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Protection for Banking Consumers in the United Kingdom and the United States of America: Fees and Charges

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C O N T E N T S

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EXECUTIVE SUMMARY

Introduction

1. Following the deregulation of interest rates for deposits in July 2001, members of the Panel on Financial Affairs expressed concern about banks starting to levy fees and charges for some basic banking services. With a view to safeguarding the interests of banking consumers in Hong Kong, the Panel requested the Research and Library Services Division to conduct a research on the protection for banking consumers in relation to fees and charges imposed by banking institutions in other jurisdictions.

2. We have selected the United Kingdom (UK) and the United States of America (US) for this study.

The United Kingdom

3. The UK government always emphasizes that greater competition can facilitate the protection of consumers. Hence, the government is committed to formulating and updating consumer legislation and has established two enforcement agencies, the Office of Fair Trading (OFT) and the Competition Commission (CC), for consumer protection and competition.

4. The regulator of the financial services industry is the Financial Services Authority (FSA) which was established under the Financial Services and Markets Act (FSMA) 2000. The FSA has consumer-related objectives: (a) to promote public understanding of the financial system and (b) to secure an appropriate degree of protection for consumers. Under the FSMA, the FSA creates a compensation scheme for the protection of consumers and establishes a new single financial ombudsman office for the resolution of consumer disputes. The FSA also promotes consumer education which encompasses education for financial literacy.

5. In addition to regulation by statute, industry self regulation also plays an important role in the area of consumer protection. The industry associations sponsor the issue of the Banking Code which sets out the minimum standards of services that banking institutions should provide when dealing with their customers.

6. The Code is enforced by an independent agency, the Banking Code Standards Board (BCSB), which may discipline banking institutions which have been found to breach the Code through disclosure of breaches, issue of a warning or reprimand, public censure, suspension or cancellation of the institution's registration as a subscriber to the Code.

7. **There is no statutory regulation of banks' fees and charges.** Banks and building societies comply with the Banking Code on a voluntary basis, but the Code does not regulate banks' fees and charges; it only demands that banks must act "fairly and reasonably" in all dealings with their customers.

8. Nowadays, **most banks in the UK do not charge for the general operation of a bank account** provided the customer keeps a cleared credit balance on the account. Banking institutions always have the rights to determine their fees and charges. Prior to deregulation of interest rates for deposits in 1971, banks already charged their customers for running their deposit accounts. After interest rate deregulation, banks continued to charge for banking services. However, **from early-1980 onwards**, **greater competition in the banking industry has resulted in most banks abolishing their fees and charges for basic banking services**, although they continued to charge for other services and facilities such as arranging overdrafts and issuing bank drafts. Therefore, **there does not appear to be any direct relationship between the deregulation of interest rates for deposits and the levying of charges by banks in the UK.**

9. Banking institutions in the UK are required to provide customers with personal notification at least 30 days before any increases to their fees and charges take effect.

10. The Labour government started to tackle the inter-linked problems of social exclusion in 1997 and established 18 Policy Action Teams (PATs) to investigate and report on specific areas of social exclusion. The No. 14 Policy Action Team (PAT 14) was asked to look into the scope for widening access to financial services. PAT 14 recommended that banking institutions should develop and promote basic account services to meet the needs of vulnerable consumers.

11. In line with the recommendation of PAT 14, banks in the UK have introduced Basic Bank Accounts to attract people who may have been "kept out" or "opted out" of banking services to open accounts. As one of the reasons for refraining from opening a bank account is often the high charges associated with inadvertent overdraft and the lack of creditworthiness, Basic Bank Accounts simply provide money transmission services with no access to credit and there is no danger of running up debts and incurring charges which people on low income may fear. At present, all major banks offer Basic Bank Account services to their customers.

12. In order to ensure that banks provide standardized marketing information on Basic Bank Accounts, the Treasury has planned to introduce a Charges, Access and Terms (CAT) standard, which refers to the standard for fair Charges, easy Access and decent Terms, by the end of 2001. Banks and building societies may advertize a Basic Bank Account as CAT standard if it meets or exceeds them.

<u>The United States of America</u>

13. In the US, matters relating to consumer protection are handled by the Federal Trade Commission (FTC).

14. Matters relating to protection for banking consumers are handled by the FTC as well as other financial regulators, namely the Office of the Comptroller of the Currency, the Board of the Federal Reserve, the Federal Deposit Insurance Corporation and the Office of Thrift Supervision. These regulators are empowered to take enforcement actions if banking institutions are found to have violated any laws for protection for banking consumers.

15. There is **no** federal law regulating fees and charges for banking services. However, seven states have enacted legislation to authorize their state banking authorities either to monitor fees and charges imposed by banking institutions, and if necessary, to regulate them or to require banking institutions to provide low cost accounts for the public.

16. The Truth in Savings Act (TISA) requires that consumers are to be provided with adequate information so as to assist them in making the best choice among the various types of accounts. This act also requires banks to give an advance notice to their customers at least 30 days before any adverse changes made to the terms and conditions of an account.

17. In 1998, about 9.5% of families in the US did not have any transaction account. One of the reasons was that fees and charges and minimum balance requirements were too high.

18. The federal government has carried out various measures to facilitate access to banking services by under-served communities. One of the measures is the introduction of the Electronic Transfer Account (ETA) which may only be opened by federal benefits recipients. This account allows a minimum of four cash withdrawals and four balance inquiries, and charges a maximum fee of US$3 (HK$23.4) per month. The federal government will subsidize banking institutions a one-time fee of US$12.6 (HK$98.2) for each ETA opened to offset the costs of establishing the account.

19. Another measure is that the federal government will provide incentives for banking institutions to offer First Account, which is one of the components of the First Account Initiative programme to people who are not federal benefits recipients and do not have any bank account.

20. Seven states have also passed laws to require banking institutions to provide Lifeline Accounts which are low cost checking and saving accounts that provide 8-10 checking or debit transactions at a fee of not more than US$3 per month.

<u>Analysis</u>

21. Both the UK and the US have enacted legislation to protect banking consumers; however, they do not have any legislation regulating the levying of fees and charges by banking institutions. At present, banking institutions in these two countries are required to provide customers with personal notification at least 30 days before any increases to their fees and charges take effect.

22. Both the UK and the US have taken measures to help disadvantaged groups to have access to basic banking services. The UK government encourages banks to offer Basic Bank Accounts while the US government subsidizes and provides incentives for banks to offering low cost bank accounts.

PROTECTION FOR BANKING CONSUMERS IN THE UNITED KINGDOM AND THE UNITED STATES OF AMERICA: FEES AND CHARGES

PART 1 - INTRODUCTION

1. Background

1.1 At the meeting of the Panel on Financial Affairs on 11 January 2001, in relation to the discussion on the implementation of the final phase of interest rate deregulation, some members expressed concern about the plan of certain banks to raise charges for some basic banking services, thereby increasing the burden on small depositors. In the absence of a mechanism to deal with consumer protection in the banking industry, the Panel requested the Research and Library Services Division (RLSD) to conduct a research on the practices and experience of other economies in safeguarding the interests of banking consumers.

2. Scope of the Research

2.1 The scope of the research, as agreed by the Panel, covers:

(a) any regulation specifically formulated to protect banking consumers, in particular, in the event that a bank alters its terms and conditions in respect of some basic banking services; and

(b) the power of the relevant regulators in protecting banking consumers in the context of (a).

2.2 In line with members' concern mentioned in paragraph 1.1 above, this study will focus on the protection for banking consumers in relation to fees and charges imposed on them by banks.

2.3 We have selected the United Kingdom (UK) and the United States of America (US) for this study as these countries, like Hong Kong, have deregulated interest rates for deposits in banking institutions. These two countries have also put in place legislation or codes of practice in their banking industries to protect banking consumers. Their experience will serve as good reference for Hong Kong.

3. Methodology

3.1 The research involves a combination of information collection and analysis. In addition to making reference to materials available in the LegCo Library, we also use reference materials acquired through the Internet and other outside sources.

3.2 In this report, we use the 2000 average exchange rate of £1 = HK$11.8 and US$1 = 7.791 to convert the British pound and the US dollar into Hong Kong dollar.[1]

[1] Census and Statistics Department, Hong Kong Special Administrative Region, *Hong Kong Monthly Digest of Statistics*, May 2001, p. 125.

SECTION A - THE UNITED KINGDOM

PART 2 - REGULATORY FRAMEWORK FOR CONSUMER PROTECTION AND COMPETITION

4. Policy Responsibility for Consumer Protection and Competition

4.1 The United Kingdom (UK) government always emphasizes that greater competition can facilitate the protection of consumers. Hence, the government is committed to formulating and updating consumer legislation and has established enforcement agencies for consumer protection and competition.

4.2 In the UK, the Secretary of State for Trade and Industry is responsible for the overall policy on consumer affairs and promotion of competition. One of his specific tasks is to develop competitive markets within a regulatory framework which promotes fairness and sustainability.[2]

4.3 The Consumer Affairs Directorate (CA) under the Department of Trade and Industry (DTI) takes the lead within the government on consumer policy and helps formulate consumer legislation in the UK. Its mission is to promote a fair deal for all consumers, thereby helping both business competitiveness and social inclusion. The CA's key priorities include:

(a) improving consumer advice and information;

(b) updating laws and regulations which protect consumers;

(c) improving enforcement; and

(d) promoting consumers' interests in the rapidly developing international world of e-commerce.

4.4 As a policy directorate, the CA works closely with other parts of government, regulators, and business and consumer groups such as the Office of Fair Trading, Local Authority Trading Standards Departments, and the National Association of Citizens Advice Bureaux.

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2 The Secretary has an overall aim to increase competitiveness and scientific excellence in order to generate higher levels of sustainable growth and productivity in a modern economy. In addition to the objective stated in paragraph 4.1, the Secretary has three other objectives: (a) to promote enterprise, innovation and higher productivity; (b) to make the most of the UK's science, engineering and technology; and (c) to enhance competitiveness of UK's companies through overseas sales and investments and a high level of quality foreign direct investment.

5. Enforcement Agencies for Consumer Protection and Competition

5.1 One of the enforcement agencies in the UK is the Office of Fair Trading (OFT) which is both a consumer watchdog and a competition authority. The aim of the OFT is to advance and safeguard the interests of consumers in the UK by promoting effective competition, removing trading malpractice, and publishing appropriate guidance. Please refer to Appendix I for information about the OFT.

5.2 Being a consumer watchdog and a competition authority, the OFT plays an important role in protecting banking consumers. Under the Consumer Credit Act, the Director General must keep under review social and commercial developments relating to the provision of consumer credit[3] and the operation of the regulatory framework. He is also required to advise the Secretary of State for Trade and Industry on these issues. In addition, the Office maintains contacts with the credit industry and consumer bodies, and liaises closely with the Department of Trade and Industry about regulatory reforms. However, the OFT has no power to handle disputes between a bank and its customers.

5.3 Another important agency for promoting competition is the Competition Commission[4] (CC) which has two distinct functions. Firstly, the CC carries out inquiries into matters referred to it by other UK competition authorities such as the OFT concerning monopolies, mergers and economic regulation of utility companies. Secondly, the CC hears appeals against decisions of the OFT and the Regulators of utilities in respect of infringements of prohibitions contained in the Act concerning anti-competitive agreements and abuse of a dominant position.

