

**Representations by the Monetary Authority
concerning an application to the Competition Commission
for a decision in relation to the Code of Banking Practice
(case reference number AD/01XX)**

On 11 December 2017, 14 institutions authorized under the Banking Ordinance (Cap. 155) (“Applicants”) made an application (“Application”) to the Competition Commission (“Commission”) under section 9 of the Competition Ordinance (Cap. 619) for a decision from the Commission confirming that the first conduct rule in section 6 of the Competition Ordinance does not apply to the giving effect of the Code of Banking Practice (“CoBP”) by the Applicants by virtue of the exclusion in section 2 (*Compliance with legal requirements*) of Schedule 1 to the Competition Ordinance. On 5 January 2018, the Commission published a notice of the Application and called for representations from interested parties about the Application. The Monetary Authority (“MA”) through his office (the Hong Kong Monetary Authority, “HKMA”) is writing to make representations to the Commission in support of a decision from the Commission confirming the Applicants’ view that the first conduct rule does not apply to authorized institutions (as defined in the Banking Ordinance, “AIs”) giving effect to the CoBP.

Statutory functions of the MA

2. As set out in section 7(1) of the Banking Ordinance, the principal function of the MA under the Banking Ordinance shall be to promote the general stability and effective working of the banking system. Section 7(2)(c) of the Banking Ordinance stipulates that one of the statutory functions of the MA is to promote and encourage proper standards of conduct and sound and prudent business practices amongst, inter alia, AIs, comprising licensed banks, restricted licence banks and deposit-taking companies. In addition, under section 7(2)(g) of the Banking Ordinance, the MA shall take all reasonable steps to ensure that any banking business, any business of taking deposits, or any other business, carried on by an AI is carried on (i) with integrity, prudence and the appropriate degree of professional competence, and (ii) in a manner which is not detrimental, or likely to be detrimental, to the interests of depositors or potential depositors.

3. Customer confidence and trust are the cornerstone for sustainable development of banks, which in turn promotes banking stability and helps reinforce Hong Kong's position as Asia's premier international financial centre. To earn and keep customers' confidence and trust, AIs should treat customers fairly at all stages of their relationship with them. A key guiding supervisory principle of the MA is therefore to encourage and require AIs to treat their customers fairly. This principle is mainly achieved through AIs' compliance with recognised ethical standards of conduct, including those currently embodied in the CoBP.

Objectives of the CoBP and compliance by AIs

4. The CoBP, which was jointly issued by the Hong Kong Association of Banks ("HKAB") and the DTC Association ("DTCA"), sets out the minimum standards which AIs should follow in their dealings with customers with a view to promoting good banking practices in the industry. The CoBP aims, inter alia, to promote a stronger culture of treating customers fairly and ensure customers' interests are taken into account by AIs in their business dealings with customers. The standards set out in the CoBP are also aligned with international standards on financial consumer protection.

5. Given its significance in the promotion of consumer protection, the CoBP is **formally and fully endorsed by the HKMA**. In fact, the HKMA has been heavily involved in the drafting of the CoBP since it was first published in 1997, and in each review exercise thereafter. AIs should **achieve full compliance** with the provisions in the CoBP.

6. The HKMA has also incorporated the CoBP into the **Guideline on Minimum Criteria for Authorization, which is a statutory guideline** issued by the MA under section 16(10) of the Banking Ordinance ("Guideline") to set out the manner in which the MA will interpret the licensing criteria set out in the Seventh Schedule to the Banking Ordinance. Paragraph 97 of the Guideline stipulates that "[i]ntegrity is concerned with the manner in which the business of the institution is carried on. The institution must observe high ethical standards in carrying on its business ... Doubts may also be raised if the institution fails to comply with recognised ethical standards of conduct such as those embodied in various codes of conduct (e.g. the Code of Banking Practice issued jointly by the Hong Kong Association of Banks and the DTC)".

