

4 SUPERVISION OF INSTITUTIONS' CONDUCT



19th century mantel clock. Banco de España collection.

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Supervision of institutions' conduct is not included in the remit of the SSM. In consequence, the Banco de España supervises the conduct of all credit institutions that provide their services in Spain and of other supervised institutions.

Protecting bank customers is a fundamental objective for the Banco de España. It is, in addition, essential to safeguard public trust in the banking system and to prevent the risk associated with a general loss of public trust. In consequence, supervision of conduct by the Banco de España plays a key part in fostering the good functioning and stability of the financial system.

Together with the specific functions of oversight and inspection of conduct rules on transparency and consumer protection, the Banco de España performs other closely related functions, such as promoting good market practice or handling enquiries and resolving complaints and claims made by banking service users. Analysis of the numbers, trends and content of claims is one of the most valuable sources of information for the supervision of conduct. Indeed, certain actions taken that led to disciplinary measures being adopted arose from infringements detected through claims filed by banking service users.

In 2017 conduct risk scoring was applied to institutions.¹ This helps to establish supervisory priorities and to draw up the annual action plan. To assist with this task and with the pursuit of supervisory activity, work was carried out throughout the year on the design and creation of a new IT tool.

4.1 Conduct-related supervisory activity

Supervisory activity in 2017 comprised actions included in the annual plan and others that were unscheduled. Given the inherent characteristics of conduct-related supervisory activity, it is only natural that unscheduled supervisory needs will arise, either as a result of matters reported to the Banco de España by individuals or public or private bodies, or when certain practices are observed at institutions that are deemed to require immediate and specific supervisory action, brought to light by a claim or by regular monitoring of institutions.

Supervisory actions, planned or unplanned, carried out in 2017 comprised on-site inspections (thorough analysis of a specific matter at a specific institution) and other off-site supervisory monitoring (actions on varying scales, which may range from occasional limited monitoring at a specific institution to horizontal actions at several institutions).

In addition, 2017 saw the start of continuous monitoring of institutions' conduct, at an individual or aggregate level, according to the importance and conduct risk scoring of each institution.

Table 4.1 presents the details of the supervisory actions taken in 2017 and Figure 4.1 an overview of the main supervisory activities.

¹ This scoring is calculated using parameters relating to each institution's conduct category (market share, type and provision of banking services to individuals) and market conduct risk profile. For more details, see Chapter 4 of the *2015 Report on Banking Supervision in Spain*.

Number		
By type	Inspections (a)	Off-site monitoring (b)
Mortgages		
Mortgages (transparency)	34	4
Mortgages (Code of Good Practice)	1	26
Consumer loans	0	5
Advertising	1	168
Other (capital contributions credit cooperatives, ATMs, financial reporting to SMEs, customer service departments, transparency)	1	20
TOTAL	37	223
<i>of which unplanned</i>	8	45