5.4 To facilitate competition in the banking sector, the OFT and CC are required to scrutinize the Financial Service Authority's rules and practices in order to determine whether they may distort competition and whether they are justified for the purpose of protecting bank consumers. (Please see paragraph 7.12 on competition analysis.)

[3] Consumer credit business covers a range of financial transactions, including credit cards, cash loans and overdrafts.

[4] The CC is an independent public body established by the Competition Act which replaced the former Monopolies and Mergers Commission in April 1999.

PART 3 - REGULATION OF FINANCIAL SERVICES, BANKING CONSUMER PROTECTION, AND COMPETITION IN BANKING SECTOR

6. Policy Responsibility for Regulation of Financial Services

Policy Department Responsible for Economic and Financial Services

6.1 The United Kingdom (UK) Treasury, headed by the Chancellor of the Exchequer, is the policy department responsible for economic and financial services. Its overall mission is to raise the rate of sustainable growth through creating economic and employment opportunities for all. In pursuit of this, its objectives include:

(a) maintaining sound public finances;

(b) maintaining an effective accounting and budgetary framework; and

(c) promoting high standards of regularity, propriety and accountability.

6.2 The Treasury is also responsible for widening access to financial services, especially by the deprived communities. Hence, the Treasury has encouraged the provision of basic banking services and planned to establish a Charges, Access and Terms (CAT) standard for basic bank accounts by the end of 2001. For details, please see section 18.

7. Role of Financial Services Authority in Consumer Protection and Promoting Competition

7.1 The regulator of the financial services industry is the Financial Services Authority (FSA) which was established under the Financial Services and Markets Act (FSMA) 2000. The Act brings together under one roof the regulation of investment businesses, banks, building societies and insurance companies previously handled by nine regulatory bodies. The FSA also establishes the framework for a single Financial Ombudsman and compensation schemes to provide protection for financial services consumers.

7.2 Under the FSMA, the FSA is given an explicit mandate in consumer protection and education[5]. These are:

(a) promoting public understanding of the financial system; and

(b) **securing an appropriate degree of protection for consumers**.

7.3 In order to fulfil its consumer-related objectives, the FSA provides the following services to consumers --

(a) Financial Ombudsman Service

7.4 The FSMA requires the FSA to establish a new single Financial Ombudsman Service (FOS) for the resolution of consumer disputes. The existing Banking Ombudsman Scheme which was set up by the industry had been incorporated under the FOS at the end of November 2001.[6] All firms authorized by the FSA will be subject to the Ombudsman's procedures, but will be required to try to resolve complaints themselves in the first instance.

(b) Financial Services Compensation Scheme

7.5 The FSMA requires the FSA to create the Financial Services Compensation Scheme (FSCS) for paying compensation to consumers who have suffered financial loss if a bank is unable to meet its liabilities.

7.6 The FSCS includes the existing Deposit Insurance Scheme which is administered by the Deposit Protection Board. This Scheme is funded by contributions from banks and each depositor may receive payment of 100% of the first £2,000, and thereafter 90% of their deposits, up to a maximum of £33,000 (HK$389,400) in the event of bank collapses.

(c) Consumer Education

7.7 The FSA promotes consumer education which encompasses education for financial literacy, provision of consumer information and advice, and a long-term plan of embedding financial literacy in the education system.

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5 Two other statutory objectives of the FSA are (a) maintaining confidence in the UK financial system and (b) contributing to reducing financial crime.

6 The FOS will replace eight dispute-resolution schemes which are used to handle complaints about financial services. The eight schemes are: (a) Banking Ombudsman, (b) Building Societies Ombudsman, (c) FSA Independent Complaints (d) Insurance Ombudsman, (e) Investment Ombudsman, (f) Personal Investment Arbitration Service, (g) Personal Investment Authority Ombudsman, and (h) Securities and Futures Authority Complaints and Arbitration Service.

7.8 The FSA also publishes comparative information on costs and charges in a range of financial products so that consumers will be better able to assess the products available. It also prepares guidelines for personal finance education and conducts consumer research to identify areas of major concern for consumers.

7.9 The FSA provides a public enquiry service in the form of "one stop shop" -- Consumer Help, issues consumer publications (booklets and factsheets explaining different financial products and services such as pensions, mortgages, savings and investments, financial planning and advice) and compiles comparative tables on financial products for consumers' reference.

Consumer Panel

7.10 In order to assess the FSA's effectiveness in meeting its objectives to protect consumers' interests and promote public understanding of the financial system, the FSA established the Financial Services Consumer Panel[7] (FSCP) in December 1998, which provides advice on the interests and concerns of consumers. The FSA must have regard to any representations made to it by the FSCP.

Competition Analysis

7.11 The FSMA stipulates that the FSA must consider the issue of competition in its policy formulation process so as to protect the interests of financial services consumers. Its rules and practices are subject to the competition scrutiny of the Office of Fair Trading and the Competitive Commission.

[7] The FSCP has 13 members including the chairman. They are appointed by an open recruitment process. The appointees are on contact terms for a fixed period.

8. Role of Industry Associations

8.1 In addition to regulation by statute, industry self regulation also plays an important role in the area of consumer protection. The British Bankers' Association[8] (BBA), Building Societies Association[9] (BSA) and Association for Payment Clearing Services[10] (APACS) sponsor the issue of the Banking Code[11], which sets out the minimum standards of services that banks and building societies should comply with when dealing with their personal customers. The term "personal customers" refers to private individuals and includes executors or trustees of private individuals. Small business customers will be protected by a new industry code of banking practice, effective from March 2002.

8.2 Banking institutions comply with the Banking Code on a voluntary basis. The Code was revised following a wide ranging consultation exercise with, among others, the Office of Fair Trading, Banking Ombudsman, the Treasury, and the Consumers' Association. The revised Banking Code came into force in January 2001 and is subject to review at least once every three years.

8.3 About 140 banks and building societies (including all high street banks and building societies), accounting for over 99% of the total number of institutions, subscribe to the Banking Code.

8.4 The three associations mentioned in paragraph 8.1 above established the Banking Code Standards Board (BCSB) in October 1999 to monitor banks and building societies' compliance with the Code. The BCSB replaced the former Independent Review Body (IRB) which was considered ineffective as it had no enforcement powers against institutions which breached the Banking Code. To improve the situation, the BCSB has been provided with more resources in monitoring and enforcing compliance with the Code. (Please see paragraphs 13.1 - 13.9 for further discussions on the BCSB.)

8.5 The BBA is also active in educating banking consumers. It publishes a wide range of public information materials which are available on its website for easy access by banking consumers.

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8 The BBA represents over 300 member banks operating in the UK from more than 60 countries.

9 Building societies specialize in housing finance and retail deposit-taking services. Some of the larger societies provide a full range of personal banking services. There are 68 authorized building societies, all of which are members of the BSA, with total assets of around £160 billion (HK$1,888 billion).

10 The main payment systems are run by three separate companies operating under an umbrella organisation, the Association for Payment Clearing Services.

11 The Banking Code was first published in 1991.

PART 4 - INDUSTRY SELF REGULATION IN THE PROTECTION FOR BANKING CONSUMERS

9. Regulation of Banks' Fees and Charges

9.1 **There is no statutory regulation of banks' fees and charges.** Banks and building societies comply with the Banking Code on a voluntary basis, but the Code does not regulate banks' fees and charges; it only demands that banks must not breach the first key commitment in the Code, i.e. to act "fairly and reasonably" in all dealings with their customers. The Banking Code Standards Board (BCSB), which is responsible for enforcing the Code, has emphasized that the concepts of "fairness" and "reasonableness" should be considered in accordance with normal dictionary meanings and the Ombudsman's interpretation.

9.2 The Banking Code requires that customers should be given, at the start of the relationship and at any time they ask, details of the fees and charges which apply to their particular account. Its intention is that customers should not be surprised at any charge they see appearing on their statements in connection with the basic operation of an account. The BCSB has advised banks and building societies to include a warning statement that the fees and charges may change in the future.

10. Notification of Increases in Fees and Charges

10.1 The Banking Code requires that banks and building societies should provide the customer with personal notification at least 30 days before any increases to their fees and charges take effect.

11. Charge for Basic Banking Services

11.1 Nowadays, **most banks in the United Kingdom (UK) do not charge for the general operation of a bank account** provided the customer keeps a cleared credit balance on the account. In other words, most banks do not charge for basic banking services such as paying in by machine or at the counter, cash withdrawals, normal clearance of cheques, processing of standing orders, direct debits, paying-in books, cheque books, statements, and advice of balances.[12] However, banks may charge their customers for certain types of banking services such as arranging overdrafts, stopping a cheque, issuing bank drafts, crediting foreign cheques, and sending money abroad.

[12] British Bankers' Association, *Understanding Bank Charges and Interest*, 2001.

12. Relationship between Interest Rate Deregulation and Levying of Fees and Charges

12.1 The British Bankers' Association (BBA) says that banking institutions in the UK always have the rights to determine their fees and charges. Prior to deregulation of interest rates for deposits in 1971[13], banks already charged their customers for running their deposit accounts. After interest rate deregulation, banks continued to charge for banking services.

12.2 However, **from early-1980 onwards**, **greater competition in the banking industry has resulted in most banks abolishing their fees and charges for basic banking services**, although they continued to charge for other services and facilities such as arranging overdrafts and issuing bank drafts. Therefore, **there does not appear to be any direct relationship between the deregulation of interest rates for deposits and the levying of charges by banks in the UK.**

13. Monitoring and Compliance

13.1 The BCSB is responsible for enforcing the Banking Code. It is an industry self-regulatory regime and is sponsored by banks and building societies which pay an annual subscription fee based on the size of their business.

13.2 Though it is funded by the industry, the BCSB has emphasized that it can maintain its independence of banking interests as independent directors always form the majority of the board. The BCSB has ten directors, consisting of five public interest directors[14], three financial industry directors, an independent chairman and a chief executive. If there is a vacancy for a public interest director, the Board will publicly advertize the post and select the appropriate applicant to take up the job.

13.3 The BCSB handles complaints about the general running of the Code (for example, a failure to inform customers about changes to terms and conditions). However, the BCSB does not resolve customer complaints, which is a matter for the Banking Ombudsman, who had been incorporated in a new Financial Services Ombudsman scheme at the end of November 2001.

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13 In September 1971, the Bank of England deregulated the interest rates for deposits and abandoned ceilings on bank lending so as to improve the competitive environment in the banking sector. As a result, banks have been able to set interests paid on bank accounts freely since 1971.

14 They are independent directors who are responsible for protecting the benefits of the public. The BCSB pays them attendance fees for attending meetings.

13.4 The BCSB is responsible for ensuring that banks and building societies comply with the Banking Code by monitoring their conduct through:

(a) scrutinizing an annual self-certification questionnaire, the Annual Statement of Compliance, signed by the chief executive of each subscribed financial institution;

(b) conducting market research activities, including "spot check" mystery shopper visits;

(c) undertaking compliance visits by its own officers and by authorized agents;

(d) monitoring media comment and analysis of the banking industry; and

(e) investigating complaints regarding the general running of the Banking Code from the public.

