

Meeting on Panel of Financial Affairs (FAP) on 5th May 2008 - Agenda Item IV

Submission by The Hong Kong Association of Banks (HKAB)

The purpose of this submission is to share with FAP the further study by HKAB on various issues relating to banking services discussed at the FAP meeting on 2 April 2007 and last updated to FAP on 31 August 2007.

HKAB observes a continuing trend of rising popularity of the Internet and other electronic channels for accessing banking and financial services while at the same time a steady growth of bank outlets including branches, ATMs and self-service centres since our last update.

HKAB appreciates the focus of FAP discussions was on how all the parties concerned could work together to explore and enhance access to basic banking services by people without sufficient IT skills including the elderly living in public housing estates. From the same perspective, the banking industry has been joining hands with other stakeholders to make basic banking services, including cash withdrawal services, even more convenient for the target groups of customers.

In parallel, HKAB has requested the Task Force on Financial Service Delivery Channels¹ and the Technical Operations Committee² to further explore a number of suggestions raised at the 2 April 2007 FAP meeting. In undertaking the study in light of overseas experience vis-à-vis the local environment of Hong Kong, the subgroups seek to strike a balance between the objective to help certain target groups adapt to automated channels and the need to ensure millions of customers continue to enjoy highly convenient banking services through various channels familiar to them. HKAB endorses the collective views as summarised below.

1. Assisting customers to switch bank accounts

- 1.1 Every one has a responsibility in ensuring that Hong Kong is kept clean of money laundering and terrorist financing through the banking system. Banks need to comply with the “Know Your Customer” (KYC) requirements of the Hong Kong Monetary Authority in providing banking services and cooperation of customers is required in providing the relevant information and documentation upon applying for a new account.

¹ The Task Force was set up by HKAB in February 2006 to explore alternative channels to enhance access to basic banking services by target groups of customers. Besides the 8 bank representatives nominated by HKAB, the Task Force has also one representative each from the Hong Kong Monetary Authority and the Financial Services and the Treasury Bureau.

² The Technical Operations Committee is a forum for member banks of HKAB to consider matters relating to interbank payment clearing and settlement as well as other technical developments affecting the industry. It has 10 bank representatives, including a number of the more active consumer banks.

- 1.2 It is fairly simple and easy for private individuals to switch their bank accounts in Hong Kong. Before account switching, it is important that appropriate arrangements are in place to direct any regular receipts or payments (including loan and credit card repayments) made through these accounts to the new account in order not to miss any pre-arranged regular payments or receipts.
- 1.3 Banks provide a variety of services in helping customers to make or receive regular payments efficiently. To use such service, customers may initiate the standing instructions directly through their own bankers or via the creditor (i.e. the service provider) with authorisation from the customer concerned.
 - 1.3.1 Auto-credit payment. After an account is successfully set up, it is very straight forward for the beneficiary customers to arrange for receiving regular payments like salary, dividend payment of listed securities and social security allowances etc. via their bank accounts by simply providing their account details to the party initiating the payment. It generally takes less than one week for the banker of the initiating party to establish an autocredit instruction.
 - 1.3.2 Autodebit instruction and direct debit authorisation (DDA). It is equally simple for banks to set up instructions for customers to make regular payments like utilities bills, school fees, management fees of a property etc. from their designated bank accounts. Customers may either set up their own autodebit instructions with their bankers direct, or arrange it through the service provider by giving a DDA to the service provider to debit the payment from the designated accounts regularly. We note that DDA is more commonly used by utilities companies. It may take more time, generally between 2 – 4 weeks, to put these autodebit instructions into effect, depending on the processing time required by the creditor. However, it is quite common that loan repayments, such as mortgage and credit card repayments through the borrower's account maintained with the lending bank are not treated as autodebit, but are effected simply as book transfer between the customer's and the lending bank's account.
- 1.4 All successful transactions via the above mentioned standing instructions are recorded in the bank statements, passbooks etc. However, there are different practices of banks on whether the name of creditor and/or initiating party are recorded in the bank statement or passbook. For some banks, the name of the creditor for each autodebit, including DDA, transaction is shown on the passbook or statements but not the name of the initiating party of the autocredit transaction.