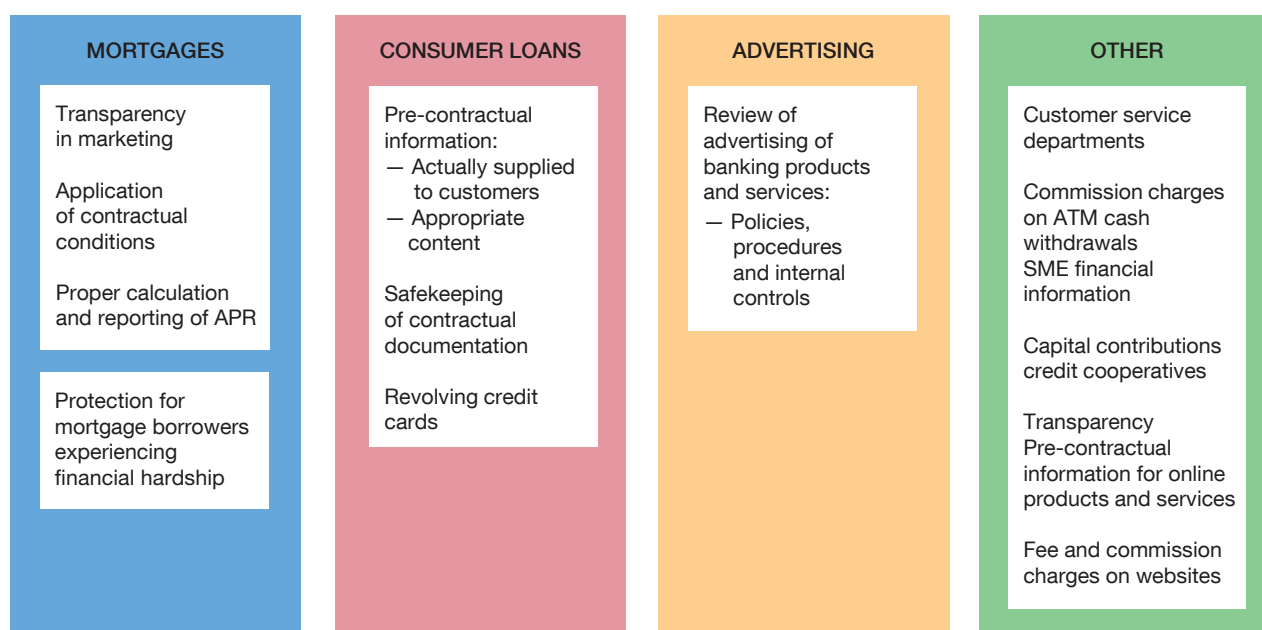
SOURCE: Banco de España.

a Of these inspections, 24 were initiated before the beginning of 2017.

b Of these off-site monitoring activities, 93 were initiated before the beginning of 2017.

OVERSIGHT OF CONDUCT: MAIN AREAS OF ACTIVITY

FIGURE 4.1



SOURCE: Banco de España.

4.1.1 MORTGAGE LENDING

Purchasing and paying for a home is one of the key milestones in a person's life. For this reason, one of the Banco de España's priority objectives is to ensure transparency in the marketing of mortgage loans.

Work was undertaken in 2017 to conclude the eight ongoing on-site inspections on mortgage lending, involving supervising correct compliance with the regulations on the pre-contractual and contractual information to be provided at the different stages of the marketing of mortgage loans and of their arrangement, settlement and payment. These inspections, which began in 2015, have reviewed a significant sample of Spanish households' residential mortgage loans. Another four inspections on mortgage lending were opened in the year.

All these actions included verification, among other aspects, of:

- i) the content of the pre-contractual information and contractual documentation;
- ii) calculation of the APR established in the pre-contractual and contractual documentation;
- iii) application of the contractual terms, such as, for example, correct setting of the interest rate agreed or correct calculation of the regular instalments;
- iv) application of the system for substitution of official benchmark indices; and
- v) calculation of mortgage closure or early repayment fees.

In addition, six inspections were opened on transparency in the marketing of mortgage loans and, in particular, on the adequacy of the pre-contractual information and calculation of the APR.

4.1.2 MEASURES TO PROTECT MORTGAGORS EXPERIENCING FINANCIAL HARDSHIP

Protecting mortgagors experiencing serious economic difficulties is also a priority for the Banco de España. Accordingly, in 2017 supervisory efforts continued to be devoted to checking that the Code of Good Practice (CGP) contained at annex to Royal Decree-Law (RDL) 6/2012 of 9 March 2012 on urgent measures to protect mortgagors experiencing financial hardship was being correctly applied by its signatory institutions. The CGP contains a series of measures, which are mandatory for the signatory institutions, to allow restructuring of mortgage debts in the case of borrowers who are experiencing extraordinary difficulties meeting their mortgage payments and who satisfy