Sanctions

13.5 The BCSB initially refers allegations of breaches of the Code to the bank or building society concerned to take appropriate action and asks for an explanation from the financial institution.

13.6 If the institution fails to correct the malpractice, the BCSB may discipline it through the following ways:

(a) publication of the name of the financial institution concerned and details of the institution's breach in the Annual Report of the BCSB;

(b) issue of directions as to future conduct;

(c) issue of recommendations on the remedy of past conduct;

(d) issue of a warning or reprimand;

(e) cancellation or suspension of an institution as a subscriber of the Banking Code; and

(f) public censure of an institution, by notifying the media of the BCSB's findings in respect of a breach or breaches and any sanctions applied, and posting the press release on the BCSB website. In addition to notifying the media, notification may also be made to any of the three Associations sponsoring the Code, or any other bodies as the Board may see fit.

13.7 The BCSB has not sought the power to fine the institution concerned on the ground that reputational risk via "naming and shaming" presents a more powerful sanction and the procedure of fining the institution is complicated. The BCSB is not yet convinced that fining power is worthwhile in terms of speed of response or cost.[15]

Disciplinary Actions Taken

13.8 The BCSB has provided some examples of disciplinary actions taken against Code subscribers' malpractice. As an example, the BCSB has suspended or refused the registration of institutions which were unable to meet important Code requirements. In another case, a director from a leading bank was summoned to appear before the BCSB and told to change current practices.[16]

13.9 The BCSB points out that many shortcomings are rectified as a result of BCSB's monitoring activity and dialogue with banks and building societies, without the need to deploy formal disciplinary powers.

14. Complaints

14.1 The Banking Code stipulates that banks and building societies should have a set of internal procedures for handling complaints. Customers should be told what further steps are available if they are not satisfied with the outcome of their complaint from the institution concerned (i.e. recourse to the Financial Ombudsman Service).

14.2 Banks and building societies have to adopt the FSA rules in handling complaints in given time limits. The actions required to be taken in the given time limits are set out in Table 1.

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15 Banking Code Standards Board, *Seven Key Questions about Bank Service,* February 2001.

16 Banking Code Standards Board, *Frequently Asked Questions*, May 2001.

Table 1 - Actions Required to be Taken in Given Time Limits

Actions Required to be Taken	Given Time Limits
Written acknowledgement.	Within two business days of receipt of complaint
Either final response, or holding response saying when the institution will make further contact.	Within ten business days of receipt of complaint
Either final response, or explanation for delay and indication when final response will be given. In the latter case, inform complainant of right to refer to Financial Ombudsman Scheme if dissatisfied with the delay.	By the end of eight weeks from receipt of complaint

Source: Banking Code Standards Board

14.3 We have not been able to obtain the number of complaints received by the BCSB and the Banking Ombudsman about banks' fees and charges because they do not have a breakdown of the complaints received.

PART 5 - ACCESSIBILITY TO BASIC BANKING SERVICES

15. Tackling Social Exclusion

15.1 After winning the election in May 1997, the Labour government started to tackle the inter-linked problems of social exclusion[17], which the government has defined as follows --

> *a shorthand term for what can happen when people or areas suffer from a combination of linked problems such as unemployment, poor skills, low incomes, poor housing, high crime, bad health and family breakdown.*[18]

As these dimensions of social exclusion are typically interrelated, each one increases the likelihood of others.

15.2 To reduce social exclusion in the United Kingdom (UK), the Social Exclusion Unit (SEU) was set up in December 1997 to co-ordinate and improve government action. The Unit's remit was to improve government action to reduce social exclusion by producing "joined up solutions to joined up problems". (Human and financial costs caused by social exclusion are in Appendix II.)

15.3 The Unit's initial report, *Bringing Britain Together: a National Strategy for Neighbourhood Renewal*, was published in September 1998. Subsequently, the SEU established 18 Policy Action Teams (PATs) to investigate and report on specific areas of social exclusion.[19] The No. 14 Policy Action Team (PAT 14), a mixed group of government officials and experts, was asked to look into the scope for widening access to financial services. PAT 14 published its findings in November 1999.

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[17] This is a deliberately flexible definition, and the problems listed are only examples. Many other dimensions of exclusion can be added.

[18] Social Exclusion Unit, *Bringing Britain Together: a National Strategy for Neighbourhood Renewal,* September 1998.

[19] The 18 areas dealt by the SEU are: jobs, skills, business, neighbouring management, housing management, neighbourhood wardens, low demand/unpopular housing, anti-social behaviour, community self-help, arts and sport, schools plus (building learning communities), young people, shops (improving shopping access for people living in deprived neighbourhoods), financial services, closing the digital divide, learning lessons (skills and knowledge needed for effective neighbourhood renewal), neighbourhood renewal, and better information.

16. Promoting Financial Inclusion

Policy Action Team 14's Report Access to Financial Services

16.1 PAT 14 found that about 1.5 million low income households (7% of total households in the UK) did not use financial services in 1998. This represented over two million adults, mostly not in employment, or living on welfare benefits, and most of them were social housing tenants.

16.2 PAT 14 found that the reasons why poor people used less financial services were complex. The problem was a mismatch between potential customers' needs and the financial products available. Providers should therefore develop new products that were more suitable for low income customers, so that those who lived in poor neighbourhoods, as well as those in less deprived areas, should benefit. PAT 14 therefore recommended that banks, building societies and other providers should develop and promote low cost basic account services.[20]

The Office of Fair Trading's Report *Vulnerable Consumers and Financial Services*

16.3 In 1999, having undertaken a study on what could be done to help vulnerable consumers[21] to use financial services, the Office of Fair Trading (OFT) published a report entitled *Vulnerable Consumers and Financial Services* in which the OFT recommended that banks and building societies offer a basic, on-line, no-overdraft, low-cost-account on which it was not possible to incur high charges for unauthorized credit to help vulnerable consumers to use financial services. Such accounts could be widely accessible through the existing bank network or at home by telephone. The UK government has agreed to the recommendations.

16.4 The British Bankers' Association (BBA) has also undertaken studies with a view to promoting financial inclusion. Details of such studies, together with the findings of PAT 14 and OFT's study, are in Appendix III.

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20 Policy Action Team 14, *Access to Financial Services*, November 1999, p. 3.

21 The OFT identified seven categories of the population which might be considered to be vulnerable. These seven categories were: (a) those on low income; (b) the unemployed; (c) those suffering from a long-term illness or disability; (d) those with a low level of education attainment; (e) members of ethnic minorities; (f) older people; and (g) the young.

17. Basic Bank Accounts

17.1 In line with the recommendation of PAT 14, banks in the UK have introduced Basic Bank Accounts to attract people who may have been "kept out" or "opted out" of banking services to open accounts. As one of the reasons for refraining from opening a bank account is often the high charges associated with inadvertent overdraft and the lack of creditworthiness, Basic Bank Accounts simply provide money transmission services with no access to credit (thus eliminating the need for credit history) and there is no danger of running up debts and incurring charges which people on low income may fear.

<u>Features of Basic Accounts Defined by the Banking Code</u>

17.2 In an effort to provide standardized guidelines for banks, the Banking Code was revised in January 2001 to specify the features of a Basic Bank Account:

(a) income can be paid by employers directly into the account;

(b) benefits can be paid by the government directly into the account;

(c) cheques and cash can be paid into the account;

(d) bills can be paid by direct debit, by transferring money to another account or by a payment to a linked account;

(e) cash can be withdrawn at cash machines;

(f) there is no overdraft facility; and

(g) the last penny in the account can be withdrawn.

17.3 Although the Banking Code has defined the features of a Basic Bank Account, it does not require banks and building societies to offer such accounts; it merely requires banks and building societies to give their customers information on all appropriate products and services (including Basic Bank Account).

Reasons for Offering Basic Bank Accounts

17.4 In reply to our enquiry as to why banks are willing to offer Basic Bank Accounts although the provision of such banking service to the public may not be profitable, the BBA says that profitability of individual banking products is based on the benefit that the bank gains from the account (e.g. balances held, the opportunity to sell other products) against the cost of providing that product. The more features a product has and the more manual involvement that is required by bank staff, the more costly it is to provide the service. Basic Bank Accounts have relatively few features and the level of manual involvement is relatively low, but balances held on the account are also likely to be low and the opportunities for cross-selling are also likely to be low. However, individual accounts can fluctuate in profitability according to how they are used by the customer and an account that is not profitable at one stage may become profitable in the future.

Basic Bank Account Availability and Functionality

17.5 Table 2 shows a summary of Basic Bank Account availability and functionality in 2001 drawn up by the BBA. By now, all major banks in the UK offer Basic Bank Account services to their customers, including the "big four" banks, namely HSBC, Lloyds TSB, National Westminster Bank and Barclays.

17.6 Basic Bank Accounts are not exclusive to certain members of society. However, as with all banking products and services, banks may impose restrictions as to who may open a basic account. Generally speaking, people who have bad debts, bankruptcy orders, or record of fraud may be denied the opportunity to open a Basic Bank Account.

17.7 It can be seen that 11 of the 13 banks surveyed do not require minimum deposits for Basic Bank Accounts. All banks surveyed provide payments-in by automated credit transfers, direct debits and standing orders, and cash machine card services. Nearly half the banks surveyed also provide free buffer zone[22] and electronic payment card services. However, 11 of the 13 banks do not provide any cheque book for their Basic Bank Account holders.

[22] This means that banks provide free temporary overdraft so funds can be drawn from a cash machine when there is less than £10 (HK$118) in the account.

Table 2 - Summary of Basic Bank Account Availability and Functionality in 2001

	Restrictions on who may open a Basic Bank Account[(a)]	Minimum deposit required?	Payments in by automated credit transfers?	Direct Debits & standing orders?	Cash machine card?	Free buffer zone[(b)]?	Electronic payment card?	Cheque book?
Abbey National "Instant Plus"	✓	✓	✓	✓	✓	✗	✓	✗
Alliance & Leicester "Alliance account – Electron tier	✓	✗	✓	✓	✓	£10	✓	✓
Bank Of Scotland "Easycash"	✗	✗	✓	✓	✓	£10	✓	✗
Barclays "Cash Card Account"	✓	✗	✓	✗	✓	£10	✗	✗
Clydesdale "Cashmaster"	✓	✗	✓	✓	✓	✗	✗	✗
Co-operative Bank "Cashminder"	✓	✗	✓	✓	✓	✗	✓	✗
Halifax "Cardcash"	✓	✓	✓	✓	✓	✗	✓	✓
Lloyds TSB "Bank account"	✓	✗	✓	✓	✓	£10	✗	✗
HSBC "Basic bank account"	✓	✗	✓	✓	✓	£10	✗	✗
National Westminster Bank "Step account"	✓	✗	✓	✓	✓	£10	✓	✗
Royal Bank of Scotland "Key account"	✗	✗	✓	✓	✓	✗	✗[(c)]	✗
Woolwich "Open Plan (without credit)"	✓	✗	✓	✓	✓	£50[(d)]	✓	✗
Yorkshire Bank "Readycash"	✓	✗	✓	✓	✓	✗	✗	✗

Notes:
(a) People who have bad debts, bankruptcy orders, or record of fraud may be denied to open a Basic Bank Account.
(b) Free temporary overdraft so funds can be drawn from a cash machine when there is less than £10 in the account.
(c) Introduction planned for later this year.
(d) Not for cash withdrawals at branches or cash machines.

