



# Establishing a “Banking Ombudsman” in Romania

## Summary of Preliminary Findings

Draft for Consultations

Bucharest, November 30, 2006

# The Assignment

**SPI Committee has asked the Convergence Program to prepare a background study on how to set up a Banking Ombudsman (BO) in Romania:**

- to address adequately the complaints from individuals/businesses against banks,
- to improve the public image of banks,
- to protect banking customers,
- to ensure an informal out-of-court alternative

# Some Complaint Examples

- ✓ refusal to open accounts without any valid reason;
- ✓ errors/miscalculations of deposit interest rates, etc.;
- ✓ delays/inappropriate charges to money transfers;
- ✓ failure to honor guarantee/LC by banks;
- ✓ unauthorized/fraudulent withdrawals from accounts;
- ✓ lender gives confusing/unclear info to borrower about loan's interest rates;
- ✓ erroneous stop of consumers' credit cards;
- ✓ denied access to customer's funds due to errors in bank's electronic funds transfer system;

# Case Study Example

**Situation:** Mr A had debts of £4K. Lender encouraged him to take out a loan to re-finance the debt, assuring new arrangement would be to his benefit. Once new loan went through, Mr A found he was charged a very high IR.

**Client complaint:** Mr A came to O after being unsuccessful with the lender. He complained for being committed to an unaffordable repayment level.

**O resolved complaint informally:**

Mr A relied heavily on lender's advice to take the loan. IR-49%, was much higher than before. Lender gave no evidence to O on how it had arrived at this IR. When O explained to lender the serious shortcomings, it offered to write-off the debt.

# I. Analysis of Consumer Protection

**Banking sector ⇒ value to customers & contribution to Romania:**

- banking penetration  $\approx$  45% of GDP (2005)
- household loans/GDP - 7.4%,
- 25.2 mio clients (24.2 mio individuals)
- no. of cards - 7.87 mio (credit cards < 6%)

**Actual alternatives to address complaints:**

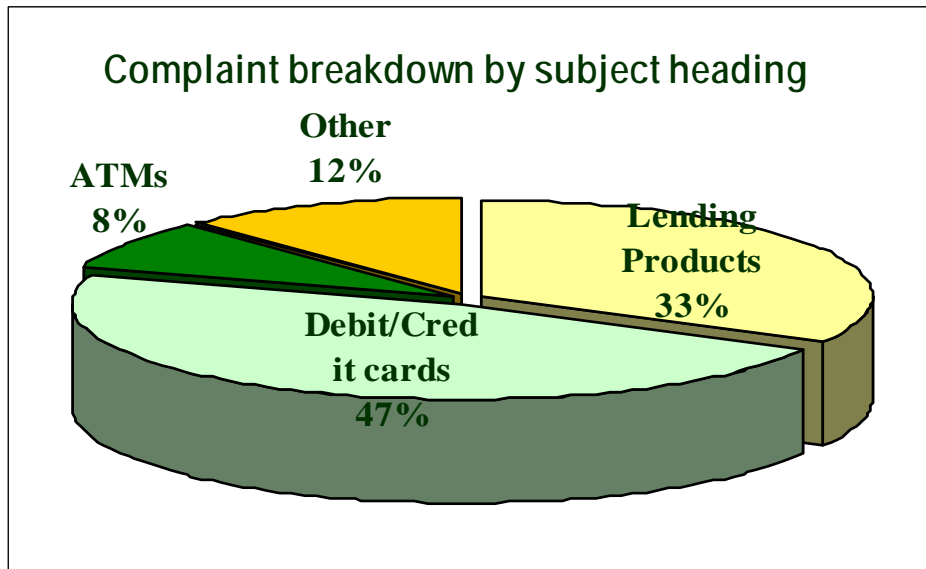
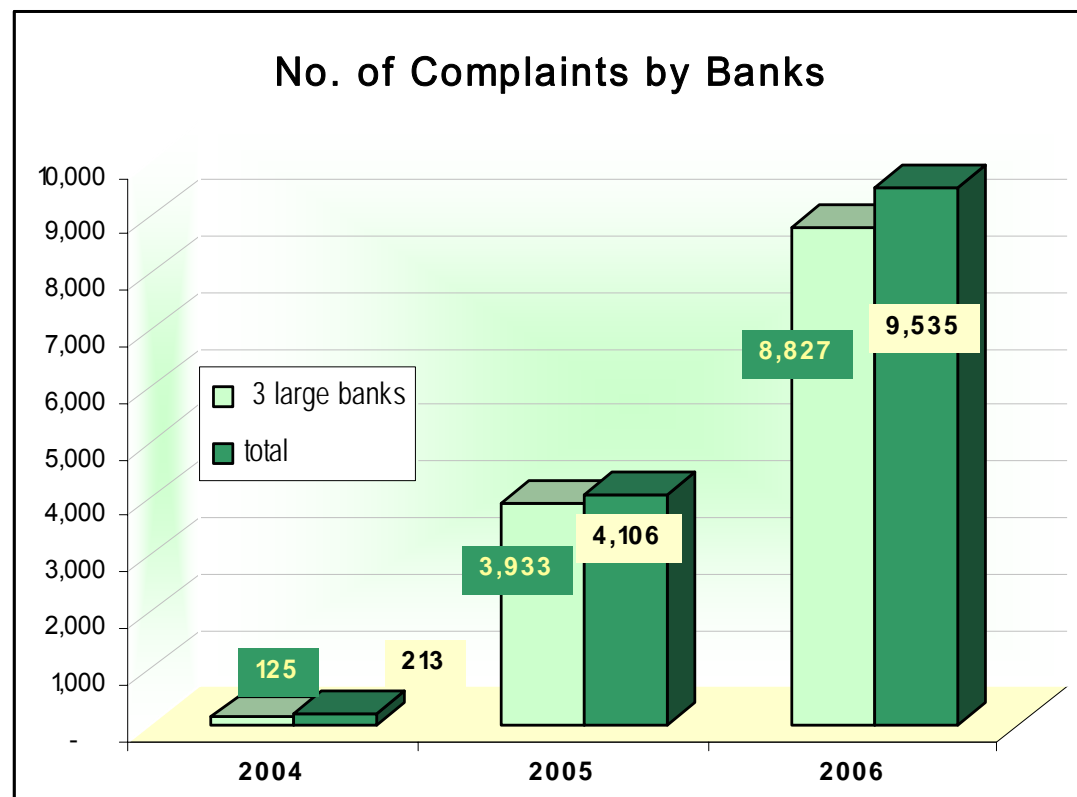
- ❑ service providers,
- ❑ cons. protection bodies/regulators
- ❑ courts

