUND

2. The Panel discussed the issue of consumer protection in the banking sector in February and June 2002. In the June meeting, the Panel noted the efforts made by the HKMA and the industry in further enhancing consumer protection in the banking sector. It was generally content with the approach in enhancing protection of bank customers by stepping up industry self-regulation. Members requested the Administration to report progress six months later in the light of developments in the trend of customer complaints.

III. PROGRESS AND DEVELOPMENTS

Code of Banking Practice Committee

3. The Code of Banking Practice Committee (CoBP Committee) has continued to respond to topical consumer issues brought to its attention by members of the Legislative Council, the Consumer Council and the HKMA. This has resulted in a number of recommendations on improving business practices in the industry.

(i) *Guarantees and third party securities*

4. At the last Panel meeting, the HKMA reported that the CoBP Committee had agreed to address the concerns raised by Panel Members regarding AIs' existing practice in relation to the "all-monies" clause in mortgage documents¹. To promote

¹ Members considered that there was a lack of choice in the market as most AIs included an "all-monies" clause in their mortgage documentation. Moreover, this practice was unfair to the guarantor whose liability could be extended, without his knowledge, to cover any additional loans granted by the AI to the borrower.

wider choice and safeguard the interest of the guarantors, the CoBP Committee has successfully added new provisions to the Code. With effect from 4 February 2003, AIs are required to offer a choice of limited or unlimited guarantee to any individual proposing to give a guarantee or third party security. Furthermore, in respect of unlimited guarantees, AIs should notify the guarantors as soon as reasonably practicable when further facilities are extended to the borrower. This ensures that the guarantor is fully aware of his liability when additional loans are granted by the AI to the borrower.

(ii) Standards of advertising tactics

5. In May 2002, the Consumer Council published a survey and criticised that some AIs had used inappropriate and misleading advertising tactics to solicit business. In response, the CoBP Committee had developed specific principles which AIs should observe in order to fully comply with the requirements of section 11.2² of the Code in relation to bank marketing. These principles require AIs to:

- make fair and reasonable comparisons in advertising materials. In particular, the comparisons should be made on a like-with-like basis and the basis of comparison should be shown clearly;
- take effective means so that prospective customers are aware of any conditions attached to the benefits (such as gifts or interest rate reductions) before they decide to purchase a product or service. Such conditions should also be displayed in the advertising materials in a clear and prominent manner and in a font size that will facilitate ease of reading;
- ensure that benefits in kind, which cannot easily be translated into pecuniary terms, should not be factored in the standard Annualised Percentage Rates of Interest for a loan product; and
- ensure that AIs' frontline staff are provided with adequate training to handle customer enquiries arising from advertised products or services.

6. These principles aim to ensure that AIs' advertising materials disclose sufficient information about the true cost of products or services, and the information presented is fair, reasonable, and not misleading.

(iii) Debt collection tactics

² Section 11.2 of the Code requires AIs to ensure that all advertising and promotional materials are fair and reasonable, do not contain misleading information and comply with all relevant legislation and rules.

7. The HKMA reported in June 2002 that there was a rapid increase in the number of complaints particularly related to misconduct by debt collection agents (DCAs). After this was brought to the CoBP Committee's attention, it promptly advised AIs to step up the monitoring of their DCAs to comply with the Code. In particular, AIs were expected to put in place an effective mechanism to monitor and prevent their DCAs from using harassment or improper tactics in debt collection, especially in cases involving a third party who has no connection with the debtor. Furthermore, the Committee was also aware that a number of complaints arose because the DCAs had failed to identify themselves and the institution for which they were acting during debt collection. The Committee has therefore provided more detailed guidance to AIs on the issue of authorization documents to DCAs by AIs. Proper identification of the DCA helps to provide the customer or complainant with a means of immediate recourse to the relevant AI in case they are subject to harassment.

First Self-Assessment on Compliance with the Code

8. The industry's enhanced efforts in self-regulation have been complemented by the HKMA's supervisory efforts in monitoring compliance with the Code. The HKMA has stepped up its monitoring role by introducing a new annual self-assessment framework in 2002. The first self-assessment report covered the initial six months of the operation of the revised Code.³

9. The self-assessment indicated that the industry's progress towards full compliance was satisfactory. The majority (90%) of AIs had achieved full, or almost full⁴, compliance with all sections of the Code.⁵ Most AIs also reported that they had adequate internal procedures and management oversight to ensure on-going compliance with the Code.