Source: British Bankers' Association

Interest Paid on Basic Bank Accounts

17.8 Banks may either pay a Basic Bank Account lower rate of interest compared to a savings account or no interest in order to reduce the cost of providing a Basic Bank Account. In the UK, interest rates vary a great deal between different types of account and different banks and building societies. Decisions on the rate of interest offered are a commercial matter for the individual banks and building societies concerned. As a general rule, there tends to be a balance between the interest rate offered and the features that form the account package; in other words, the higher the cost of providing the account, the lower the interest rate offered.

Costs of Providing a Basic Bank Account

17.9 The BBA used the 1998 data obtained from banks and estimated that it might cost up to £80 (HK$944) per customer to set up a Basic Bank Account and about £70 (HK$826) per annum to maintain it[23]. The costs included producing plastic card(s) for operating the account, processing cash withdrawals, operating direct debits, dealing with queries, postage and a share of overheads. Those figures also suggested that the average daily balance needed to cover just the annual costs of maintaining an account would be about £1,300 (HK$15,340).[24]

18. Proposed CAT Standard on Basic Bank Accounts

18.1 In order to ensure that banks provide standardized marketing information on Basic Bank Accounts, the Treasury has planned to introduce a Charges, Access and Terms (CAT) standard, which refers to the standard for fair Charges, easy Access and decent Terms, by the end of 2001. This standard may help consumers to choose products on an informed basis that best suit their needs and thereby improve access to banking services by all groups in the community. The CAT standard is voluntary and does not carry a government endorsement or guarantee. Banks and building societies may advertize a Basic Bank Account as CAT standard if it meets or exceeds them.

18.2 Table 3 shows the features of proposed CAT standard for Basic Bank Accounts. One of the features of CAT is "no one-off or regular charges for everyday transactions". This means that banks and building societies have to provide free basic banking services for their Basic Bank Account holders if such CAT standard is adopted.

[23] The BBA admitted that annual running costs could vary considerably around this figure, depending on the extent to which, and how, the account was used.

[24] British Bankers' Association, *Promoting Financial Inclusion*, April 2000.

Table 3 - Proposed CAT Standard for Basic Bank Accounts

	Basic Bank Accounts
Charges	• No one-off or regular charges for everyday transactions. • No risk of an overdraft.
Access	• No requirement for initial or regular deposits. (Undischarged bankrupts and persons under aged 16 may be turned down.) • Account holders must be able to use the following: (a) cash machines; (b) cash and cheque deposits; (c) automated credit transfer; and (d) direct debit, standing order, or Budget Accounts[25].
Terms	• All advertising and paperwork must be straightforward, fair and clear. • Account holders must be given regular statements, and at least six months notice if the bank can no longer offer a Basic Bank Account on CAT standard terms. • Ability to withdraw all funds.

Source: The Treasury, *Standards for Retail Financial Products*, January 2001, p. 53.

[25] A Budget Account allows a customer to make a fixed, single monthly payment into an account from which the bank will pay all agreed recurring bills throughout the year.

SECTION B - THE UNITED STATES OF AMERICA

PART 6 - OVERVIEW OF PROTECTION FOR BANKING CONSUMERS IN THE UNITED STATES OF AMERICA

19. Consumer Rights

19.1 In the United States of America (US), all rights and liberties of people are guaranteed by the Constitution.[26] To conform to the Constitution, laws and regulations are enacted to prevent unfair or deceptive acts or practices in respect of individual industries and trades so as to protect the rights of consumers.

20. Authority Responsible for Consumer Protection

20.1 The federal laws governing antitrust and consumer protection are enforced by the Federal Trade Commission (FTC) which has also issued trade regulation rules. Please refer to Appendix IV for information about the FTC.

21. Consumer Protection Laws Relating to Consumer Finance

21.1 In the area of financial transactions, such as transactions involving charge and credit cards, Automated Teller Machines (ATMs), deposit accounts, automobile leases and mortgages, the rights of consumers are protected by the respective federal and state laws. Please refer to Appendix V for a summary of consumer protection and civil right laws which are related to consumer finance.

21.2 These laws are enforced by the FTC, and other financial regulators, namely the Board of the Federal Reserve System (Fed), the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS). Please refer to Appendix VI to Appendix IX for information about the functions of these agencies.

[26] Sol Bloom, *Questions and Answers Pertaining to the Constitution*, National Archives and Records Administration, http://www.nara.gov/exhall/charters/constitution/conqa.html

22. Objectives of Protecting Banking Consumers

22.1 In the US, protection for banking consumers means to achieve the following objectives:

(a) safeguarding a depositor's deposits;

(b) promoting competitive banking services;

(c) providing customers with a meaningful disclosure of deposit and credit terms;

(d) ensuring that all consumers are receiving equal treatment and have equal access to all banking services;

(e) promoting financial privacy; and

(f) preventing problems and abusive practices during credit transactions, debt collection and reporting of personal credit histories.

23. Types of Banks

23.1 In the US, banking institutions are divided into the following three types, depending on the government agency which charters them, and whether or not they are members of the Fed.

(a) National Banks

23.2 National banks are commercial banks[27] that are chartered and regulated by the OCC. By law, all national banks are members of the Fed and are insured by the FDIC.

[27] Commercial banks are banks that serve business customers in the old days. Nowadays they also serve individual consumers.

(b) State Banks

23.3 State banks are banks that are chartered by banking authorities of states. State banks are not required to join the Fed, but they may elect to become members if they meet the standards set by the Fed.[28] All state member banks are federally-insured and are regulated by the Federal Reserve Board, while state non-member banks that are federally-insured are regulated by the FDIC and state non-member banks that are not federally-insured are regulated by the FTC.

(c) Thrifts

23.4 Thrifts refer to savings banks[29] and savings and loans associations[30] (S&Ls). All federally-insured thrifts are regulated by the OTS while non-federally-insured thrifts are regulated by the FTC.

24. Choice of Accounts

24.1 Table 4 shows the types of accounts that are commonly offered by banking institutions in the US. It should be noted that banking institutions do not always call their accounts of the same nature by the same names. They often choose distinctive names in the hope of attracting consumers.

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28 State member banks are required to subscribe to the stock in their regional Federal Reserve Bank in an amount equal to 3% of their capital and surplus, and receive a 6% annual dividend. These banks are eligible for voting for directors of the Reserve Bank.

29 Savings banks are depository institutions that engaged primarily in accepting consumer savings deposits and in originating and investing in securities and residential mortgage loans. They also offer checking-type deposit accounts and loans services.

30 Savings and loans associations are depository institutions that accept deposits mainly from individuals and invest heavily in residential mortgage loans. They also offer checking-type deposit accounts and loans services.

Table 4 - Types of Accounts Commonly Offered by Banking Institutions in the US

Type of account	Features
Savings account	• Earns interest • Does not require a substantial deposit to open an account • Allows to withdraw money at any time
Checking account	• Does not earn interest • Fees may be charged because banking institutions incur significant costs to process checks drawn on these accounts
Negotiable Order of Withdrawal (NOW) account	• Checking account that earns interest • Caters for non-business customers • Minimum balance is required
Money Market Deposit account	• Similar to NOW account • Earns a higher rate of interest • Requires a higher minimum balance (often US$2,500 or more) • Limits the number of checks drawn per month
Certificate of Deposit (CD)	• Savings deposit that requires customer to keep a certain amount of money in a banking institution for a fixed period of time • Rate of interest is higher if deposit period is longer • No check-writing facilities
Individual retirement account	• Savings deposit that requires customers to keep their money in the banking institution until they reach a certain age (usually aged 60 or older) • Offers excellent rewards • Charges a significant penalty to individuals who withdraw their funds before they reach a specified age

25. Truth in Savings Act

25.1 As consumers are given a variety of choices and they need to determine what type of account will best suit their needs or offer the best returns, it is necessary to provide them with adequate information so that they can make better choices.

25.2 In 1991, the federal government enacted the Truth in Savings Act (TISA), the purpose of which is to require the disclosure of (a) the rates of interest which are payable on deposit accounts and (b) the fees that are assessable against deposit accounts so that consumers can make a meaningful comparison of the terms and conditions of one type of account to those of the others.

25.3 To implement the TISA, the government published Regulation DD (12 CFR 230) in 1992 and mandatory compliance commenced in 1993.

<u>Types of Information to be Disclosed</u>

25.4 The information that should be disclosed to consumers as prescribed by Regulation DD is listed below:

(a) interest rates;

(b) fees;

(c) periodic service charges;

(d) penalties;

(e) terms and conditions;

(f) account restrictions;

(g) minimum balance requirements; and

(h) minimum amount required to open an account.

25.5 The above information is required to be disclosed under the following circumstances:

(a) on request;

(b) when an account is opened;

(c) when terms are adversely changed on an existing account;

(d) before certain time accounts mature;

(e) if periodic statements are sent; and

(f) when accounts are advertised.

25.6 It should be noted that if a banking institution plans to adversely change any terms or conditions of an existing account, it is required to mail or deliver a written notice to its customers at least 30 days before the effective date of the adverse change. The notice should highlight the adverse changes.

25.7 All disclosures are required to be in writing and in a form that a consumer can keep. Even though some disclosures are allowed to be conducted electronically, they should be supplemented with written notices.

26. Consumer Complaints

26.1 If a consumer has a complaint against a banking institution, he may in the first place contact a staff member of the institution and attempt to resolve the complaint directly. If he is not satisfied with the resolution, he may put forward the complaint to the relevant regulator for further investigation.

26.2 All financial regulators respond to complaints and inquiries made by the public about consumer protection issues involving banking institutions under their jurisdictions. If banking institutions are found to violate any laws for protection for banking consumers, regulators may take enforcement actions.

26.3 For violations that are not severe and do not involve abusive practices, regulators may request the banking institution concerned to take necessary corrective actions. These include verbal or written commitments by the institution's officials to resolve identified violations, board resolutions that record such commitments, and memoranda of understanding that reflect an agreement between the regulator and the institution's directors. For more severe violations and unsafe or abusive practices, regulators may take formal and legally enforceable actions. These actions encompass written agreements, cease and desist orders[31], suspension, prohibition, or removal actions.

26.4 Any insured banking institution which has been found to violate any law, regulation, or order issued by regulators is required by the court to pay a civil penalty of not more than US$5,000 (HK$38,955) for each day during which such violation continues. For those which knowingly commit the violation, the maximum amount of penalties is not to exceed US$1,000,000 (HK$77,910,000) or 1% of the total assets of the banking institution which ever is the less.[32]

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[31] A cease and desist order is an order issued after notice and opportunity for hearing, requiring a depository institution, a holding company, or a depository institution official to terminate unlawful, unsafe, or unsound banking practices.

[32] FDIC, *1000 - FDIC Federal Deposit Insurance Act*, Section 8 (i).