Association and endorsed by the HKMA) ... In considering what action to take in respect of a breach of statute or of a code of conduct, the MA would have regard to the seriousness of the breach, whether the breach was deliberate or an unintentional or unusual occurrence, and whether it could be detrimental to the interests of depositors or potential depositors.” (emphasis added). The Seventh Schedule to the Banking Ordinance sets out minimum authorization criteria that an AI must meet on a continuing basis, one of which is that the MA is satisfied that the business of the AI is being carried on with integrity, prudence and the appropriate degree of professional competence. Paragraph 5(a) of the Guideline also stipulates that “*failure to meet the criteria by existing authorized institutions would be a ground for revocation of authorization...*”. It should therefore be noted that, while the CoBP is not a statutory code issued under The Hong Kong Association of Banks Ordinance (Cap. 364), it is distinct from other industry codes in that the CoBP has the full endorsement of the HKMA, while compliance with the CoBP is ensured under the Banking Ordinance as a result of the MA’s various statutory powers to monitor compliance and take supervisory sanctions for non-compliance.

7. Compliance with the CoBP is also one of the ongoing **supervisory requirements of the HKMA**. The HKMA monitors AIs’ compliance with the CoBP as part of its **regular supervisory process** and through **a wide range of supervisory activities**, including:

- (a) requesting AIs to carry out self-assessments on a regular basis on compliance with the CoBP and reviewing the self-assessment reports submitted by AIs. A self-assessment requires the internal auditors of an AI or equivalent units to independently review the AI’s compliance with the requirements under individual sections of the CoBP;
- (b) conducting various thematic reviews by obtaining information under section 63(2) of the Banking Ordinance;
- (c) conducting examinations and investigations under section 55 of the Banking Ordinance; and
- (d) carrying out other supervisory activities, such as mystery shopping programme.

8. The MA views non-compliance with the CoBP seriously. The HKMA will follow up on an AI's non-compliance with the CoBP to ensure timely rectification and enhancement of relevant systems and controls to avoid similar instances of non-compliance occurring again. In the event that material deficiencies are not adequately addressed by an AI in a timely manner, the MA can take **a wide range of supervisory sanctions** under the Banking Ordinance, as appropriate. Supervisory sanctions under the Banking Ordinance include the following:

- (a) *Section 16(5)*: The MA may at any time, by notice in writing served on an AI, attach to its authorization such conditions (including attach by way of amending conditions already attached to its authorization), or cancel any conditions attached to its authorization, as he may think proper – this power may be used to restrict the business of an AI until the relevant supervisory concerns have been adequately addressed;
- (b) *Section 59(2)*: The MA may require an AI to submit an auditor's report on (amongst other things) whether the AI has in place systems of control which are adequate to enable, as much as is practicable, the affairs, business and property of the AI to be prudently managed and the AI to comply with its duties under the Banking Ordinance;
- (c) *Seventh Schedule*: Crucially, and related to the point made under paragraph 6 above, an AI's failure to comply with the CoBP may cast doubt on whether the business of the AI is being carried on with integrity, prudence and the appropriate degree of professional competence, which is part of the minimum authorization criteria set out in the Seventh Schedule to the Banking Ordinance. Failure by an AI to meet the minimum authorization criteria set out in the Seventh Schedule would be a ground for revocation of authorization under the Banking Ordinance;
- (d) *Section 22*: The MA may (after consultation with the Financial Secretary) revoke an AI's authorization under the Banking Ordinance on any of the grounds specified;

- (e) *Sections 24 and 25*: The MA may (after consultation with the Financial Secretary) suspend an AI's authorization under the Banking Ordinance on the same grounds as those for revocation of authorization under section 22 of the Banking Ordinance; and
- (f) *Section 71*: If the MA is no longer satisfied that the chief executive or a director of an AI is fit and proper for the position, the MA may withdraw his consent for such person to be the chief executive or a director of the AI.

9. To conclude, compliance by AIs with the CoBP is not voluntary – AIs are required to comply with the CoBP and the requirement is imposed under the HKMA's broad supervisory framework which is underpinned by the MA's various statutory powers under the Banking Ordinance.