10. Notwithstanding the above, the HKMA takes seriously any instances of non-compliance and expects AIs to take prompt remedial action to rectify the problem. AIs that reported that they have not yet fully complied with the Code are required to submit an additional report to the HKMA before 31 January 2003 to rectify or account for all instances of non-compliance. Currently, there are only a small number of AIs which are yet to achieve full compliance and they have been required to set a target date to do so. The HKMA is closely monitoring individual AIs' progress.

11. AIs are required to submit the 2002-2003 self-assessment results to the HKMA in the third quarter of 2003. In line with past practice, the aggregate results will be published.

³ The revised Code took effect on 1 December 2001.

⁴ Refers to AIs which reported 5 or fewer instances of non-compliance.

⁵ There are 186 sections in the Code. To achieve compliance, AIs should satisfy two requirements in respect of each section of the Code. AIs should have (i) documents/information which comply with the section; and (ii) effective procedures in place to ensure compliance with the section. An instance of non-compliance refers to an AI's failure to comply with either one or both requirements in respect of each section of the Code.

Efforts to Tackle Increasing Customer Complaints

(i) Closer monitoring of DCA complaints

12. Given that a large proportion of complaints received by the HKMA are attributable to misconduct by DCAs, the HKMA has since March 2002 required all AIs to submit a quarterly return on the number of complaints received against the DCAs that they employ. The report covers the nature and number of complaints received and what actions the institution has taken against DCAs which have breached the Code of Banking Practice.

13. The survey is intended to contribute to the more effective supervision of AIs in respect of debt collection. For example, if an individual AI has consistently attracted a higher-than-average number of complaints, it may reflect inadequacies in their internal controls or compliance with the Code. In such cases, the HKMA has held bilateral meetings with the AI's senior management or conducted special on-site examinations on problematic areas in order to improve their procedures.

14. Where the survey revealed any complaints involving breach of the Code, the AIs were expected to take disciplinary action⁶ against the DCAs in question. 16 instances of substantiated breach of the Code were reported during the last three quarters of 2002 and disciplinary actions had been taken in all cases. Where a DCA consistently attracted higher than average number of complaints or repeatedly breached the Code, we have reminded AIs to consider whether they should terminate the relationship with the DCA. Furthermore, AIs were reminded to take extra caution in more serious areas such as complaints involving innocent third parties.

15. Since the survey was first conducted, the number of DCA complaints received by the industry has dropped to 260 in the fourth quarter from 374 in the second quarter (Annex A).

(ii) Enhanced Complaint Handling Mechanism

16. The HKMA's Guideline on Complaint Handling Procedures came into full effect in July 2002. This means that all AIs should have already put in place effective procedures for the proper handling of customer complaints. AIs should investigate and deal with complaints in a fair and thorough manner, and respond to complainants within specified time limits. Furthermore, the Guideline emphasises that AIs should ensure that their complaint handling procedures are transparent and accessible to customers. AIs are required, for example, to publish their internal complaint handling procedures in a leaflet or on their websites. They should also supply a copy of the leaflet to new customers, complainants or upon request. In

⁶ Includes the issuance of warning letter, suspension or termination of agency contract.

addition, the HKMA has uploaded contact details of AIs' complaint officers on its website for easy access.

17. To promote customer awareness of its role in handling customer complaints against AIs, the HKMA has also published a leaflet in the same month to educate customers on what to do if they have a complaint against AIs. The leaflet sets out how the HKMA will handle complaints, what its role and functions are, and the type of complaints which it cannot handle. Generally, complainants should try to resolve their disputes through AIs' internal procedures first before coming to the HKMA. The leaflet clarifies that the HKMA will normally admit a complaint if the AI fails to give a response within a reasonable period or the customer is not satisfied with the way the AI has dealt with the complaint.⁷ Since adopting this definition of a complaint, it has resulted in a decrease in the number of complaints received by the HKMA in the second half of 2002 (Annex B). The complaint statistics seem to reflect that AIs' mechanism is effective in resolving the majority of complaints. The above developments are in line with Members' expectation that AIs should provide a more formal, transparent and effective mechanism to resolve customer disputes.