PART 7 - REGULATIONS OF PROTECTION FOR BANKING CONSUMERS IN RELATION TO FEES AND CHARGES

27. Laws Regulating Fees and Charges

27.1 ***At present, there is no federal law regulating fees and charges for banking services in the US***. ***However, seven states have either enacted legislation to authorize their state banking authorities to monitor fees and charges imposed by banking institutions, and if necessary, to regulate them or to require banking institutions to provide low cost accounts for the public.***

28. Interest Rate Deregulation

28.1 Prior to January 1986, bank interest rates were regulated by the federal government and a ceiling was imposed on interest rates for deposits. Following the enactment of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA), interest ceilings for deposits were orderly phased out. Please refer to Appendix X for the provisions and effects of the DIDMCA.

28.2 One of the reasons that led to the abolition of interest ceiling in 1980 was that continuous inflation and increase in market interest rates between 1976 and 1979 increased the opportunity cost of holding deposits in banks. Depositors therefore withdrew their funds from deposit accounts and invested them in other financial instruments paying market interest rates. As the decrease in the amount of funds held by banks had affected adversely their profitability, banks demanded the federal government to remove the interest ceiling so that they could compete for funds against other financial institutions which offered investment opportunities at market interest rates. Following the enactment of the DIDMCA, banks are free to determine interest rates for deposits.

29. Fees and Charges for Banking Services

29.1 Prior to interest rate deregulation, banking institutions had already imposed fees and charges for their services on banking consumers. Therefore, the imposition of fees and charges by banking institutions for their services on banking consumers does not appear to have any direct relationship with the deregulation of interest rate for deposit accounts.

29.2 According to the Federal Deposit Insurance Corporation (FDIC), non-interest income, particularly fee income, constitutes a large portion of a banking institution's income. In 1999, non-interest income accounted for over 40% of net operating revenues.[33]

29.3 In 1999, the US Public Interest Research Group (PIRG)[34] conducted a survey on service fees charged by banking institutions. The survey covered 526 banking institutions in 33 states and the District of Columbia. The findings showed that except for senior citizen accounts which were only available in Massachusetts, a maintenance fee was charged for all types of accounts if one failed to meet the minimum balance requirement. Table 5 shows the balance requirements and the average maintenance fee charged by banking institutions for different types of accounts.

Table 5 - Balance Requirements and Account Maintenance Fees Charged by Banking Institutions in the US in 1999

Type of accounts	Minimum daily balance to avoid fees (US$)	Average daily balance to avoid fees (US$)	Average monthly maintenance fees (US$)
Regular checking accounts	519-616	1,093-1,357	7.12-7.76
NOW accounts	1,062-1,342	2,054-2,459	8.42-9.28
No Frills checking accounts[1]	Not applicable	Not applicable	3.34-4.14
Savings accounts	217-271	Not available	2.63-3.01
ATM-only accounts	Not applicable	Not applicable	3.02-3.77
Senior citizen accounts[2]	Not applicable	Not applicable	5.45 for aged 50-54 3.32 for aged 55-61 0.39 for aged 62-64 0 for aged 65 & above

Remarks:

1. No Frills checking accounts are accounts which limit the number of checks drawn and charge a fee regardless of balance.
2. Massachusetts was the only state surveyed that required banking institutions to provide free checking account for senior citizens aged 65 or above.

Source: US Public Interest Research Group, *Big Banks, Bigger Fees: The 1999 PIRG Bank Fee Survey*

33 US Public Interest Research Group, *Big Banks, Bigger Fees: PIRG's 1999 Bank Survey*, http://www.pirg.org/reports/consumer/bankfees/bank99.pdf

34 US Public Interest Research Group (PIRG) is a national lobbying office for state PIRGs. State PIRGs are alliances of state-based, citizen-funded organizations which safeguard public interest.

30. Fees and Charges for Other Basic Banking Services

30.1 In addition to charging a maintenance fee for not meeting the minimum balance requirement, banking institutions also charge fees for other basic banking services. Table 6 shows the fees charged in 1999 for some basic banking services.

Table 6 - Fees and Charges for Some Basic Banking Services in the US in 1999

Type of fees	Average amount (US$)
Bounce checks[1]	21.19 - 23.08
Stopping payment on a check	18.24 - 20.44
Deposit item returned[2]	4.51 - 5.12
Off-us ATM fees[3]	1.03 - 1.27
ATM surcharges[4]	1.08 - 1.35
Early account closing fees[5]	12.60
Telephone call centre fees[6]	1.57 for a call to human operator 0.42 for a call to computer centre
Monthly fees for ATM cards	1.50
Check safekeeping[7]	1.00-5.00

Remarks:
1 Bounce checks are checks drawn against insufficient funds.
2. Deposit item returned refers to the bounce check which has been deposited by a consumer.
3. Off-us ATM fees are fees imposed on banking institutions' own customers for using other banking institutions' ATM machines.
4. ATM surcharges are charges imposed on customers of other banking institutions for using the banking institutions' ATM machines.
5. Early account closing fees are fees imposed on banking customers who close the accounts which have been opened for less than one year.
6. Telephone call centre fees are fees imposed on banking customers who call to make balance inquiries. In general, banking institutions allow an average of 2.7 free calls per month to human operators and 3.9 free calls per month to computer centres.
7. Check safekeeping is a service provided by a banking institution which will keep the bounce check for its customer if the customer wants to get back his check.

Source: US Public Interest Research Group, *Big Banks, Bigger Fees: The 1999 PIRG Bank Fee Survey*

31. Complaints about Fees and Charges

31.1 In 1999, the OCC handled 94 000 complaint cases, of which 1 787 cases (1.9%) were about fees and charges.[35] People mainly complained about the increase in and imposition of additional fees such as fees for check cashing and bounce checks.

[35] The figure 1 787 was deduced from the following: the OCC handled 94 000 complaint cases, of which 22% related to deposit accounts. Among the complaints about deposit accounts, 48% were about service issues, of which 18% were about fees and charges.

PART 8 - ACCESSIBILITY TO BASIC BANKING SERVICES

32. Ownership of Transaction Accounts

32.1 According to a survey conducted by the Federal Reserve Board in 1998, about 9.5% of families in the US did not have any transaction account[36] and nearly one in four low income families did not have any checking account. Among those who did not have any checking account, 82.6% had annual incomes of less than US$25,000 (HK$194,775), or of less than 65% of US family median income.[37]

32.2 The reasons for families not having any checking account in 1998 are given in Table 7. Service charges and minimum balance requirement are impediments to the ownership of a checking account. In fact, 47.9% had owned a checking account some time in the past and the survey's analysis indicated that these families were much more likely to respond that fees were a deterrent for having an account.

Table 7 - Reasons Given by Families for Not Having Any Checking Account in 1998

Reason	Families (%)
Do not write enough checks to make it worthwhile	28.4
Do not like dealing with banks	18.5
Do not have enough money	12.9
Service charges are too high	11.0
Minimum balance is too high	8.6
Cannot manage or balance a checking account	7.2
Do not need/want an account	6.3
Credit problems	2.7
No bank has convenient hours or location	1.2
Others	3.1
Total	100

Source: Federal Reserve Board, "Recent Changes in US Family Finances: Results from the 1998 Survey of Consumer Finances", *Federal Reserve Bulletin*, January 2000, http://www.federalreserve.gov/Pubs/oww/oss2/98/bull0100.pdf

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36 Transaction accounts refer to checking account, savings account, money market deposit account, money market mutual funds and call account at brokerage.

37 Gary Gensler, Treasury Under Secretary (Domestic Finance), *Testimony Before the House Committee on Banking and Financial Institutions*, 27 June 2000

33. Measures to Increase Access to Basic Banking Services

33.1 During the 1970s, some savings and loans associations (S&Ls) denied credit to low income[38] and minority groups as credit extension was based on the perceived characteristics instead of the creditworthiness of individual loan application. Such practice did not only deter potential home buyers from purchasing property, but it also impeded capital flow.

33.2 In view of the above unfair practice, the federal government enacted the Community Reivestment Act (CRA) in 1977 to encourage banking institutions to help meet the credit needs of the communities in which they operated. The federal government has also developed other measures in the past 20 years to facilitate access to banking services by the under-served communities. The federal government has been promoting the use of banking services because[39]-

(a) People who cannot afford a bank account usually resort to check cashers, pay day loan operators, high cost mortgage lenders and pawn shops for check cashing and money borrowing. Most of these cashing outlets are not regulated and the cost for the services is very high.

(b) It is difficult for families to accumulate savings without any bank account.

(c) Account ownership is critical to participation in the mainstream economy. It is difficult and expensive for a person to establish credit, obtain a credit card, qualify for a loan to buy a car or a house, or obtain financing for a small business if that person does not have any bank account.

(d) The cost for the federal government to make payment by electronic transfer is far less than the cost of processing a check.

(e) People are unable to make any on-line financial transaction if they do not have any bank account.

38 Low-income borrowers refer to borrowers with household incomes that are less than 80% of the local median family income of their metropolitan area.

39 Gary Gensler, Treasury Under Secretary (Domestic Finance), *Testimony Before the House Committee on Banking and Financial Institutions*, 27 June 2000

33.3 Other measures taken by the federal government include encouraging banking institutions to install ATMs in local post office in under-served communities, offering financial incentives to banking institutions to increase retail banking services to under-served communities through the Treasury's Community Development Financial Institutions Fund [40] and Bank Enterprise Award Programme[41], and introducing Electronic Transfer Accounts (ETAs) and First Account Initiatives, the details of which are described in the ensuing paragraphs.

34. Electronic Transfer Accounts

34.1 An Electronic Transfer Account (ETA) is an account introduced by the Department of the Treasury (Treasury) in 1996 to ensure that individuals receiving federal benefits payments through electronic transfer have access to an account that charges a reasonable fee and provides the same consumer protection which is available to other account holders at the same banking institutions.

<u>Features of Electronic Transfer Accounts</u>

34.2 In 1998, the Treasury published for consultation in the Federal Register[42] a Notice of Proposed ETA Features. In response to the comments obtained from financial institutions, financial institution trade associations, consumer and community-based organizations, the Treasury issued a guideline to the effect that the ETA should carry the following features -

(a) be an individually owned account at a federally-insured banking institution;

(b) accepts federal benefit, wage, salary and retirement payments which are made through electronic transfer, and such other deposits as a banking institution agrees to permit;

(c) be subject to a maximum service fee of US$3.00 (HK$23.4) per month;

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[40] Community Development Financial Institutions Fund promotes access to capital and local economic growth by directly investing in and supporting community development financial institutions and expanding banking institutions' lending, investment, and services within under-served communities.

[41] Bank Enterprise Award Programme is the Treasury's Community Development Financial Institutions Fund 's primary tool for pursuing its strategic plan goal of expanding banking institutions' community development lending and investment activity.

[42] The Federal Register is the official daily publication for Rules, Proposed Rules, and Notices of Federal agencies and organizations, as well as Executive Orders and other Presidential Documents.

(d) allows a minimum of four cash withdrawals and four balance inquiries per month, to be included in the monthly fee, through any combination of proprietary ATM transactions and/or over-the-counter transactions;

(e) be subject to consumer protection[43] that is available to other account holders at the same banking institution;

(f) allows access to the on-line point-of-sale network of banking institutions;

(g) requires no minimum balance, except as required by federal or state law;

(h) be either an interest-bearing or non-interest-bearing account subjected to the option of the banking institution; and

(i) provides a monthly statement.

