

# FINANCIAL SUPERVISION IN EUROPE

## Consumer perspective

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## Summary

BEUC is very disappointed that in its communication on the EU financial supervisory structure the Commission has once again totally forgotten the conduct-of-business side of supervision despite the fact that links between prudential supervision and consumer protection in financial services area are so obvious.

First, we provide the examples of national experiences in terms of financial supervision and consumer protection. These examples are provided with an objective to draw the lessons from the past.

Then, BEUC's concrete suggestions on the improvements needed in financial supervision at national and EU level, to take into account the consumer perspective, are presented. Our suggestions are as follows:

1. More powerful and independent national supervisors are needed in every Member State. Reflection should be launched on the necessity to separate prudential supervision on the one hand and control of methods of marketing and professional compliance on the other.
2. In order to provide better protection to consumers, national supervisory bodies should fulfill the following functions: participate in advertising control, control of financial information, unfair practices, distribution of financial products, etc.
3. A unique supervisor is needed to cover all financial services and all financial institutions. Therefore, there is a need to merge existing national supervisory authorities (bank/non bank credit, insurances, securities/pensions funds).
4. Better consumer representation on the boards of financial supervisors should be ensured. For this purpose, consumer representatives should be provided with necessary means.
5. Strengthen the cooperation between national supervisors and regulators
6. Create a centralised EU financial supervision authority in charge of control of financial institutions operating at cross-border level, whatever there size is.
7. Make the legislation more coherent to avoid regulatory arbitrage between financial products.
8. Adopt binding rules at EU level so that all Member States are obliged to comply with them

## Introduction

Prudential supervision and conduct-of-business supervision (consumer protection) are tightly interlinked. If prudential measures fail, it would be rather difficult to protect consumers who make deposits, borrow money, plan their future, etc. In the same vein, poor marketing practices and toxic products cause major problems to consumer interests and can represent a significant prudential risk. Nevertheless, the objectives of prudential supervision and consumer protection are not identical and might be subject to conflicts of interest.

BEUC responded to the consultation on the de Larosière Report and the Commission Communication "Driving European Recovery". Regarding micro-prudential supervision, we have notably criticized the proposal to create the European System of Financial Supervisors (ESFS) and have suggested establishing a centralised EU supervisor for multinational institutions operating at cross border level (see our response in annex). We have also asked for a supervision scheme taking on board consumer protection.

In its Communication on "European Financial Supervision"<sup>1</sup> the European Commission has once again totally forgotten the conduct-of-business side of supervision despite the fact that links between prudential supervision and consumer protection in financial services area are so obvious.

Yet the discourses on consumer protection at European<sup>2</sup> and global level in the financial services area are in abundance: conclusions of G20, speeches of high-level EU representatives, etc. Commissioner Meglena Kuneva in a speech she delivered in Lisbon on the 27 April 2009 - "**Restoring Consumer Trust in Retail Financial Services**" notably said:

*"We can learn some lessons on how trust has previously been restored to consumer markets. In some particularly risky sectors such as food, we have separated the regulatory oversight of retail markets from the regulatory oversight of the producers. This has produced bodies that are accountable only to consumers and whose main job is to ensure that the interest of consumers is respected. This issue is being debated on both sides of the Atlantic. But I think as part of the wider debate for the future, we must consider whether such a regulatory model is needed in financial markets - with a single regulator in charge of supervising the sale to consumers of all retail financial products.*

*As for enforcement, the European Commission must work with our Member States to ensure the highest standards for enforcement. The next Commission should usefully explore a more effective oversight in the implementation of consumer law, for instance by strengthening the resources, scope and efficacy of the Consumer Protection Cooperation network. Ultimately national regulators need to be held accountable for persistent violations of Community consumer protection law".*

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<sup>1</sup> Communication from the Commission "European Financial Supervision" – COM(2009) 252 final – 27 May 2009:  
[http://ec.europa.eu/internal\\_market/finances/docs/committees/supervision/communication\\_may2009/C-2009\\_715\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/committees/supervision/communication_may2009/C-2009_715_en.pdf)

<sup>2</sup> Commissioner Meglena Kuneva, speech Lisbon: "Restoring Consumer Trust in Retail Financial Services", 27 April 2009:  
<http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/09/198&format=HTML&aged=0&language=EN>

If some EU initiatives should be proposed in the following months to fill the gaps in the EU financial products legislation (see the EC Communication on Packaged Retail Investment Products<sup>3</sup>) nothing tangible has been announced until now regarding conduct-of-business supervision.

It is time for policy makers to take concrete actions; otherwise the goal of a single and safe market in retail financial services for the benefit of European consumers will remain purely rhetorical.

## **What can be learned from national experiences?**

Here are some facts reported by BEUC members.