BANKING REGULATION AND DISCIPLINE LEGISLATION, RDL 6/2012

FIGURE 4.2

Obligations	Most common incidents detected in recent years
<p>Art. 5.9 Information on the CGP Institutions must provide appropriate information on the existence of the CGP and the possibility of having recourse to the CGP measures. This information must be made available through the branch network, to all customers, and in writing to customers who have failed to meet any loan repayments or who have payment difficulties.</p>	<ul style="list-style-type: none"> – Proactive information on the CGP is not provided. – Written information on the CGP is not provided. – Requests are not dealt with diligently (delay in information on whether or not the documentation presented is complete). – Delays in attending to requests. – Incorrect analysis of the documentation presented. – Deficient information on the different CGP measures and the fact that they are successive measures.
<p>Art. 5.4 Application of the CGP When a customer certifies that he/she has reached the exclusion threshold, the institution must apply the CGP measures (restructuring or reduction of loan or dation in payment) from that point in time.</p>	<ul style="list-style-type: none"> – The restructuring plan is not notified and offered within one month from presentation of the request for application of the CGP. – The restructuring plan specifying the financial consequences for the customer is not provided. – Information on the complementary measures available if the restructuring plan is inviable is not provided. – The measures are not applied from the date of declaration of the exclusion threshold. – Novation costs are passed on to the customer when it is the institution that requests the recording as a public deed.

SOURCE: Banco de España.

certain conditions that place them on the exclusion threshold defined in the legislation. Broadly speaking, signatory institutions shall i) proactively inform their customers of the existence of these measures and the possibility of their having recourse to them, and ii) apply the measures without delay to borrowers who demonstrate that they meet these conditions.

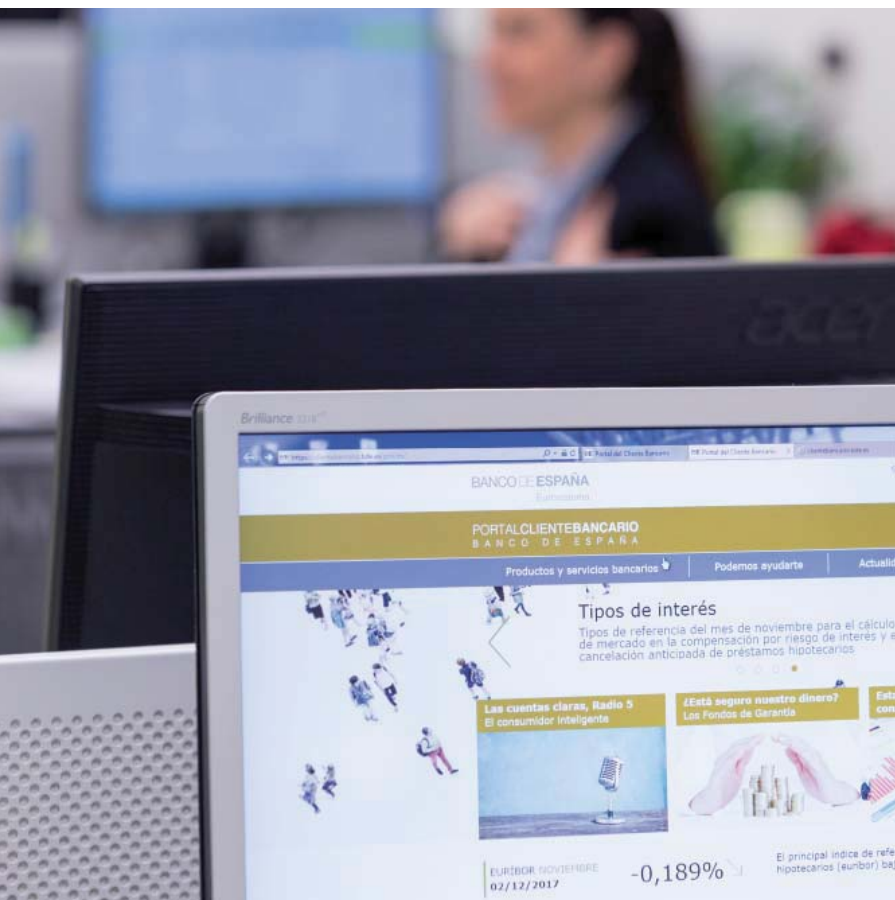
Figure 4.2 summarises the most common incidents detected in recent years relating to application of RDL 6/2012.