34.3 One of the required features of the ETA is that banking institutions are not allowed to charge any fee in addition to the monthly fee. However, they are allowed to charge ETA holders other account-related fees such as fees for additional cash withdrawals, balance inquiries, card replacement, account research and using ATMs that owned by other banking institutions. They are allowed to impose fees for these services at their customary rates, except that overdraft fees are not allowed to exceed US$10 (HK$77.9) per case.

34.4 Additional features, such as check writing or Automated Clearing House[44] debit capability, are not required even if the cost of providing such features falls within the maximum monthly fee. ETA does not include a bill payment feature. A banking institution may also limit any additional deposits to electronic deposits or allow recipients to deposit checks and/or cash in addition to other electronic deposits.

34.5 Federal benefits recipients are allowed to switch to other checking or deposit accounts any time to receive their federal benefits payments and are encouraged to do so if other accounts better meet their needs. If an ETA holder stops receiving federal payments, the account is allowed to remain open at the discretion of the banking institution.

43 Consumer protection includes federal insurance and Truth in Savings Act disclosures.
44 Automated Clearing House is an electronic payment option that allows participants to pay Customs fees, duties, and taxes electronically.

Advantages of Holding Electronic Transfer Accounts

34.6 The advantages of holding an ETA are listed below -

(a) Security

34.7 Payments made through electronic transfer are safer than those made by checks. Recipients do not have to worry that their check payments will be lost or stolen.

(b) Efficiency

34.8 Payments made through ETA are faster than those made by checks because funds delivered to a recipient's account are available on the date the payment is due. Besides, problems concerning payments made through electronic transfer can often be resolved within 24 hours, whereas those relating to payments made by paper checks take about two weeks.

(c) Cost Effectiveness

34.9 In general, check cashing outlets charge up to 3% for cashing a check, and on average, social benefits recipients pay US$9 (HK$70) to US$16 (HK$125) per month for cashing checks.[45] Such amount is higher than the average monthly fee (US$7.12 to US$7.76) required to be paid for maintaining a regular checking account.

34.10 From the federal government's point of view, payment made through ETA would reduce the cost of processing paper checks. Each year, the Treasury replaces over 800,000 checks that are lost, stolen, delayed or damaged during delivery.[46]

Providers of Electronic Transfer Accounts

34.11 It is not mandatory that all banking institutions offer ETA. However, banking institutions choosing to offer ETA are required to enter into a contractual agreement (ETA Financial Agency Agreement) with the Treasury, and the Treasury will reimburse these institutions a one-time fee of US$12.60 (HK$98.2) per ETA opened to offset the costs of setting up the account. Set up costs include the costs of holder enrolment, staff training and card issuance. As of 22 June 2000, 586 banking institutions have agreed to offer ETA in 6 132 branches nation-wide.[47]

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[45] Office of Public Affairs, Department of Treasury, *Remarks of Treasury Secretary Lawrence H. Summers to the Consumer Bankers Association, Washington, DC,* 8 May 2000

[46] Statement of John D. Hawke, Jr., Treasury Under Secretary for Domestic Finance at the House Banking and Financial Services Committee, 25 September 1997, http://www.house.gov/financialservices/92597haw.htm

[47] Gary Gensler, Treasury Under Secretary (Domestic Finance), "Testimony before the House Committee on Banking and Financial Institutions", *Treasury News*, Office of Public Affairs, 27 June 2000, http://www.ustreas.gov/press/releases/ps736.htm

Acceptability of Electronic Transfer Accounts

34.12 Although the Debt Collection Improvement Act enacted in 1996 requires that starting from January 1999, all federal benefits payments are to be made through electronic transfer, individual federal benefits recipients may choose to continue to be paid by check if they claim that payments made through electronic transfer to ETA would impose a hardship.

34.13 Therefore, as of June 2000, only 2 500 ETAs have been opened.[48] It is suspected that some people are worried that banking institutions may be able to "capture" their federal benefits if they fall behind on their loan payments, while others are afraid that the tax authority may figure out how much money they make and tax their income.

35. Lifeline Accounts

35.1 Lifeline Accounts are low cost checking and savings accounts that provide approximately 8-10 checks or debit transactions at a fee of not more than US$3 (HK$23.4) per month. In general, these accounts require little or no minimum balance.

Background

35.2 Starting from the mid 1980s, there was growing concern about high service fees imposed by banking institutions in seven states, namely Illinois, Massachusetts, Minnesota, New Jersey, New York, Rhode Island and Vermont. To address this issue, these states have enacted legislation either to authorize their state banking authorities to monitor bank fees, and if necessary, to regulate them or to require state banking institutions to provide Lifeline Accounts for the public.

48 Michael A. Stegman, MacRae Distinguished Professor of Public Policy and Business, Chairman, Public Policy Curriculum, Director, Centre for Community Capitalism, Frank Hawkins Kenan Institute of Private Enterprise, Kenan-Flagler Business School, University of North Carolina, *Testimony on H.R.4490, First Accounts Act 2000*, 27 June 2000, http://commdocs.house.gov/committees/bank/hba65616.000/hba65616_0.htm

35.3 Although states have enacted laws to regulate fees and charges levied by banking institutions or to provide low cost accounts, these laws are preempted by federal laws because the Constitution preserves federal laws as "supreme law of the land".[49] Therefore, banks under the jurisdiction of the Office of the Comptroller of the Currency (OCC) and thrifts under the jurisdiction of the Office of Thrift Supervision (OTS) need not abide by state laws to provide low cost accounts, neither are they subject to state regulations in respect of the level of fees and charges.

Features of Lifeline Accounts

35.4 Table 8 lists the features of Lifeline Accounts offered by the seven states.

[49] General Accounting Office, Letter from Richard J. Hillman, Associate Director, Financial Institutions and Markets Issues, Lynn H. Gibson, Associate General Counsel, Office of the General Counsel to James A. Leach, Chairman of Committee on Banking, Finance and Urban Affairs, House of Representative on 7 February 2000, http://www.gao.gov/corresp/ggd-00-51r.pdf

Table 8 - Features of Lifeline Accounts in the Seven States

State	Account Features	Eligibility
Illinois	Basic checking account: • US$100 minimum initial deposit; or • a written agreement with the account holder requiring direct deposit with the banking institution from a third party of recurring payments on a monthly basis; • no minimum balance; • 10 free checks each month; • after the 10th check, fees vary by institution.	Persons aged 65 or above
Massachusetts	Savings account: • no service fees; • deposit and balance requirements vary by institution.	Persons aged 65 or above and Persons aged 18 or below
Minnesota	Savings account: • no service fees if US$50 is maintained in the account.	All persons
New Jersey	Checking account: • US$3 monthly service charge; • 8 free checks per month -- each check after that is US$0.5; • US$50 or less needed to open the account; • US$1 to maintain the account; • unlimited in-bank withdrawals and deposits.	All persons
New York	Checking account: • US$25 minimum opening deposit; • no minimum balance requirement; • US$3 monthly service charge; • 8 free checks per month; • applies to state-chartered banks only.	Varies with each bank
Rhode Island	Passbook/statement savings account: • no charge.	All persons
	Basic savings account: • no fee if US$500 or less is kept in the account.	Persons aged 17 or below
	• State-chartered institutions are required to cash state, municipal or federal checks of US$750 or less at no charge to non-account holders.	Customers must produce photo ID when cashing checks
Vermont	Banking commissioner conducts quarterly surveys to make sure the state's 29 banking institutions are offering basic, low cost checking and savings accounts.	Not applicable

Source: Bankrate.com, http://www.bankrate.com/smm/news/chk/19981013a.asp

36. First Account Initiative

36.1 First Account Initiative is a pilot scheme which the government targets the low income non-federal benefits recipients. To help these people to access basic banking services, the federal government introduced the First Accounts Initiative in the Financial Year 2001 budget, and an appropriation of US$8 million (HK$62.3 million) has been made for the implementation of the Initiative.

Purpose

36.2 The purpose of the First Accounts Initiative is to extend traditional banking services to people who do not have any checking or savings account or any other relationship with a banking institution. This programme complements the ETA programme.

Components

36.3 The First Account Initiative has four major components as follows -

(a) Pilot First Accounts

36.4 The Treasury works with banking institutions to pilot first accounts which are low cost, electronic banking accounts for people who do not own any bank account and are not federal benefits recipients. The programme provides banking institutions with flexibility and incentives to design products which suit the needs of those people, and are also profitable for the banking institutions.

(b) Increase the Number of ATMs and Other Access Points

36.5 To encourage access to banking services, the Treasury works with banking institutions and electronic networks to increase the number of ATMs in low income neighbourhoods that lack basic banking services. These include the provision of incentives for the installation of ATMs in safe, secure and convenient locations, expanding the number of point-of-sale terminals at merchant outlets and providing internet-based solutions in these communities.

(c) Educate Low Income Families about Banking and Financial Services

36.6 The Treasury works with community-based organizations to educate low income families about the benefits of having a bank account, managing household finances and building assets. This programme supports partnerships between banking institutions and community-based organizations with expertise in delivering consumer financial literacy.

(d) Funding Research and Development Projects

36.7 The initiative also funds new research at the Treasury on the financial services needs of low and moderate income individuals who do not receive federal benefits, as well as the development of products that can help banking institutions to meet those needs.

Progress

36.8 The Treasury has published a Request for Information Notice to solicit input from interested organizations on possible structures for First Accounts pilots. Funding is available to pilot project vendors[50] for establishing and marketing low cost accounts in urban centres and rural Native American areas that lack access to basic banking services. Awards will also be given to banking institutions which provide the best First Account services. This programme will be reviewed in 2002.

[50] Project vendors refer to banking institutions, community organizations, tribal governments, and financial services electronic networks and a combination of all these parties.

SECTION C - ANALYSIS

37. Overall Comparison

37.1 We will compare the manners in which banking consumers' interests are protected in the United Kingdom (UK) and the United States of America (US), with specific reference to the levying of fees and charges by banking institutions.

38. Protection for Banking Consumers

38.1 In both the UK and the US, protection for banking consumers refers to the promoting of competitive banking services, ensuring consumers having access to basic banking services, providing consumers with relevant information about bank accounts, safeguarding depositors' deposits, and promoting consumer education.

39. Regulators for Banking and Financial Services

39.1 Both the UK and the US have enacted legislation to protect banking consumers. In the case of the UK, the relevant Act is the Financial Services and Markets Act (FSMA), for which the Financial Services Authority which is the only financial regulator in the UK, is the responsible authority. In the US, several financial regulators are responsible for protecting the interests of banking consumers and they are the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the Board of the Federal Reserve.

40. Code of Banking Practice

40.1 With regard to standards of business practices, the industry associations in the UK have established a Banking Code, one of the objectives of which is to protect the interests of banking customers. The Code is enforced by an independent agency, the Banking Code Standards Board (BCSB), which may discipline banking institutions which have been found to breach the Code.

40.2 However, in the US, the interests of banking consumers are protected entirely by laws. There is no non-statutory instrument similar to the Banking Code in the UK, which is a common feature in Commonwealth countries.