- 1.5 When approached by a customer to close a bank account, it is normally the practice of the bank to remind the customer to review whether there are any standing instructions for regular payments or regular receipts made through the account to be closed by going through past bank statements, and if so, make appropriate arrangements in advance to avoid the risk of rejected transactions and attendant handling charges.
 - 1.6 The additional steps mentioned in 1.5 above add value to customer service and minimise potential customer enquiries and complaints. Through a circular issued on 11 April 2008, HKAB has encouraged all member banks to adopt the good practice by reminding customers to re-establish or cancel the standing instructions by going through recent bank statements or passbooks as necessary. The guideline also encourages member banks to provide a list of the autodebit, DDA and autocredit details upon request by customers. Note, as mentioned in 1.4 above, the beneficiary bank might not have details of the party which initiated the autocredit instructions.
2. Depositing cheques through any ATM within a particular ATM network or drop box of any bank
 - 2.1 Banks keep enhancing their services and have been making available more self-servicing machines like cheque deposit machines, cash deposit machines and bank book updating machines for their customers. Cheque deposit machines are welcome by many customers who are provided with a receipt in confirmation of the deposit of each cheque.
 - 2.2 As general customer behaviour changes over time and with the emergence of other channels accepting cheque deposit, ATMs are now primarily serving customers to make cash withdrawal, balance enquiry, fund transfer, bill payment etc. While most commonly used model of ATMs no longer accept cheque deposit, it is noted that there are a few older ATMs still offering such function.
 - 2.3 The above-mentioned channels refer to the deposit of a cheque by a customer with his / her banker. The suggestion of allowing a customer to deposit a cheque with a third party bank (i.e. a bank with which the individual does not have an account relationship) through any ATM or drop box involves a number of challenges, highlighted as follows:
 - 2.3.1 The suggestion would involve more intermediaries and additional steps and would thus necessarily lengthen the process flow as additional time would be incurred in sorting and sending the cheques to the relevant payee bank, extending the clearing and settlement window of these cheques. Currently, the payee of a cheque receives interest from the same day of deposit of the cheque with his banker and has the good funds available on the next working day. Service degradation in terms of interest loss and delay in receiving good funds might be a major issue for many customers who have been enjoying the convenience of banking services.

2.3.2 The intermediary bank, not being a collecting or drawee bank, does not have the mandate from the cheque depositor to deal with the cheque. In addition, a detailed review of the current laws of banking is required in understanding the potential legal liability of the banks and customers concerned.

2.3.3 Unlike a cheque deposit machine which issues a receipt to the depositor, a person who has deposited a cheque through a cheque deposit box has no 'audit trail' to make enquiries on the cheque status in case of need. Furthermore, the individual's bank account information must be disclosed to the intermediary bank.

3. Movable bank branches (Mobile banks)

3.1 Delivery channels for banking and financial services have been evolving in keeping up with the constant changes in the market. Helped by advances in technology, there is a clear global trend of migration towards automated delivery channels given their distinct advantages including 7x24 availability to the customers and their effectiveness in serving a large customer base at the same time. Hong Kong as an international financial centre is of no exception in the growing usage of automated channels. In contrast, it is noted that in the U.K. which has limited adoption of mobile branches, the effectiveness of such delivery channel is being re-evaluated in view of declining transactions through that channel, the ease of substitution of the transaction types which were conducted through mobile branches with standing order, direct debit, Internet and automatic transaction machines, lack of interviewing room or privacy to engage in more complicated customer enquiries etc.

3.2 Channel development strategy and new product and services development forming part of the banks' competition strategy should remain a commercial matter for individual banks. If individual banks are interested in providing bank services through movable bank branches, they will need to satisfy the physical security (for both customers and bank staff), systems and other relevant requirements in opening a bank branch.

4. Biometric authentication as substitute to PIN for accessing ATMs

4.1 The need to memorise and input a PIN is perceived as a potential hurdle for elderly and inexperienced customers in accessing ATMs for basic banking services. While biometric technologies are being sparsely adopted as authentication for certain applications such as physical access control by staff to gain entry to an office, overseas experience has shown that they are still very much at an infancy stage as a substitute for PIN in accessing ATMs.

- 4.2 Up till now, biometric authentication for accessing ATMs is yet to be adopted in mature markets like U.S. and U.K. because of reliability and effectiveness issues as well as sociological concerns throughout society such as potential physical harm of the technology to the individual, risk of misuse of biometric information etc.
- 4.3 Based on our desk-top research, the use of biometric authentication in the following countries is still in an experimental stage on a limited scale:
- 4.3.1 In Japan, as a physical security measure against serious fraud problems besetting ATMs in the country, the pilot bank used palm vein pattern of the customer as the biometric identifier for making cash withdrawal services through specially equipped ATMs, in addition to requiring the customer to input a PIN code.
- 4.3.2 In Columbia, as a physical security measure against theft, the pilot bank used the customer's fingerprint biometrics, as an alternative to PIN, in accessing ATMs located in mountains and jungles, where a high error rate of almost 30% was detected initially and currently stood at around 8%.
- 4.3.3 India has been considering a pilot programme to fight corruption problems by installing 15 fingerprint-reading ATMs at "village kiosks" in five districts across southern India.
- 4.4 In Hong Kong, there are over 12 million bank cards with ATM functions with a daily average of 500,000 ATM transactions. Many of the ATMs are located outside bank premises, used by customers day and night. ATM is an efficient delivery channel as revealed in a recent survey of HKAB³. It is possible that the adaptation of the biometric technology in ATM usage may become more widely accepted for a large customer base over time after overcoming the relevant issues, including privacy concerns about collection, access, storage and use of additional personal information. While banks in Hong Kong are committed to monitoring technology development, it is likely that PIN-based access to ATMs will continue to be the well-adapted and efficient authentication method in the near term.

25 April 2008

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³ According to a recent study on ATM services in Hong Kong by the research team of the University of Hong Kong for HKAB, over 80% of all the 1,006 interviewees considered ATM services convenient.