4.1.3 CONSUMER LENDING

It is vital that customers are aware of the conditions and risks they assume when they purchase a bank product. This is especially important in the case of consumer loans or credit, since neither the lower amounts involved nor the immediacy of obtaining the loan or credit is conducive to reflection.

In consumer lending the Banco de España's powers are limited to verifying that the institutions under its supervision comply with the regulatory and disciplinary rules. In consequence, it does not enter into other matters such as, for instance, assessing whether contractual terms are unfair, or monitoring loans or credit granted by other firms that are not under its supervision (non-supervised firms are free to grant consumer loans as it is not a restricted activity).

In 2017 this activity focused on verifying that supervised institutions effectively provided pre-contractual information to customers and that this information was clear and transparent, especially in the case of revolving credit.



Portal for Banking Customers.



Market Conduct and Claims Department.

Advertising by supervised institutions plays an essential role in the marketing of banking products and services, as it is frequently the first contact with potential customers and is a key factor in generating customer expectations.

In 2016 horizontal supervisory monitoring of advertising was begun in institutions within the scope of application of Ministerial Order EHA/1718/2010 of 11 June 2010 on regulation and control of advertising of banking products and services, and of Banco de España Circular 6/2010 of 28 September 2010 to credit institutions and payment institutions on advertising of banking products and services.

These regulations encourage self-regulation by institutions and are based, on one hand, on prevention measures, through internal controls and procedures, and on the other on corrective measures, through subsequent review by the supervisor of samples of the advertising material, which allow any misconduct to be corrected. These review measures by the Banco de España have been stepped up considerably in recent years.

In a first stage, all institutions covered by the above-mentioned regulations (312 in total) were asked to provide their internal advertising records, to allow the supervisor to verify that they were compliant with the regulations and to ascertain the actual volume of advertising.

In a second stage, institutions that were effectively pursuing advertising activities (170) were analysed, focusing on the following

aspects: i) that internal advertising records were being kept correctly; ii) that the advertising was compliant with the regulations; and iii) that an appropriate commercial communication policy, procedures and controls were in place. As a result, 113 requirement letters (containing 326 individual requirements), 30 recommendation and comment letters and a further 24 other letters were sent.

The most common shortcomings identified were: i) incomplete internal records not consistent with the advertising reported; ii) advertising not fully compliant with the relevant regulations; and iii) shortcomings relating to the commercial communication policy document, which at some institutions did not exist and at others was very deficient or severely lacking.

In short, the supervisory assessment revealed the need for institutions to pay more attention to their advertising activity and seriously reconsider the division of functions and coordination between the marketing and the regulatory compliance areas, conferring on the latter the necessary importance in this respect. In addition, management bodies should become closely involved in the processes of approval and updating of their advertising procedures and controls, with audit plans necessarily in place for this control function.

The Banco de España intends to continue to oversee all advertising and to increase the volume of advertising actually reviewed.

Most revolving credit is extended in the form of cards and is generally offered to provide quick access to liquidity. Given their financial terms, default on these cards can lead to a build-up of interest and expenses, making it difficult for the debt to be repaid and resulting in debt overhang and, ultimately, financial exclusion for the borrower.

To facilitate daily life's typical financial calculations, and specifically those required for revolving credit, the Banco de España's website has a simulator that enables consumers to calculate when the last payment will be due on a revolving card. It also has other simulators which, for example, allow consumers to calculate loan instalments and obtain loan repayment schedules (<https://clientebancario.bde.es/pcb/es/>).