41. Resolution of Consumer Complaints

41.1 The UK has a statutory ombudsman scheme laid down in the FSMA to arbitrate disputes, but the US does not have such a scheme. If consumers have complaints about banking practices in the US, they may have them resolved by putting them forward to the respective regulators.

42. Relationship between Interest Rate Deregulation and Levying of Fees and Charges

42.1 In the UK, prior to deregulation of interest rates for deposits in 1971, banks already charged their customers for running their deposit accounts. After interest rate deregulation, banks continued to charge for banking services. However, from early-1980 onwards, greater competition in the banking industry has resulted in most banks abolishing their fees and charges for basic banking services, although they continued to charge for other services and facilities such as arranging overdrafts and issuing bank drafts. Therefore, there does not appear to be any direct relationship between the deregulation of interest rates for deposits and the levying of charges by banks in the UK.

42.2 In the case of the US, similarly the imposition of fees and charges by banking institutions for their services on banking consumers does not appear to have any direct relationship with the deregulation of interest rate for deposit accounts because fees and charges had already been levied by banking institutions for their services prior to interest rate deregulation.

43. Regulation of Banks' Fees and Charges

43.1 In the UK, there is no legislation regulating banks' fees and charges. The Banking Code does not regulate banks' fees and charges, but demands that banks must act "fairly and reasonably" in all dealings with their customers.

43.2 In the US, there is no federal law regulating the fees and charges levied by banks and thrifts. However, seven states have enacted legislation to monitor banks' fees and charges, and to regulate them if necessary.

44. Notification of Increases in Banks' Fees and Charges

44.1 In both countries, banking institutions are required to provide customers with personal notification at least 30 days before any increases to their fees and charges take effect.

44.2 In the case of the UK, this requirement is prescribed in the Banking Code which is a non-statutory guideline. In the US, the requirement is stipulated in the Truth in Savings Act (TISA).

44.3 Any bank in the UK found to have breached this requirement and other provisions in the Banking Code, which is a non-statutory instrument, may be disciplined by the BCSB through disclosure of breaches, issue of a warning or reprimand, public censure, suspension or cancellation of the institution's registration as a subscriber to the Code. In the US, if banks have been found to violate the TISA or any other laws for protection for banking consumers, regulators may take legally enforceable actions such as the issue of cease and desist orders and the removal of the banks' charter.

45. Accessibility to Basic Banking Services

45.1 Both countries have taken measures to help disadvantaged groups to have access to basic banking services.

45.2 The UK government encourages banks to offer Basic Bank Accounts which are on-line, no-overdraft, and no-service-charge accounts. At present, all major banks in the UK offer such accounts.

45.3 In the case of the US, the federal government subsidizes and provides incentives for banks to providing low cost bank accounts. One type of low cost accounts is the Electronic Transfer Accounts which may only be opened by federal benefits recipients. Another type of low cost accounts is the First Account under the First Account Initiative programme.

Appendix I

The Office of Fair Trading

A.1 The goal of the Office of Fair Trading (OFT) is "*to make markets work well for consumers.* The OFT's activities in pursuit of this goal involve:

(a) enforcement -- of competition and consumer protection rules;

(b) investigation -- into how markets are working; and

(c) communication -- to explain and improve awareness and understanding.

A.2 With respect to consumer protection, the OFT encourages traders across all business sectors to provide high standards of consumer service and to ensure that complaints are tackled quickly and fairly.

A.3 Under the Fair Trading Act[51], the OFT has to encourage trade associations to develop industry codes of practice for the above purpose, and to give advice to consumers on how to resolve complaints with various schemes, the ombudsman, advice agencies and trading standards officers.

A.4 In order to educate consumers about their rights and choices, the OFT publishes a range of publications aimed at individual consumers and the professions. They vary from basic introduction to consumer rights to technical and research reports. The OFT also provides a public enquiry service known as Consumer Help which gives general advice on consumer rights in the United Kingdom and tips on how to complain or where consumers should turn to for assistance with a particular problem.

A.5 With respect to promoting competition, the OFT is empowered by the Competition Act[52] to prohibit anti-competitive agreements and practices and the abuse of a dominant market position. The OFT has to identify mergers that may have an adverse impact on competition and public interests for reference to the Competition Commission for further inquiry.

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51 Under the Fair Trading Act, the Director General of the OFT must: (a) review the commercial activities in the UK with a view to identifying practices which may adversely affect the economic interests of consumers; and (b) where the Director considers that a trader has persisted in a course of conduct that is detrimental to consumers and involves breaches of the law, endeavour to seek assurances from the trader that such practices will cease. Court action can follow if a trader declines to give an assurance or breaks one already given.

52 The Competition Act, which came fully into effect in March 2000, strengthened competition law. It is modelled on European Commission competition law and provides a strong deterrent against anti-competitive practices and agreements such as cartels, and against abuse of a dominant market position. The Act prohibits agreements, practices and conduct which have a damaging effect on competition.

Appendix II

Human and Financial Costs Caused by Social Exclusion

A.1 The core elements of social exclusion are identified as follows:

(a) low income related to employment status, for example, lack of employment opportunities and low levels of welfare benefit among people not in work;

(b) lack of access to services such as education, vocational training, health care and financial services; and

(c) poor environment, including poor housing, deprived neighbourhoods and difficult family life.

A.2 The government has emphasized that large numbers of people in deprived communities do not share the economic prosperity as a result of social exclusion. This has affected all aspects of life in these communities: housing, health care, education, and crime, among others. The country has to bear both human and financial costs.

A.3 The human costs are faced by:

(a) individuals
-- underachievement in education and the labour market, low income, poor access to services, stress, ill-health and the impact on children; and

(b) wider society
-- has reduced social cohesion, higher crime and fear of crime, and higher levels of stress and reduced mobility.

A.4 The financial costs come in paying for crime, school exclusions, drug misuse and unemployment, and in lost tax revenue. Businesses also suffer from a less skilled workforce, lost customers and markets, and -- like the rest of the population -- have to pay the tax bills for social failure.

Appendix III

Promoting Financial Inclusion

A. Background

A.1 The United Kingdom (UK) government has been actively promoting social inclusion to improve financial services for people living in poor neighbourhoods through encouraging greater use of banking facilities and access to a range of delivery points, for cash withdrawals and other services, whether provided by banks and other financial institutions.

A.2 The discussions on promoting financial inclusion in the past few years are summarized below.

B. British Bankers' Association's Report *Access to Current Accounts*

B.1 The British Bankers' Association (BBA) commissioned Dr Elaine Kempson, one of the UK's leading academics[53] specializing in social exclusion, examined the "unbanked" population -- who and how many they were, their experiences and needs.

B.2 The BBA published a report entitled *Access to Current Accounts* in August 1998. One of the major findings of the research was that between 6% and 9% of individuals -- about 2.5 to 3.5 million adults -- did not have a bank account. The major reasons for not having a bank account included:

(a) people who preferred a cash budget;

(b) people who had had an account before, typically closed it after a drop in income or debt problems;

(c) young people who were not engaged in regular work; and

(d) people who had been refused an account because they could not provide proof of identity or address or because they had debt problems.

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53 She worked in the Personal Finance Research Centre at the University of Bristol.

B.3 The research found that there was a need for some form of basic banking product to meet the needs of the public. The main benefits of such an account over working entirely in cash were:

(a) increased security;

(b) cheaper prices when paying by direct debit because some companies (e.g. for gas and electricity firms) charged higher prices if people paid by cash; and

(c) easier and cheaper to get funds when the person received a cheque.

C. The Office of Fair Trading's Report *Vulnerable Consumers and Financial Services*

C.1 The Office of Fair Trading (OFT) published a report entitled *Vulnerable Consumers and Financial Services* to determine who comprised vulnerable consumers and study what could be done to help the vulnerable consumers to use financial services in January 1999.

C.2 The OFT identified seven categories of the population which might be considered to be vulnerable. These seven categories were:

(a) those on low income;

(b) the unemployed;

(c) those suffering from a long-term illness or disability;

(d) those with a low level of education attainment;

(e) members of ethnic minorities;

(f) older people; and

(g) the young.

C.3 The OFT mentioned that there was a need for an account which would help consumers to manage modest resources on a tight budget. Developments in on-line services made it possible to eliminate the consumer's exposure to the risk of overdrawing and incurring substantial charges. Thus it was possible to conceive a low cost account providing money transmission services (sending and receiving). The Banking Code might be employed to specify such an account.

C.4 To help the vulnerable consumers to use financial services, the OFT recommended that banks and building societies offered a basic, on-line, low-cost account on which was not possible to incur high charges for unauthorized credit. Such accounts should be widely accessible through the existing bank branch network or at home by telephone. Post Offices were both more numerous than bank branches and more evenly distributed geographically. But high cost of present paper-based systems in handling transactions precluded such systems from delivering what vulnerable consumers needed. The provision of on-line banking services, whether on an agency basis or directly by the corporation could meet this need. Such services might be provided in conjunction with ways of reducing the administrative cost of a wide range of other transactions, including the payment of social security benefits.

D. The Policy Action Team's Report *Access to Financial Services*

D.1 In November 1998, the Treasury set up the Policy Action Team 14 (PAT 14), a mixed group of civil servants and experts, to tackle financial exclusion and examine the role of retail banks, post offices and other organizations in providing access to and delivery of financial services in deprived neighbourhoods. The report was published in November 1999.

D.2 The PAT 14 found that an important reason for financial exclusion was mismatch between potential customers' needs and the products available. Financial services providers should develop more new products that would be suitable for low income customers. The PAT 14 recommended that banks, building societies and other providers should develop and promote basic account services, in the light of the announcement on the future benefit payment system and the future of Post Office Counters services.[54]

D.3 The PAT 14 concluded that banks and building societies could promoting the use of Basic Bank Accounts in order to extend banking services to low-income households. The proposed features of a Basic Bank Account were:

(a) income (including welfare benefit payments) paid in Automated Credit Transfer (ACT);

(b) cheques and cash paid in by the account holder;

(c) cash out at convenient access points;

[54] The UK government planned to computerize the network of post offices by the end of 2003 and to pay welfare benefits by automated credit transfer by the end of 2005. Paying welfare benefits the new way would increase the demand for financial services. Computerization would provide a platform for the Post Office to be an alternative delivery channel for the community.

(d) bill payment by direct debit, credit transfer or budget account, linked to the account;

(e) no cost to the customer for everyday transactions; and

(f) no risk of unauthorized overdraft.

D.4 The following were desirable additional features:

(a) debit card for shop purchases; and

(b) modest agreed buffer zone facility, i.e. free overdraft for a small amount and limited duration, so that, for example, people could withdraw cash from an automated teller machine (ATM), even if they had less than £10 (HK$118) in their account.

E. British Bankers' Association's Report *Promoting Financial Inclusion*

E.1 The British Bankers' Association (BBA) published another report entitled *Promoting Financial Inclusion* in April 2000 reviewing the work of the banking industry in promoting financial inclusion. The report also covered some of the changes that the banking industry was undergoing and identified the need for partnerships between the banking industry, the public sector and voluntary organizations to tackle key challenges in promoting financial inclusion. It also included the first review of the current availability of Basic Bank Accounts and indications of the average cost of setting up and running such accounts. Some of the major findings are summarized below.