### Czech Republic

Financial supervision is performed by the Czech National Bank (banking, securities and insurance), the Czech Trade Inspectorate (some aspects of the Consumer Credit Act) and the Czech Financial Arbitrator (disputes between institutions, such as banks or institutions issuing electronic payment instruments, and their clients).

The problems of the Czech consumers are mainly due to the insufficient level of consumer protection in substantial law. At the same time, the competence of the Financial Arbitrator might be increased (e.g. cover more types of disputes in financial market).

Due to ineffective division of competences between the Czech National Bank and Czech Trade Inspectorate there are some problems with identifying the competent authority. These problems are joined with the fragmented legal regulation. We promote the centralised model of supervision. Therefore, the Czech National Bank should be the only institution with supervision authority in the Czech Republic.

It is worth mentioning that non-bank creditors are almost not supervised at all in the Czech Republic. This causes many problems to consumers. Czech National bank should supervise this part of the financial market too.

### Finland

The Consumer Ombudsman's broad competence to monitor the compliance with legislation that has been enacted to protect consumers covers also all financial services (banking, securities, insurance). This competence and monitor is parallel to that of the special authority in this field, the Financial Supervisory Authority, FIN-FSA. But also FIN-FSA has a task to supervise the procedures that service providers apply to their customer relationships and their mutual contacts.

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<sup>3</sup> The Commission's communication on Packaged Retail Investment Products, 30 April 2009 : [http://ec.europa.eu/internal\\_market/fin services-retail/docs/investment\\_products/29042009\\_communication\\_en.pdf](http://ec.europa.eu/internal_market/fin services-retail/docs/investment_products/29042009_communication_en.pdf)

The Finnish supervisory model is well-functioning. The broad overall jurisdiction of the Consumer Ombudsman as the monitor of compliance with the consumer protection provisions in law ensures that consumers' interests are taken into consideration in the same way and level in all branches. Also, the model of two parallel supervisors provides a flexible opportunity to combine the special expertise of both authorities.

### Germany

German financial supervisor has no legal obligation to protect consumers. Financial Supervisory Authority (BaFin), Bundesbank and the Federal Ministry of Finance therefore even explicitly exclude any reflections on individual interests of consumers. Market supervision - as they usually put it - is public not private and therefore cannot and must not take notice of the individual. Reflections on a risk of damage claims of consumers against the authorities failing to provide adequate supervision were some of the underlying reasons to completely exclude consumer interest as a concept with these authorities so far.

Therefore, financial supervisors are not endowed with necessary investigation and sanctioning powers. BaFin runs a kind of consumer complaint center, but apart from registering complaints consumers do not get any sort of substantial help, neither directly nor indirectly. Financial ombudsmen are provided privately by schemes hosted by the banking associations themselves. There are no public schemes of ombudsmen similar to those in UK and Sweden, which might helpfully interfere and tackle consumers' claims and pass these issues on to the authorities.

Conflicts of interests are constant. It is easy to consider the conflict that may arise within one authority that might need to deal with consumers and providers interest, e.g. if a high court decision rules on substantial repayment claims for consumers and support for these claims would substantially destabilise those providers, which needs to be prevented by that authority as well.

### Greece

In Greece the vertical supervisory model involves the following institutions: the Bank of Greece (BofG), the Hellenic Capital Markets Committee (HCMC) and the Private Insurance Supervision Committee (PISC). Consumer protection is only partly ensured by these authorities due to lack of relevant legislation and different interpretation by the authorities of the existing legislation.

For instance, the BofG is responsible for protecting consumers only with regards to transaction transparency. It is not responsible for unfair contract terms even though in some cases unfair terms could be interpreted as being related to transaction transparency. On the other hand, the PISC, which has been recently established, has been endowed with more powers.

### Hungary

Consumer protection is provided by law and ensured by the Hungarian Financial Supervision Authority (HFSA). The HFSA takes into consideration unfair market practices, individual complaints, initiates and executes investigations. The HFSA is able to impose fines in cases of unfair commercial practices, and apply those instruments which are able to drive service providers to fair behaviour.

Some conflicts of interest can be noticed: it happens that the HFSA suggests/makes perceptible that it agrees with the complaint of the consumer, but as it has no power to address them, consumers remain disappointed (in case of credit handling, mortgage credit, unit-linked services at elderly people).

### Ireland

A problem arises due to the fact that the Financial Regulator and the Central Bank of Ireland are quite closely linked so there may be reluctance on the part of the Regulator to properly investigate financial institutions. Ireland has suffered a terrible banking crisis due in part to problems within large financial institutions when largely unchecked by the Financial Regulator – this is despite reports that the Regulator was aware of certain bad practices of these institutions. When the Regulator does take action it is generally against smaller, foreign institutions that may not be regulated or authorised to operate in Ireland. The question arises on whether the larger, Irish institutions are properly investigated.