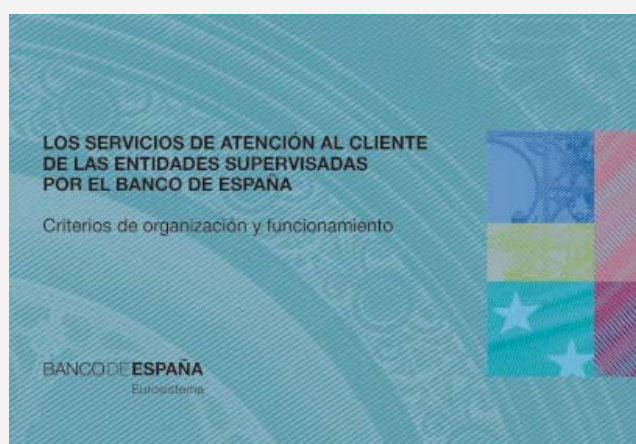
4.1.4 ADVERTISING

A key aspect of supervisory activity in 2017 was the review of bank product advertising, to verify and ensure that advertising was truthful, clear and concise. Box 4.1 describes the supervisory monitoring of advertising carried out in 2017, in the framework of actions begun in 2016.

4.1.5 OTHER SUPERVISORY ACTIONS

Supervisory actions in other areas in 2017 included, in particular, the following:

- i) reviewing the correct functioning of customer service departments, described in Box 4.2;



institutions supervised by the Banco de España (*Adenda: Los servicios de atención al cliente de las entidades supervisadas por el Banco de España*) listing good practice criteria for the organisation and functioning of customer services at supervised institutions.

The underlying basis for these criteria is that institutions' CSDs are understood to be control bodies that play a vital role in their respective organisations. Thus, CSDs should not simply handle and settle claims, but should also play a key role alongside institutions' various other control bodies, in order to ensure correct risk control, prudent business conduct and compliance with legislation, regulations and supervisory requirements and with internal policies and procedures, located at the second line of defence in the three lines of defence model.

As a result of the supervisory measures taken in recent years to verify the correct functioning of customer service departments (CSDs), the 2016 *Memoria de Reclamaciones* (Claims Report, available only in Spanish) included an addendum on CSDs at

From this privileged position, CSDs should be a source of important information, an early warning mechanism for the early detection of problems, enabling any such problems to be corrected or prevented by institutions' governing bodies.

- ii) verifying that obligations relating to ATM cash withdrawal charges were being met, for which purpose the information provided through banks' ATMs was monitored *in situ*, together with the procedures used by banks to notify changes in the charges they pass on to their customers who make cash withdrawals from other banks;
- iii) verifying that institutions were complying with their obligations to provide information on the financial situation and payment history of SMEs and self-employed persons (through the "SME-Financial Information" document);
- iv) reviewing the transparency of the information provided in the marketing of contributions to the capital of credit cooperatives;

SUPERVISORY MEASURES ADOPTED IN 2017

TABLE 4.2

Number	Inspections (a)	Off-site monitoring (b)
Initiation of penalty procedures	5	1
Letters of requirements	8	114
Recommendation and observation letters	8	226
Other letters	0	81
Other actions concluded not involving letters	1	14
TOTAL	22	436

SOURCE: Banco de España.

- a The eight requirements letters contain 68 specific requirements for the institutions. In addition, there are five completed inspections for which the adoption of supervisory measures has yet to be formalised.
- b The 114 requirements letters contain 330 specific requirements for the institutions.

- v) verifying the pre-contractual information provided by institutions offering bank products that may be acquired online or through mobile apps; and
- vi) monitoring that institutions comply with the transparency requirements relating to information provided on their websites on interest rates and fees and commissions.

4.2 Supervisory measures

In 2017 the Banco de España initiated six conduct-related penalty procedures, five of which arising from on-site inspections on mortgage lending and one from supervisory monitoring of the correct application of the CGP. Also, 122 requirement letters and 234 recommendation and comment letters were sent, seven of each relating to inspections on mortgage lending. Table 4.2 shows the type of measures adopted in the procedures concluded in 2017.