<u>Promoting Financial Inclusion</u>

E.2 The BBA mentioned that the UK government had put promoting financial inclusion near the top of its policy agenda. The crux of the matter was to try to ensure that a range of appropriate financial services was available to everybody. It meant helping the public to understand and to access those services. Banks were making progress to promote financial inclusion. The BBA identified some areas for particular attention in the future:

(a) continued work on the development of Basic Bank Accounts so that there was a wide availability of such accounts by the end of year 2000;

(b) promoting adult financial literacy and partnerships between banks and other organizations so that people without accounts were aware of how a Basic Bank Account could help them; and

(c) helping all groups in the society to benefit from the new delivery channels.

<u>Costs of Operating a Basic Bank Account</u>

E.3 The report indicated that Basic Bank Accounts could bring benefits to a lot of people. However, to be sustainable, a Basic Bank Account needed to be cost effective -- "basic" did not mean costless to the bank. The vast majority of customers paid no bank charges for their day-to-day banking businesses if they did not run up an unauthorized overdraft, had none of their cheques bounced and used one of the free cash machines provided by their bank. Thus one important way for a bank to recover the cost of providing an account was to invest the idle balance remaining in the account at a higher rate of interest than was paid on that balance. This might be particularly important if there was little chance of cross selling other products or services to the customer.

E.4 Data the BBA obtained by from banks in 1998 estimated that it might cost up to £80 (HK$944) per customer to set up a basic account and about £70 (HK$826) per annum to maintain it. The costs included producing plastic card(s) for operating the account, processing cash withdrawals, operating direct debits, dealing with queries, postage and a share of overheads. Those figures suggested that the average daily balance needed to cover just the annual costs would be almost £1,300 (HK$15,340).

Appendix IV

Federal Trade Commission

A1. The Federal Trade Commission (FTC) is an independent administrative agency which was organized in 1915 pursuant to the Federal Trade Commission Act of 1914. Under this Act, the Commission is empowered to:

(a) prevent unfair methods of competition, and unfair or deceptive acts or practices in or affecting commerce;

(b) seek monetary redress and other relief for conduct injurious to consumers;

(c) prescribe trade regulation rules defining with specificity acts or practices that are unfair or deceptive, and establishing requirements designed to prevent such acts or practices;

(d) conduct investigations relating to the organization, business, practices, and management of entities engaged in commerce; and

(e) make reports and legislative recommendations to Congress.

A2. The FTC is composed of five members appointed by the US President and confirmed by the Senate for terms of seven years.

A3. The Commission comprises the following principal units: Office of the Executive Director; Office of the General Counsel; Office of the Secretary; Office of the Inspector General; Office of Administrative Law Judges; Bureau of Competition; Bureau of Consumer Protection; Bureau of Economics; and the regional Offices.

Source: 16CFR, Commercial Practices, Chapter I, Federal Trade Commission, Part 0 - Organization, http://ecfrback.access.gpo.gov
Federal Trade Commission, *Statues Relating to Both Missions*, http://www.ftc.gov/ogc/stat1.htm

Appendix V

A Summary of Consumer Protection and Civil Right Laws Relating to Consumer Finance

A. Disclosure Laws

Truth in Lending Act (Federal Reserve Regulation Z)

A.1 This Act requires accurate disclosures of interest rates and finance charges so that loan applicants can comparison-shop for a mortgage or other consumer loan.

Consumer Leasing Act of 1976 (Federal Reserve Regulation M)

A.2 This Act specifies requirements for disclosures relating to consumer leasing.

Real Estate Settlement Procedures Act of 1974 (Regulation X of the Department of Housing and Urban Development)

A.3 This Act requires lenders to inform borrowers of mortgage loan settlement charges.

Electronic Fund Transfer Act (Federal Reserve Regulation E)

A.4 This Act establishes the rights, liabilities and responsibilities of parties in electronic fund transfers (EFT) and protects consumers using EFT systems.

Expedited Funds Availability Act of 1987 (Federal Reserve Regulation CC)

A.5 This Act specifies when a bank must make available to its customer funds from items deposited into the customers transaction account. It provides requirements for disclosure of the bank's funds availability policies to its customers.

Truth in Savings Act (Federal Reserve Regulation DD)

A.6 This Act requires institutions to disclose fees, interest rates and other account terms so that consumers can compare the terms and conditions in respect of deposit accounts offered by different institutions.

B. Civil Right Laws

Equal Credit Opportunity Act (Federal Reserve Regulation B)

B.1 This Act promotes the equal availability of credit to all credit-worthy applicants, regardless of such factors as age, race, colour, religion, national origin, sex and marital status.

Fair Housing Act of 1968

B.2 This Act prohibits discrimination in the sale or rental of housing and in any part of a credit transaction involving housing.

Home Mortgage Disclosure Act of 1975 (Federal Reserve Regulation C)

B.3 This Act requires that regulated lenders report annually on their mortgage-related activity as a way to detect possible lending discrimination.

Community Reinvestment Act of 1977

B.4 This Act encourages federally-insured lenders to help meeting the credit needs of their communities, especially the needs of low- and moderate-income neighbourhoods or persons, small businesses and small farms.

C. Other Consumer Credit Laws

Fair Credit Reporting Act of 1970

C.1 This Act establishes procedures for correcting mistakes on a consumer's credit file and requires that a credit file only be provided for legitimate business purposes.

Fair Debt Collection Practices Act of 1977

C.2 This Act is designed to eliminate abusive and deceptive debt collection practices and to ensure that reputable debt collectors are not competitively disadvantaged.

Unfair or Deceptive Acts or Practices (Federal Reserve Regulation AA)

C.3 This Act deals with unfair and deceptive practices. It prohibits a lender from taking a non-possessory security interest in household goods, except on a purchase money loan.

National Flood Insurance Act of 1968

C.4 This Act sought to accomplish two objectives. These include making flood insurance available to residents of flood-prone areas at reasonable rates and encouraging local governments to enact land use restrictions that limit future development in flood-prone areas.

Home-owners Protection Act of 1998

C.5 This Act is designed to eliminate inequities in the maintenance of private mortgage guaranty insurance.

Right to Financial Privacy Act of 1978

C.6 This Act creates a legal interest that customers may enforce against federal agencies or employees seeking their financial records.

Title V of Gramm-Leach-Bliley Act

C.7 This Act establishes a set of rules to govern the protection and disclosure of consumer financial information by institutions.

Source: Kenneth Spong, *Banking Regulation, Its Purposes, Implementation, and Effects, Division of Supervision and Risk Management*, Federal Reserve Bank of Kansas City, 5th ed., 2000

Appendix VI

Federal Reserve System

A.1 The Federal Reserve System (Fed) is the central bank of the US. It is constituted of a Board of Governors and 12 regional Reserve Banks. The main duties of the Fed are listed as follows:

(a) Conducting the nation's monetary policy by influencing money and credit conditions in the economy in pursuit of full employment and stable prices;

(b) Supervising and regulating banking institutions to ensure the safety and soundness of the nation's banking and financial system and to protect the credit rights of consumers;

(c) Maintaining the stability of the financial system and containing systemic risk that may arise in financial markets; and

(d) Providing certain financial services to the US government, to the public, to financial institutions, and to foreign official institutions, including playing a major role in operating the nation's payments system.

Appendix VII

Office of the Comptroller of the Currency

A.1 The Office of the Comptroller of the Currency (OCC) is a bureau of the Department of the Treasury. The Comptroller of the Currency is appointed by the US President and confirmed by the Senate for a term of five years. The principal function of the OCC is to regulate the national banking system and agencies of foreign banks.

A.2 In regulating national banks, the OCC has the power to:

(a) examine banks;

(b) approve or deny applications for new charters, branches, capital, or other changes in corporate or banking structure;

(c) take supervisory actions against banks that do not comply with laws and regulations or that otherwise engage in unsound banking practices. The OCC can remove officers and directors, negotiate agreements to change banking practices and issue cease and desist orders as well as impose civil money penalties; and

(d) issue rules and regulations governing bank investments, lending and other practices.

Appendix VIII

Federal Deposit Insurance Corporation

A.1 The Federal Deposit Insurance Corporation (FDIC) is a federal government agency managed by a five-member board of directors appointed by the US President and confirmed by the Senate.

A.2 The FDIC provides insurance protection for depositors at most US banks. It also supervises and examines insured state-chartered banks which are not members of the Federal Reserve System.

A.3 The FDIC has a variety of enforcement powers to carry out its bank supervisory and deposit insurance responsibilities. These powers include the ability to terminate deposit insurance at insured institutions and to issue cease and desist orders, remove bank officials and other affiliated parties, and levy fines on state non-member banks.

Appendix IX

Office of Thrift Supervision

A.1 The Office of Thrift Supervision (OTS) is a bureau of the Department of the Treasury and is the primary regulator of all federally-chartered and many state-chartered thrifts. OTS is headed by a Director who is appointed by the US President with the Senate's confirmation.

A.2 OTS is responsible for chartering, examining, supervising and regulating federally-chartered and state-chartered thrifts belonging to the Savings Association Insurance Fund[55].

[55] The Savings Association Insurance Fund is one of the two federal deposit insurance funds administered by the FDIC. The other fund is the Bank Insurance Fund.

Appendix X

Provisions and Effects of the Depository Institutions Deregulation and Monetary Control Act of 1980

Provision	Effect
Phases out deposit interest ceilings	Interest rate ceiling on deposits is to be phased out over a period of 6 years. A depository institutions deregulation committee was set up to do this.
Nationwide NOW accounts permitted	Any depository institution after 31 December 1980, was allowed to offer NOW accounts; that is, interest-bearing checking accounts to individuals and nonprofit organizations. Automatic transfer services (ATSs) were also allowed in all commercial banks. Savings and loan associations can use remote service units, and credit unions that are federally insured can offer share draft accounts (CUSDs).
Reserves required on all transactions accounts at depository institutions	Gradually, reserve requirements are to be uniformly applied to all transactions accounts which are defined as demand (checking) deposits, NOW accounts, ATS accounts, and credit union share drafts. This required reserve system is to be phased in over 8 years for all depository institutions that are not Federal Reserve members. For Federal Reserve members, the act meant a reduction in reserve requirements; those reductions would be phased in over 4 years.
Increased access to the discount window	All depository institutions issuing transactions accounts and non-personal time deposits now have the same borrowing privileges at the Federal Reserve discount window just as if they were member commercial banks.
Fees established for Federal Reserve services	A fee schedule for the Federal Reserve "chores" such as check clearing and collection, wire transfers, and the like was to be established by Oct. 1, 1981.
Power of thrift institutions expanded	Federally insured credit unions were allowed to make residential real estate loans. Savings and loan associations had higher loan ceilings and some ability to make consumer loans, and the power to issue credit cards.
The imposition of supplemental reserves	The Federal Reserve Board, under extraordinary circumstances, can impose additional reserve requirements on any depository institution of up to 4 percent of its transactions accounts. This supplementary reserve, if imposed, must earn interest.
Increased level federally insured deposits	Previously, federally insured deposits had a ceiling of US$40,000; that ceiling was increased to US$100,000.

Source: OCC, *A History of Depository Institution Regulation in the United States,* http://occ.awlonline.com/bookbind…medialib/download/ect/ect15a.htm

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