### Italy

In Italy consumer protection in financial services is performed by three Authorities: Banca d'Italia (transparency of products and correctness of the banks), CONSOB (efficiency of the securities market), Autorità garante della Concorrenza e del mercato (unfair commercial practices and anti-competitive practices). In recent years only Autorità garante della concorrenza e del mercato sanctioned the banks. However, the penalties imposed on banks and financial institutions are small (maximum 500.000 euro).

### Netherlands

The financial supervisory system in the Netherlands is dual (supervision by objectives): a conduct-of-business supervisor (AFM) as well as a prudential supervisor (DNB). They have no restrictions to particular products, but supervise the whole array of products (lending, saving, investments, pension schemes, etc.) and providers (banks, insurance companies, pension funds, etc.).

In principle, the current supervisory model is preferable as it safeguards a better focus on both issues: conduct of business and prudence. But numerous dysfunctions have been observed. For instance, despite several research projects done by AFM in 2006 which made clear that the percentage of mis-selling in mortgages was unacceptably high, nothing really improved for consumers and new research from the same AFM proved the percentages remained at the same level in 2009.

In theory, the financial supervisor is endowed with necessary investigation and sanctioning powers to protect consumers, but in practice it is not the case. Financial penalties are low and most of the effect has to come from reputational repercussions. Also the person responsible for the wrong doing can not be punished on a personal basis, nor is there a system of personalised permits which can be revoked for a period of time to prohibit that person to work within the financial sector.

An example of conflict of interests: the prudential supervisor DNB knew already in August 2008 that there was something wrong with the Icelandic savings bank Icesave. Nothing happened and in October the bank went bankrupt. The predominant argument of the supervisor was stability in the financial system. But from the consumer's perspective, the negative effects of that were strongly felt.

Another example: due to legislation AFM is not allowed to state the names of the financial service providers they have included in their researches. Even if the outcome of such research shows that 30% of providers do not meet the legal requirements. Thus, consumers are left in the dark as to which financial service provider is and which is not doing a proper job.

### Slovenia

In Slovenia there are three main national financial supervisory authorities: The Bank of Slovenia (responsible for bank institutions), Slovene Securities Market Agency (liable for investment firms) and Insurance Supervision Agency (controlling insurance companies, intermediates and agents). Furthermore, the Market Inspectorate is in charge of supervision of non-bank credit institutions.

These institutions are endowed with necessary investigation and sanctioning powers, but unfortunately not specifically for consumer protection issues. They cannot directly intervene in existing consumer contracts, but merely publish recommendations or directions for action on specific topics regarding consumer issues, in case these are also important for market stability.

### Spain

In Spain there are several regulators (the central bank, the securities commission and the Directorate General for Insurance). No relevant consumer protection is ensured by financial supervisory authorities as these authorities do not have any capacity to sanction entities not complying with the orders issued by them. They are simply not binding! An example: in between 30-40% of decisions by the Bank of Spain favourable to consumers, banks did not follow the recommendation from the central bank.

### Sweden

Three authorities - the Consumer Board, the Financial Services Authority and the Enforcement Agency cooperate in a consumer literacy and protection project initiated by government. They have good ideas, but insufficient financial resources. To some extent the financial supervisors have necessary investigation and sanctioning powers to protect consumers. Yet more personal and financial resources are needed and legislation needs to be improved.

### UK

Consumer protection is a statutory objective for the UK financial services regulator, the Financial Services Authority (FSA). It is enshrined in the legislation which set up the FSA. However, the same legislation also stipulates that the FSA has to maintain confidence in the financial system. The regulator is therefore hesitant to publish information that is damaging to firms but which would be beneficial for consumers to know.

Despite a statutory requirement to protect consumers being in place, the regulator does frequently not prioritise consumer needs over the needs of regulated firms. The FSA has the necessary powers but does not use them enough. Much of its supervisory and enforcement work happens behind closed doors and consumers are unaware that certain firms are being investigated for activities against the interests of consumers e.g. mis-selling of products and carry on buying products from these firms despite the fact that they are being investigated. Also, the levels of fines issued by the FSA are too low especially for larger firms.

Conflicts of interest have been noticed in the past. The FSA is often too focused on protecting firms' reputations and lets this get in the way of protecting consumers from bad sales practices and bad products. An example of conflict of interest between consumers and financial institutions are mortgage arrears fees. The FSA is currently investigating four mortgage lenders for charging excessive fees to customers in arrears. However, it will not reveal their names until it decides to take enforcement action. This potentially puts consumers at risk as they are continuing to take out mortgages with these lenders.