# Analysis of Survey Findings

**Survey** conducted\* from cons. & banks perspective.

- observation: flaws and deficiencies in compliant tracking systems
  - unable to respond, poor complaint collection, controversial data
- All banks have in-house settlement systems, but 42% of customers\* are aware of this!
- banks report “**effective**” systems, consumers have a “**weak**” perception!
- Banks respond to customer complaint in a week; no answer on compensation awarded!

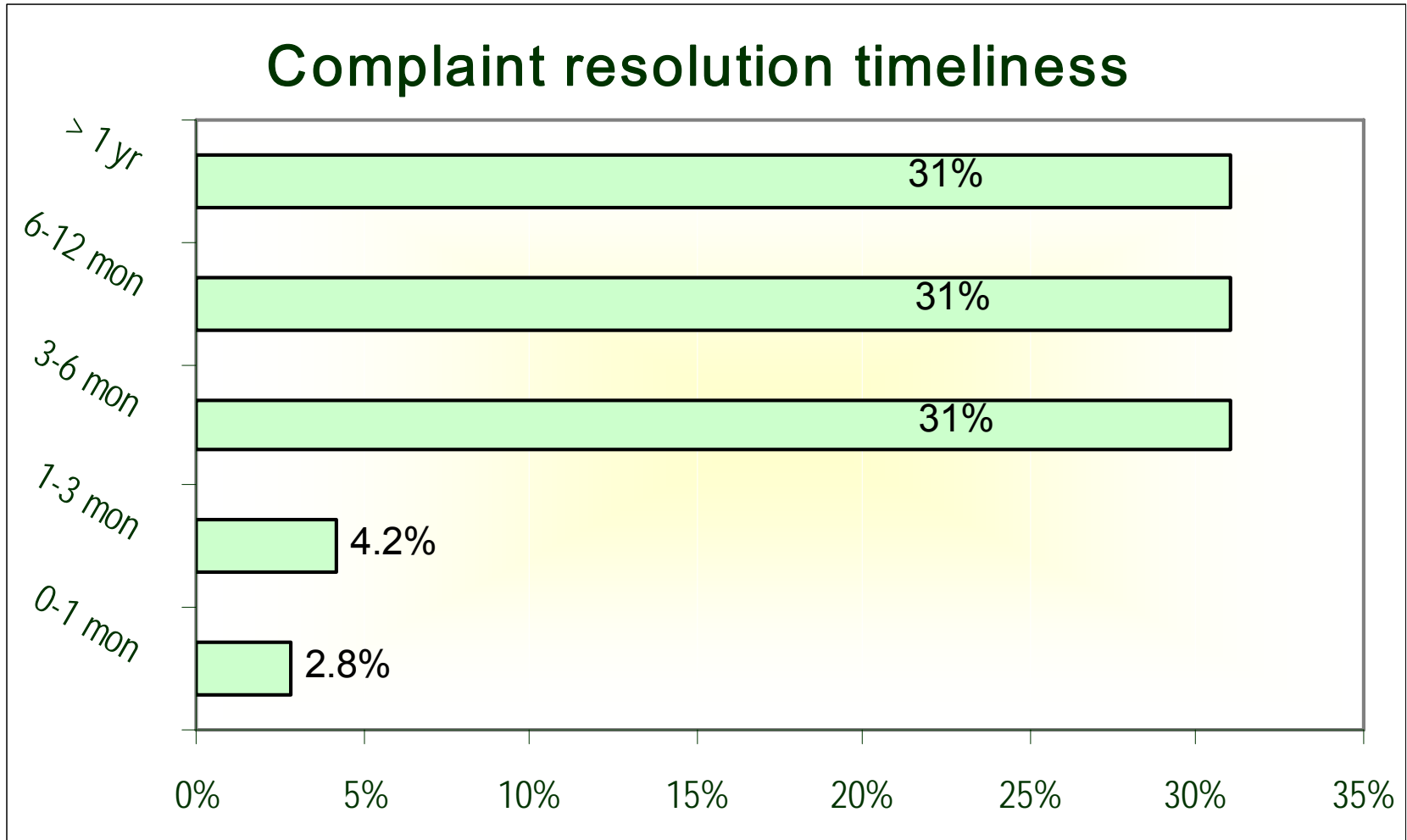
# Analysis of Survey Findings (2)



Insufficient docs by clients  
 >55%: customers' lack of banking knowledge/ info.  
 Conclusion: "consumers' education and protection is urgently required"

# Analysis of Survey Findings (3)

Consumers



# Summary of Survey Findings

- Bank's dispute resolution systems rated as partially efficient to customers as per EU standards:
  - customer's awareness,
  - system accessibility,
  - quickness to provide response,
  - fairness.
- Consumers' financial literacy is inadequate.

***Conclusion: consumer protection in banking doesn't provide proper EU standards.***

# II: BO Organization

- ❑ Governing principles
- ❑ Scheme mandate and organization
- ❑ Governance structure
- ❑ Jurisdiction: powers and duties
- ❑ Eligible complainants
- ❑ Scheme participation (rights & obligat.)
- ❑ Profile
- ❑ Procedures to complaint handling
- ❑ Operational & funding issues

# Bank Ombudsman Governing Principles

- ✓ **Objectivity & independence**
- ✓ **Accessibility**
- ✓ **Consistency**
- ✓ **Timeliness**
- ✓ **Courtesy**
- ✓ **Reasonableness, clarity & accuracy**
- ✓ **Confidentiality**
- ✓ **Quickness**
- ✓ **Informality**

## Eligible complainants

A consumer usually =:

- *an individual,*
- *a self-employed (professional),*
- *a small business.*

# Scheme Mandate & Organization

## BOs:

- Independent, out-of-court redress bodies between banks and customers\*
  - public/private;
  - statutory/non-statutory;
  - compulsory/voluntary.
- Fin-Net members.
- FOS in UK: public & statutory; part of govern.'s legislation (Act – 2000);
- statutory regulations ⇒ scheme participants legally obliged to comply;

# Scheme Mandate & Organization (2)

- **Public & statutory schemes:** Spain, GER-owned and run by CB; CAN, LUX (like UK); Czech Rep. (Fin.Arbitr elected by Parliament),
- **Private, voluntary** schemes set up by BAs, designed in industry's interest- AUT, POL...
- GER&IT: BOs not registered as legal entities, admin. functions run by BA.