Consumer Involvement

18. Regarding a proposal at the Panel's June 2002 meeting to increase public involvement in overseeing the industry self-regulation process, the HKMA believes that the current arrangement of ongoing consultation and exchange with the Consumer Council and the LegCo already provides an effective forum for public discussion on bank-related consumer issues. Further, the publication of the results of AIs' self-assessment of their compliance with the Code of Banking Practice will also facilitate market surveillance of the industry self-regulation efforts. In view of the above, the HKMA believes that there is already sufficient consumer involvement in this area.

IV. CONCLUSION

19. The HKMA believes that operation of the Code and the enhanced mechanism in dealing with customer complaints have been generally effective. AIs have also been responsive to tackling the problem at source by putting in place effective complaint handling procedures.

20. The HKMA considers that the progress made in relation to consumer protection in the banking sector under the existing statutory framework has so far been satisfactory. There does not seem to be a need for alternative arrangements for handling customer complaints which, as discussed in previous submissions, would be costly and probably require legislation of some form for implementation. Nevertheless, we will regularly review the need to strengthen the existing framework

⁷ This is in line with the practice adopted by relevant agencies in Australia and the UK.

by closely monitoring the trend in customer complaints, the level of compliance with the Code of Banking Practice, as well as developments in the market.

13 March 2003

Hong Kong Monetary Authority

Survey on debt collection agencts (DCA) complaints received by AIs - 2002*

Table 1: AIs using DCA service

	Q2/2002	Q3/2002	Q4/2002
AIs receiving DCA complaints	30	36	25
AIs receiving no DCA complaints	24	19	29
Total	54	55	54

Table 2: Number of DCAs employed by AIs

	Q2/2002	Q3/2002	Q4/2002
1 – 5	29	30	28
6 – 10	20	20	21
11 – 15	5	5	5
>15	0	0	0
Total	54	55	54

Table 3: Incidence of DCA complaints

	Q2/2002	Q3/2002	Q4/2002
DCA complaints received (A)	374	283	260
Accounts assigned (B)	196,485	193,779	193,546
Incidence of complaints per 1,000 account (C = A/B x 1,000)	1.90	1.46	1.34

Table 4: Status of complainants

	Q2/2002	Q3/2002	Q4/2002
Debtor	285	182	186
Family members/friends	72	64	57
Referees	0	5	1
Unrelated third parties	17	32	16
Total	374	283	260

* Survey began in Q2 of 2002.

Customer Complaints Received by the HKMA

(A) Number of complaints received

Nature	Q1/2002	Q2/2002	Q3/2002 [#]	Q4/2002 [#]
General complaints	229	264	83	75
Debt collection complaints	250	233	37	40
Total	479	497	120	115

(B) Analysis of Complaint Cases

i. Total Complaint Cases analysed by Generic Product Type

Generic Product Type	Q1/2002	Q2/2002	Q3/2002 [#]	Q4/2002 [#]
Current account	13	11	5	7
Savings and deposit accounts	29	32	9	8
Mortgage loans	31	35	10	12
Credit cards	266	279	42	46
Other loans and credit facilities	94	92	30	25
Remittance	4	5	2	4
Insurance products	0	5	0	2
Securities accounts	6	10	4	3
Forex accounts	4	4	2	2
Unit trust and fund investment	10	2	6	2
Stored value cards	2	0	1	0
Other	20	22	9	4
Total	479	497	120	115

[#] With effect from 1 July 2002, the HKMA will normally admit a complaint only after the customer has made use of the internal complaint procedures of the AI concerned. Therefore, the Q3 and Q4 figures are not directly comparable with those of the previous quarters.

ii. Debt collection complaints analysed by nature

Nature	Q1/2002	Q2/2002	Q3/2002[#]	Q4/2002[#]
Nuisance	169	166	26	25
Intimidation	77	56	2	11
Violence	1	5	0	0
Other debt collection malpractice *	3	6	9	4
Total	250	233	37	40

* Including chasing small or long overdue debts, levying unreasonable charges, etc.