

BOX 12

Financial Consumer Protection Framework: A Way Forward

Introduction

The level of financial literacy among the population and strength of consumer protection frameworks in place are two integral components that determine financial inclusion, which remains a key ingredient in the sustainable development of a country. Continuous technological advances, increasing complexity of financial services, and growing competition among market participants have compelled financial regulators to place greater emphasis on consumer awareness and sufficiency of the consumer protection framework. As evident, the Global Financial Crisis that preceded us exposed, among other things, the shortcomings in this important area. This exhibited the need for a more robust consumer protection framework, which could contribute to maintaining public confidence, a necessary ingredient for ensuring financial system stability during a crisis. On the contrary, it is widely accepted that a sound financial consumer protection framework effectively facilitates anticipation, identification, and resolution of issues related to consumer protection in a timely manner, minimising any impact on financial system stability.

In this context, being the apex institution in the financial market in the country, the Central Bank of Sri Lanka (CBSL) undertook several initiatives and coordinated efforts through the entities it regulates to increase the level of financial inclusion and financial consumer protection in the country. Consequently, having recognised the limitations of the current consumer protection framework and developments taking place in the rest of the world, CBSL launched an initiative to strengthen the financial consumer protection framework with the engagement of all stakeholders.

Current Financial Consumer Protection Framework of CBSL

The financial sector in Sri Lanka is diverse, with a range of financial service providers subject to different regulatory regimes under different laws and regulations. As the CBSL regulated entities accounts for about 70 per cent of financial sector assets in Sri Lanka, the regulatory measures that will be taken by CBSL in this area are expected to create a significant and lasting impact on the wellbeing of both the financial consumers and overall financial system of the country. Over the years, regulatory departments of CBSL have initiated several actions to strengthen the financial consumer protection framework applicable to entities under their purview.

For example, for the first time the Banking Act Directions No. 08 of 2011 on the Customer Charter of Licensed Banks set out a code of conduct that all licensed banks must follow, aimed at fostering a healthy relationship between financial consumers and licensed banks. The Directions list regulatory expectations regarding the introduction and promotion of banking products and services to financial consumers, the implementation of a complaint handling mechanism at the banks level, raising awareness and promoting understanding of the terms and conditions of banking products and services, providing protection from agents of banks and special attention and care for the financial consumers with special needs. Further, the Finance Business Act Directions No. 01 of 2018 and Finance Leasing Act Directions No. 01 of 2018 outline the financial consumer protection framework for Licensed Finance Companies and Specialised Leasing Companies that ensure the protection of the rights and interests of their financial consumers. The directions specify the minimum standards on financial consumer protection in the areas of disclosure and transparency, consumer education and awareness, responsible business conduct, complaint handling and redress, equitable and fair treatment, and consumer data and privacy protection. These guidelines cover transactions related to savings, lending, and other consumer related activities as well. Similarly, Primary Dealers in government securities are also required to adhere to a customer charter issued in 2013 under the Local Treasury Bills Ordinance, No. 08 of 1923 and the Registered Stock and Securities Ordinance, No. 07 of 1937. All these initiatives set a fairly solid base for the financial institutions to ensure that consumers are able to make informed decisions and have access to transparent and fair financial services.

Nevertheless, the fragmented approach of existing frameworks of CBSL has created incompatibilities and complexities, hindering the achievement of the overall objective of consumer protection. Thus, CBSL took a policy decision to introduce an integrated and comprehensive financial consumer framework aimed at strengthening the financial consumer protection framework that applies to the entities under its regulation. As a first step in this direction, and in accordance with the decision made by the Monetary Board of CBSL, the Financial Consumer Relations Department (FCRD) was established as a separate department within the CBSL in August 2020. At present, FCRD is working on issuing and implementing a new comprehensive financial

consumer protection framework for entities regulated by CBSL as the medium term target, while serving as the single point of contact for receiving and disseminating all external complaints and grievances directed to CBSL by financial consumers of institutions regulated by CBSL.

New Regulations on Financial Consumer Protection

CBSL with the technical support of IFC and World Bank developed draft Regulations, which are to be issued mid-2023 in terms of Section 10 of the Monetary Law Act, No. 58 of 1949. The draft Regulations were made available for public and industry for observations/consultations in order to make the drafting process transparent and facilitate stakeholder engagement. The proposed regulations have been prepared to cover all entities currently regulated by CBSL, namely Licensed Commercial Banks, Licensed Specialised Banks, Licensed Finance Companies, Specialised Leasing Companies, Money Brokers, and Participants of Payment and Settlement Systems, encompassing the existing consumer protection principles, rules, as well as current practices and possible near-term developments in the consumer protection areas. Due consideration was given to the following directions/areas under these draft regulations:

- a. Banking Act Directions No. 08 of 2011 on the Customer Charter of licensed banks.
- b. Finance Business Act Directions No. 01 of 2018 and Finance Leasing Act Directions No. 01 of 2018 on the financial customer protection framework for Licensed Finance Companies and Specialised Leasing Companies.
- c. Best practices and regulations on consumer protection of other jurisdictions.
- d. Current issues of financial consumers and gaps/trends identified by CBSL in relation to consumer protection activities in Sri Lanka.

Accordingly, the draft regulations include the following key areas required for an effective consumer protection framework for entities regulated by CBSL, with the necessary empowerment for CBSL to implement these regulations and closely supervise these entities:

- a. Powers, Supervisory Actions of CBSL and Governance by Financial Service Providers
- b. Disclosure, Transparency, and Accessibility Procedures
- c. Responsible Business Conduct, Complaints Handling, and Redress Mechanism

- d. Competitive Environment and Protection of Consumer's Assets and Information
- e. Fair and Equitable Treatment for Consumers, Financial Education, and Awareness

These regulations will specially empower CBSL to examine the books, records, accounts, documents, information, and other supervisory activities of CBSL-regulated entities, allowing for effective monitoring of consumer protection and market conduct. Further, these proposed regulations will provide the basis for the market conduct supervision of CBSL-regulated entities as well as enforcement of regulatory actions, enabling the Monetary Board of CBSL to take regulatory actions for market misconduct that affects the financial consumers, the market, or the financial system. Furthermore, these regulations will streamline the two tiered complaint handling procedure of both financial institutions and CBSL and empower CBSL to make binding determinations to financial institutions as one of the out-of-court settlements for valid complaints made by financial consumers. Overall, these regulations will strengthen the current financial consumer protection frameworks of CBSL, particularly Banking Act Directions No. 08 of 2011, Finance Business Act Directions No. 01 of 2018, and Finance Leasing Act Directions No. 01 of 2018, in line with international standards and establish the foundation for market conduct supervision by CBSL facilitating the development of a trusted and stable financial system in Sri Lanka, instilling confidence of financial consumers.

Challenges and Way Forward

Implementing an integrated financial consumer protection framework that caters to a diverse set of financial service providers is a daunting task to the financial institutions as well as to the CBSL given the vast differences in terms of size, scope, product and services, and consumer segments. In this regard, most of the large financial entities have already improved their business operations and practices to a great extent to meet the standards expected by the new regulations. However, there could be a number of entities that require significant changes to their existing policies, procedures, operations, resources, infrastructure and systems in order to comply with the requirements of the new regulations. It is expected that such entities would adhere to the regulations within the transitory period offered for the implementation timelines.