# Governance Structure

- BO - separate legal entity: **By-laws** & **ToR** set out governance structure
- Public BOs: by-laws approved by authority that appoints BO's gov. body (Board). ToR approved by Board.
- Private & voluntary BOs of BA's (IT, GER, etc.), BA enacts BO's by-laws.

## **By-laws** define:

- rules governing Board meetings,
- voting rights, execution of documents
- election, power and responsibilities of officers.

# Governance Structure (2)

## **TOR/Interbank Agreement define:**

- scope of BO, i.e. issues within/outside the BO's jurisdiction, principal powers and duties of BO,
- rights & obligations of members, nature of complaint, BO complaint procedures,

## ***Fundamental functions of Board***

- A. create public confidence in the process;
- B. ensure appropriate management & funding;
- C. approve ToR, budget, calculate member fees
- D. appoint Ombudsman;

# Governance Structure (3)

## Independence and impartiality warranted by:

- ❑ BO's governance structure
- ❑ mandate & organizational rules
- ❑ oversight of BO by Board\*, O is accountable only to Board.
- ❑ Board Tasks:
  - a) Ombudsman's appointment
  - b) Approval of annual budget
  - c) TOR approval
- ❑ Board plays no role on specific complaints
- ❑ European BOs in line with EC Rec. 98/257.

# Bank Ombudsman Powers and Duties

- ✓ consider disputes within ToR,
- ✓ advise public on complaint procedures,
- ✓ issue bulletins on banking practice,
- ✓ ask parties to provide necessary info.,
- ✓ implement procedures, issue decisions,
- ✓ decline a dispute if outside ToR, etc.,
- ✓ dismiss a complaint,
- ✓ prepare/publish dispute resolution proced.,
- ✓ publish Annual Report.

# Disputes within ToR

A dispute = complaint after exhausting bank's internal complaint resolution process

## ***Eligible complaints:***

### **I) by complaint nature:**

*(a) act/omission by a bank incl. offering/withholding/providing, etc. a product/service to cons.*

*(b) acts/omissions on breach of consumers' privacy.*

### **II) by complaint amount:**

– any complaint up to a limit amount.

(GER max. - €5K, Czech Rep., IT & GR - €50K).

# Disputes outside ToR

## *Disputes:*

- about banks not affiliated to BO's schemes
- not first considered by the bank
- outside various time limits
- about systemic issues
- considered previously by BO
- more appropriately dealt with another forum
- where the claim exceeds limit amount
- where consumer has not waived confidentiality rights

# Rights & Obligations of Members

## ***Member banks shall:***

- act within ToR, BO Rules, law & ind. codes
- provide to BO any information required;
- promote to clients BO membership;
- display Banking Code, etc.;
- pay membership fee or/and service fees;
- comply/enforce BOs decision to take action.

## ***Member banks shall not:***

- resort to litigation while being in a BO procedure;
- prevent a customer from using BO services;
- provide BO with misleading info.

# Bank Ombudsman's Summary Profile

## *What BO can do?*

- provide an independent and fair alternative to the court, free to customers
- help parties see options for agreement/solution
- keep service confidential
- quality and consistency of complaint process
- make decisions binding to bank up to limit amount
- decide on individual cases,
- encourage best practices

## *What BO Cannot Do*

- be a regulator /"watchdog"
- play the advocate for parties
- accept complaints before lodged first with banks
- deal with systemic issues
- make management decisions
- provide assistance on issues in litigation, arbitration, etc.
- force customers to accept its decision\*
- provide general information on banks/banking services

# Bank Ombudsman Complaint Procedures

**Five major steps a complaint follows :**

1. Receipt of an enquiry
2. Receipt of a complaint
3. Verification of complaint admissibility
4. Investigation / Assessment & Mediation
5. Recommendation/ Determination

# Operational & Funding Issues

## A. Staffing, MIS, daily operations

## B. Funding

- in voluntary schemes run by BAs - BA budget
- statutory and public BOs: funding from central banks + budget

Sophisticated financing formula in UK and AU:

- annual participation fee;
- a set fee for each complaint;
- amount on dispute resolution time (AU)

# III: Recommendations

## *Romanian banking industry:*

- ❑ ↗ people's access to banks and consumer complaints;
- ❑ needs to increase customers confidence;
- ❑ not enough vocal to promote customer awareness of internal dispute units;
- ❑ subject of criticism by consumers;
- ❑ offers time-consuming, inconvenient & costly process;
- ❑ no proper EU standards, needs to harmonize with EU
- ❑ information asymmetry + new, complex products.
- ❑ needs to enhance cons. protection legislation & financial literacy program

