BANCA D'ITALIA
EUROSISTEMA

Business conduct supervision in the financial sector

FinCoNet Annual General Meeting

Introductory remarks by Daniele Franco
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Good morning, I am happy to open the Annual General Meeting of FinCoNet, which is now an important player in promoting sound financial market conduct.

The protection of financial consumers is now considered essential for a sound financial system. Its importance grew in the aftermath of the global financial crisis. But it is still a challenge to supervisors.

Financial consumer protection was not a supervisory objective until recently. For a long time, it was assumed that an efficient capital market, effective competition among banks, a deposit insurance system, together with prudential supervision and financial market oversight were enough to provide all the protection actually needed.

In the late '70s, the relevance of information asymmetries in financial markets was eventually recognized. This induced a change in perspective and new initiatives at the national level, at the supranational level (such as the OECD Recommendation on consumer protection in consumer credit in 1977), and at the EU level (such as the first EU Directive on consumer credit in 1977).

Financial regulation originally focused on the reduction of information asymmetries by imposing disclosure and mandatory formalities in order to enhance the comparability of products and services. However, the market turmoil of 2008 together with several studies in behavioral finance proved that this was not enough: disclosure and mandatory formalities do not ensure that consumers take a decision in their best interest. Hence, disclosure requirements have been complemented with business conduct requirements aimed at promoting fairness by financial intermediaries.

Financial regulation in Europe now requires financial service providers to consider the interest of financial consumers even before their products are offered on the market. Product governance requirements impose that providers take explicitly into account the interest of consumers when designing new products, and test them to assess if they will really serve the interests and the needs of the consumers.

This evolution poses a number of challenges to supervisors dealing with financial intermediaries' market conduct. For instance, there are still differences in the range of tools and enforcement powers that conduct supervision authorities rely on in different countries.

As in the case of prudential supervision, public enforcement typically relies on on-site and off-site monitoring powers; but challenges for conduct supervision come from the nature of the analyses required. While prudential supervision can typically rely on a quantitative approach, the protection of financial consumers may require a judgment-based analysis of the quality of customer relation arrangements.

Sanctions are of course an essential deterrence tool, and (again, differently from prudential supervision) may be complemented by the power to impose the reimbursement of sums unduly charged (which directly favor damaged consumers, differently from sanctions).

Product intervention powers may further enrich the supervisory toolbox, preventing harmful products from being distributed.

In addition to public enforcement, effective customer protection may also be based on private enforcement tools. Complaint management, and effective alternative dispute resolution (ADR) schemes enabling customers to seek redress, represent relevant tools. Public authorities may have a role in establishing, or at least promoting, ADR schemes for the financial system.

Last but not least, financial education programs may obviously complement regulation and enforcement in ensuring effective consumer protection.

Overall, the work of FinCoNet over these years has become extremely relevant in supporting the comparison and evaluation of supervisory instruments, the dissemination of good practices, the analyses of critical issues, the formulation of policy proposals.

The Bank of Italy has also devoted a great effort to the development of a comprehensive consumer protection framework in the Italian banking system. In 2009 we established a Banking Ombudsman. In 2014, we established a new Directorate responsible for business conduct supervision and in charge of financial education initiatives.

Since then, we have issued several Guidelines for financial intermediaries; the Ombudsman scheme has given solutions to a very large number of complaints filed by customers; banks and other financial intermediaries reimbursed over € 300 million to customers; our financial education activities reach more than 100.000 students every year.

However, despite the steps taken so far, we are aware that we are still in the "early age" of business conduct supervision. That is why FinCoNet meetings are important: we believe that comparing practices, sharing knowledge and experiences are essential to ensure financial consumer protection.

The agenda of this two days meeting is very rich. You will be able to analyze and exchange views on several relevant issues: the tools available and their effectiveness, the evolving context in your respective jurisdictions, the use of new technology in market conduct supervision.

New technologies in the financial system challenge regulators and supervisors, they open up new streams of products and services in a fast-changing market. The rise of "open banking" and the increased accessibility of bank accounts by third parties represent the most visible innovations in this field and are already contributing to reshaping the financial landscape. Conduct supervisors must intensify the use of data and algorithms to increase the efficiency and scope of supervisory actions.

On Friday, the International Seminar jointly organized by FinCoNet and the Bank of Italy will provide useful insights on behavioral finance, shedding a light on how this approach can be embedded in supervisory activity.