Suspension of certain provisions of the CoBP by the industry

10. In December 2015, HKAB and the DTCA temporarily suspended 18 provisions of the CoBP (now 17 provisions¹) ("Suspended Provisions"), mainly relating to the level at which fees and charges are to be set by AIs, on concerns that these provisions may be potentially in breach of the Competition Ordinance. The MA notes, however, that the CoBP is in fact supportive of competition amongst AIs and specifically states as a general principle in section 2.8 (*Competition*) that AIs should allow customers to search, compare and, where appropriate, switch between products and institutions easily and at reasonable and disclosed costs. From the HKMA's perspective, the purpose of the Suspended Provisions is not to fix prices for AIs, but rather to prevent improper banking conduct and practices in Hong Kong and thus provide a measure of protection to AIs' customers. The Suspended Provisions can be categorised as follows in accordance with their underlying consumer protection intentions (extracts of the Suspended Provisions are set out in the Annex hereto):

¹ Subsequent to the issuance of a circular by the HKMA to all AIs on 14 February 2017 (<http://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2017/20170214e1.pdf>), HKAB and the DTCA amended and reinstated section 22.5 of the CoBP and the number of suspended provisions was reduced to 17.

- (a) ensuring that customers will not be charged if no service has been provided – these include 7 provisions proscribing fees for termination of banking services, fees for choosing a master fire insurance policy option, fees for cancellation of credit cards, annual fees for credit cards which have not been activated, fees for credit card account inactivity, a closed account fee on a cardholder, and fees for cancellation of stored value cards. The motivation behind these provisions is not to fix prices for AIs, but instead to address the unfairness and unreasonableness of imposing fees when in fact no services are provided;
- (b) ensuring that customers will not be charged unreasonably or charged multiple fees for a single reason in their use of credit cards – these include 6 provisions setting parameters around the imposition of over-the-limit fees, late payment fees, interest or finance charges regarding disputed amounts, and liability in relation to a lost or stolen card. Similar to (a) above, the rationale behind these provisions is not to fix prices for AIs, but instead to prohibit the charging of any unfair and unreasonable fees or liabilities on customers;
- (c) protecting customers from building up debt that they are unable to repay – these include 2 provisions capping the credit card limit that can normally be extended to students, and prescribing the minimum periodic payment amount for a credit card (being the sum of interest, fees, charges and at least 1% of outstanding principal) to ensure that the principal amount owed by cardholders will be reduced over time;
- (d) protecting customers from being charged excessive and extortionate interest rates – the provision under this category prohibits AIs from unjustifiably charging extortionate interest rates or rates exceeding the legal limit stated in the Money Lenders Ordinance; and
- (e) addressing the needs of the general public – the provision under this category disallows the charging of administrative fees on cash deposits in Hong Kong dollars, except in large quantities,

recognising that the ability of the public (particularly the elderly, low-income individuals and other vulnerable groups) to deposit cash in bank accounts is a basic banking service.

11. The consumer protections afforded by the CoBP do not conflict with the objectives of the Competition Ordinance, and if the “substance” of the CoBP is recognised to be beneficial to consumers of banking services, it is submitted that the CoBP should not be considered potentially anti-competitive simply because it takes the “form” of an industry code. On its part, the HKMA continues to view the Suspended Provisions’ regulation of AIs’ conduct and the consumer protections afforded thereby as a highly important aspect of ensuring that AIs carry on business with integrity, prudence and the appropriate degree of professional competence (see paragraph 2 above). To ensure that such important consumer protections remain in place and continue to be effective, the HKMA has therefore reminded all AIs that they are **still required to fully comply** with the CoBP, including the Suspended Provisions.

12. The Commission is respectfully requested to take the above representations into account in considering the Application.