# BO Benefits- Consumers' Perspective

- Benefits are double: in-house complaint offices and an independent third party redress body.
- BOs impartiality, objectivity, etc. encourages consumers to bring more business to banks.
- Benefit from application of common standards.
- Free service & binding BO rulings on banks.
- Difficulties in court discourage consumers;
- Discourage use of legal rep., reducing costs;
- A less bureaucratic and jargon-free;
- No risks for consumers- still free to go to a court

# Bank Ombudsman

## Benefits- Bank's Perspective

- “Conciliation is better than litigation” due to high costs/reputation problems
- Costs banks pay per case to BO are  $<$  than costs in court.
- Better customer retention rates (bank has options to rectify errors/improve relations).
- BO publishes case studies, as educational materials for consumers/banks

# Recommendations

## *Establish Independent BO*

In view of

- *Current Romanian consumer protection;*
- *Romania's imminent entry to EU;*
- *Benefits of scheme creation;*

***We recommend to PWG:***

- An independent & effective BO scheme be established, modeled after EU schemes.

# Recommendations (2)

RBA to consult with industry & NBR to establish the role of scheme.

## **A) PWG to determine the scheme status:**

**voluntary** (+ good for separate industry schemes, - risk of non-compliance, - no legal base for enforcement, +/- protects best industry's interest)

**compulsory** (+ all should legally comply, + good enforcement, + better customers' protection, - not flexible)

**private/government-run** (self-regulation better than state regulation?! + funding issues)

## **B) Safeguard Ombudsman's independence**

- i) Creation of independent governing body\*
- ii) Conclusion of a binding ToR
- iii) Assurance of O qualificat., O appointment

# Recommendations (3)

- iv) all RBA member banks to participate in BO,
- v) upgrade & promote banks' in-house complaint-settlement schemes,
- vii) PWG considers 2 options for complainants:
  - Scheme accessible to private consumers
  - Scheme open to: individ., self-employed & SME;
- viii) design a strategy to increase awareness
- ix) design and adopt the Banking Code
- x) all RBA members finance BO. PWG to explore financing formula-*flat fee/case fee, etc.*

# Actionable Steps

- ✓ PWG to set up the new Scheme's Board, to make decisions on key BO issues.
- ✓ Board to work with RBA, NBR & Consumers Bodies on scheme design.
- ✓ Board to determine on BO's jurisdiction.
- ✓ Legal expertise needed for major scheme docs (by-laws, TOR, etc.),
- ✓ Assistance offered by UK FOS.
- ✓ BO Board to decide on O's qualifications & appointment.
- ✓ Developing policy and practices (manuals, procedures)

# Actionable Steps (2)

- ✓ Recruiting, professional & management staff training
- ✓ Estimations for the first 3 yrs of operational budget
- ✓ IT solution to create a proper database
- ✓ Prepare brochure-how to resolve disputes.
- ✓ Draft a template form of complaint
- ✓ Build a website, etc.
- ✓ Independent assessor for quality purposes
- ✓ Application to become FIN-NET member.
- ✓ Publication of Annual Report\*

# Budget Considerations

1. **Capital expenditures** (furniture, electrical installations, computer, telecommunication equipment, building, etc.)
2. **Proforma income statement**
  - **Revenue from ordinary activities**
  - Employee benefits expense
  - Board members' fees & Consulting fees
  - Occupancy costs
  - Technology costs
  - Utility costs (water, energy, tel.)
  - Travel and accommodation expenses
  - Promotion and information expenses
  - Auditor's remuneration
  - Depreciation and amortization expense
  - Other expenses from ordinary activities
  - **Profit before income tax expense**

# This Is A “Convergence” Review

**“Convergence”**<sup>1</sup> is a World Bank-sponsored financial sector development program for South-East Europe focused on:

- Undertaking analytical tasks of micro-institutional issues calling for solutions tailored to country circumstances
  - Taking EU integration as a strategic perspective
  - Building awareness of market participants and involving them in the search of market-building solutions
  - Fostering dialogue between authorities and market participants to identify workable solutions in local context
  - Using the experience of regional former policy makers and experts whenever possible
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- 1/ “Convergence” is supported by a grant from Italy’s Ministry of Economy and Finance