## Consumer perspective – BEUC’s suggestions

In the position paper on the financial crisis BEUC made concrete suggestions on the improvements needed to financial supervision in Europe<sup>4</sup>. Our suggestions are as follows:

1. More powerful and independent national supervisors are needed in every Member State. Reflection should be launched on the necessity to separate prudential supervision on the one hand and control of methods of marketing and professional compliance on the other hand: clear definition of corresponding responsibilities of both supervisors to avoid conflict of interests. The national experiences illustrated above reveal that such conflicts are numerous and constant in many Member States.

Financial supervisors for consumer protection must be endowed with necessary investigation and sanctioning powers to protect consumers (“barking and biting” mandate). These tools must be effective and binding.

For instance, the US Government has already taken steps on the issue, announcing on 17 June the establishment of a new Consumer Financial Protection Agency (CFPA). CFPA will be charged with protecting consumers in credit, savings, and payment markets, and will be guided in this mission by five fundamental principles: transparency, simplicity, fairness, accountability, and access<sup>5</sup>.

Another example, the Financial Consumer Agency of Canada (FCAC) was established in 2001 to strengthen oversight of consumer issues. FCAC is responsible for: ensuring that federally regulated financial institutions comply with federal consumer protection laws and regulations; monitoring financial institutions' compliance with voluntary codes of conduct and their own public commitments; informing consumers about their rights and responsibilities when dealing with financial institutions; and providing timely and objective information and tools to help consumers understand, and shop around for, a variety of financial products and services<sup>6</sup>.

2. In order to provide better protection to consumers, national supervisory bodies should fulfill the following functions: participate in advertising control, control of financial information, unfair practices (bundled and tied products), distribution of financial products (for example in the area of consumer credit); take charge of an early warning system (inform consumers about the risks/risk category of various financial products on the basis of continuous enquiries).
3. Since the development of financial services has led to the emergence of universal actors providing a wide range of financial services (for instance, together with their traditional role, banks offer more and more insurance services, investment products, etc.) it is not necessary to have a large

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<sup>4</sup> See BEUC’s position paper “Facing up to the financial crisis”:  
<http://docshare.beuc.org/docs/1/LELDPMLCHJKMFPOPMDCCDJMDPDBG9DBYPW9DW3571KM/BEUC/docs/DLS/2009-00128-01-E.pdf>

<sup>5</sup> US Consumer Financial Protection Agency:  
[http://www.financialstability.gov/docs/regulatoryreform/strengthening\\_consumer\\_protection.pdf](http://www.financialstability.gov/docs/regulatoryreform/strengthening_consumer_protection.pdf)

<sup>6</sup> Financial Consumer Agency of Canada: <http://www.fcac-acfc.gc.ca/eng/default.asp>

- number of supervisory authorities. A unique supervisor is needed to cover all financial services and all financial institutions (banking and non-banking). Therefore, there is a need to merge existing national supervisory authorities (bank/non bank credit, insurances, securities/pensions funds).
4. Effective consumer representation on the boards of financial supervisors should be ensured. For this purpose, consumer representatives should be provided with necessary means, e.g. sufficient financial resources.
  5. Strengthen the cooperation between national supervisors and regulators: for example, create a binding network between them (see for instance the Regulation on consumer protection cooperation). Such a network already exists for national competition authorities and appears to be effective. What is necessary is to interconnect supervision knowledge (share experience) and potential to act.
  6. As financial systems and markets are becoming more and more integrated, it is necessary to create a centralised EU financial supervision authority in charge of control of financial institutions operating at cross-border level, whatever their size is. The proposals of the de Larosière group are extremely unclear concerning the corresponding responsibilities of the suggested new bodies (European Systemic Risk Council and European System of Financial Supervisors). This would possibly generate further difficulties for consumers in the future.
  7. Coherent legislation to avoid regulatory arbitrage between financial products. The French Financial Markets Regulator (AMF - Autorité des Marchés Financiers) produced a report which clearly illustrates this problem. Structured investment products sold by most banking systems are in competition with UCITS and life insurance contracts. These three categories of products are broadly substitutable. UCITS are regulated by the UCITS Directive, the obligations arising from the structured products are provided by the Prospectus Directive, while the Insurance Code and Life-insurance Directives regulate life-insurance contracts<sup>7</sup>.
  8. Adopt binding rules at EU level so that all Member States are obliged to comply with them. Soft law has shown its limits especially in case of financial services. Therefore, the regulatory gaps must be filled in.

END

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<sup>7</sup> Rapport de la mission de réflexion et de propositions sur l'organisation et le fonctionnement de la supervision des activités financières en France, janvier 2009, page 72 : <http://lesrapports.ladocumentationfrancaise.fr/BRP/094000030/0000.pdf>