Hong Kong Monetary Authority
February 2018

**Extracts of Suspended Provisions
categorised by their underlying consumer protection intentions**

(A) Ensuring that customers will not be charged if no service has been provided

- (1) Section 5.10 – “... In case the customer decides to terminate the banking service, the [AI] should not charge any fees for the termination under the following conditions [in relation to a variation of terms and conditions]”.
- (2) Section 22.11 – “... [AIs] should not charge any fee if a customer chooses the master fire insurance policy option. ...”.
- (3) Section 26.9 – “... card issuers should not replace or renew a card without allowing the cardholder at least 30 days from the date of replacement or renewal to cancel the card without having to pay any fee.”.
- (4) Section 26.12 – “Card issuers should not levy any annual fees on credit cards (including any principal or subsidiary card) which are not activated by cardholders. In the case of renewal or replacement cards which are not activated, if the accounts have no outstanding balances and no cardholder-initiated activities during the first 18 months from the date of issuance of the cards, card issuers should not levy any annual fees on the credit card accounts.”.
- (5) Section 28.2 – “Card issuers should not impose an account inactivity fee on a cardholder.”.
- (6) Section 28.3 – “Card issuers should not impose a closed account fee on a cardholder, provided that a card issuer may recover the cost of a welcome gift or other benefit already received by the cardholder if the conditions for receiving the gift or benefit as stated in the terms agreed with the cardholder have not been fulfilled by the cardholder.”.

- (7) Section 52.1 – “[stored value card] issuers should not automatically renew a [stored value card] without giving customers at least 30 days’ notice commencing from the date of renewal to cancel the [stored value card] without having to pay the renewal fee.”.
- (B) Ensuring that customers will not be charged unreasonably or charged multiple fees for a single reason in their use of credit cards**
- (8) Section 26.15(e) – “When card issuers provide over-the-limit facilities to cardholders, card issuers should ... not impose more than one over-the-limit fee or charge per billing cycle on the cardholders who have not opted out of the over-the-limit facilities”.
- (9) Section 26.15(f) – “When card issuers provide over-the-limit facilities to cardholders, card issuers should ... not impose an over-the-limit fee or charge for a billing cycle if a cardholder exceeds a credit limit solely because of fees or interest charged by the card issuers to the cardholder’s account.”.
- (10) Section 28.4 – “If card issuers impose a fee for violating the terms or other requirements of an account, the fee should be set at a reasonable amount. Late payment fee should be an amount determined in accordance with the above principle or the amount of minimum payment, whichever is the lower. In addition, when charging fees on minor breaches involving small amounts, under normal circumstances card issuers should exercise flexibility in waiving or reducing the fees. ...”.
- (11) Section 28.5 – “Card issuers should not impose more than one fee in case a late payment is triggered by a returned payment. They can either impose a late payment fee or a returned payment fee.”.
- (12) Section 34.3 – “Where the cardholder reports an unauthorized transaction before the payment due date, the cardholder should have the right to withhold payment of the disputed amount during the investigation period. Card issuers should not impose any interest or finance charges on such disputed amount while it is under investigation or make any adverse credit report against the cardholder. ...”.

(13) Section 36.3 – “... Provided that the cardholder has not acted fraudulently, with gross negligence or has not otherwise failed to inform the card issuer as soon as reasonably practicable after having found that his or her card has been lost or stolen, the cardholder’s maximum liability for such card loss should be confined to a limit specified by the card issuer, which should not exceed HK\$500.”.

(C) Protecting customers from building up debt that they are unable to repay

(14) Section 26.1(c) – “Card issuers should act responsibly in the issue and marketing of credit cards and the setting of credit card limits, in particular to persons (such as full time students) who may not have independent financial means. Card issuers should in all cases – ... not grant credit limit exceeding HK\$10,000 to students in an institution of higher education, unless the student has submitted a written application and has given financial information indicating that the student has an independent ability to repay the proposed extension of credit in connection with the account. ...”.

(15) Section 30.1 – “Card issuers should set the minimum periodic payment for a credit card account at an amount no less than all interest and fees and charges (including annual card fees), plus at least 1% of outstanding principal.”.

(D) Protecting customers from being charged excessive and extortionate interest rates

(16) Section 12.3 – “While [AIs] are exempt from the Money Lenders Ordinance (Cap. 163) so that the interest rates they charge are not restricted, they should not charge customers extortionate interest rates. If the [annualised percentage rates] charged by them ... exceed the level which is presumed to be extortionate under the Money Lenders Ordinance, they should be able to justify why such high interest is not unreasonable or unfair. Unless justified by exceptional monetary conditions, the [annualised percentage rates] charged ... should not exceed the legal limit as stated in the Money Lenders Ordinance.”.

(E) Addressing the needs of the general public

- (17) Section 6.5 – “[AIs] should not impose administrative charges for handling cash deposits in Hong Kong dollars, except those in large quantities.”.