MFSA MALTA FINANCIAL SERVICES AUTHORITY

6 February 2024

Dear Chief Executive Officer
Dear Compliance Officer

Re: Mystery Shopping Exercise –Personal Loans and Payment Accounts

You are receiving this letter as the Chief Executive Officer and Compliance Officer of a Credit Institution supervised by the Malta Financial Services Authority (referred herein as "MFSA" or "the Authority").

Background

The MFSA endeavours to ensure compliance with applicable rules governing credit institutions which it licences such that these entities, *inter alia*, provide fair, clear and not misleading information and documentation to its clients. This will strengthen consumer protection leading to increased confidence in the market. To this end, the Authority's continuous supervision is aimed at achieving high compliance standards by its licenced entities through an array of tools including off-site work, on-site inspections and also through mystery shopping exercises.

Since mystery shopping is considered as a form of research to support and enhance current market practices within the industry, the Conduct Supervision Function within the Authority has chosen to be part of a Mystery Shopping exercises conducted by the European Banking Authority ("EBA").

During the first half of last year, MFSA has collaborated with the EBA to conduct a mystery shopping exercise ("the exercise") in order to determine the conduct practices being adopted by institutions in the provision of personal loans and payment accounts. A number of Maltese authorised credit institutions were selected for this exercise. The report as published by the EBA highlighting the findings of this exercise, may be accessed from this link: Mystery shopping exercise into Personal Loan and Payment Accounts (EBA/REP/2023/30).

This letter relates to the findings of this mystery shopping exercise with respect to local credit institutions, which was carried out between the month of February and March 2023. The fieldwork for the mystery shopping exercise was conducted on behalf of the MFSA by an outsourced and independent external provider.

This letter provides an insight of the identified observations arising out of this exercise, as reported to the MFSA by the EBA, and highlights good and bad practices observed in the market.

1.0 Scope and Methodology

In view of its consumer protection mandate, the EBA was mandated to undertake this exercise, following the outcomes of exercises done throughout the past years to determine the effectiveness of **Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC** which is accessible via **Link** (hereinafter referred to as the "Consumer Credit Directive") and **Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features** which is accessible via **Link** (hereinafter referred to as the "Payment

Accounts Directive") as well as the outcomes of the Consumer Trends Report which is accessible via **Link** and thematic review exercises conducted by the EBA, which revealed a number of deficiencies and inconsistencies across Member States.

The mystery shopping exercise focused on the **pre-contractual phase with respect to the personal credit products and payment accounts offered by the credit institution - that is when a customer makes an initial enquiry** to obtain a personal loan or to open a payment account, including a payment account with basic features. More specifically, the scope of the exercise was to:

- **Assess compliance with the requirements of the Consumer Credit Directive 2008/48/EC and Payment Account Directive 2014/92/EU, including EBA Guidelines and Regulatory Technical Standards on fees and charges.** This included an assessment of whether the relevant credit institutions' staff went through a proper process of establishing the client's needs by asking relevant questions, making good recommendations, and following requirements to ensure that fees and charges are disclosed in a manner which is transparent, fair, clear, and not misleading. The purpose was also to establish whether there are any irregular practices in place such as those relating to cross-selling of products.

- **Verify whether relevant and adequate information was effectively disclosed to the consumer at the pre-contractual stage, at the time of initial enquiry, in a timely manner.** This included evaluating:

  (i) the adequacy of information disclosure concerning the products and services selected and possible promotion of tied/bundled products and services. Focus was made on the provision of pre-contractual information and the relating selling practices;

  (ii) use of personal data at the pre-contractual phase; and

  (iii) any additional information over and above the prescribed information which should be provided during the pre-contractual stage such as general information or forms (where applicable) available on websites and in branches. Moreover, the shoppers' role was also to determine what information was provided by default and what needed to be prompted by the mystery shopper.

- **Assess whether the relevant staff interacting with prospective clients possessed an adequate level of knowledge, competence and a general level of professionalism when selling products such that consumers able to make an informed decision on the basis of the information provided.** This included assessing whether the relevant staff of institutions possessed and maintained an adequate and up-to-date level of knowledge and competence in relation to the offering, and/or selling of the selected products and services demonstrating a high level of professionalism.

The exercise was conducted through both onsite and off-site engagement and included a total of **five** credit institutions as per below table:

Product Type	**Distribution Channel**	**No. of visits per credit institution**
Personal Loans	Onsite	9 visits
	Online/Offsite	1 interaction
Payment Accounts (incl. bank account with basic features)	Onsite	7 visits
	Online/Offsite	3 interactions

The objective of the interaction conducted by mystery shoppers was to understand what information and guidance is provided to prospective clients at the very enquiry stage and did not delve into the more intensive and detailed pre-contractual stage where there is a more concrete discussion prior to the issue of a personal loan or the opening of a payment account.

The mix of interactions between onsite/off-site as well as the choice of scenarios was dependant on general market practices in Malta for the particular product being assessed. In fact, the majority of the interactions between the mystery shoppers and the credit institutions were carried out on face-to-face basis through on-site visits at branches. Off-site interactions were carried out mainly through phone, email and chats.

2.0 Findings/Observations

A. <u>Personal Loans</u>

_A total of 50 interactions were made in relation to Personal Credit, 45 of which were onsite and 5 of which were off-site.

(i) <u>Regulatory Requirements</u>

The Consumer Credit Regulations (S.L. 378.12) transpose the requirements of the Consumer Credit Directive. In particular, Regulation 5(1) of these Regulations stipulate that *"A creditor shall take all necessary steps to ensure full compliance with these regulations"*. Additionally, both Regulation 6(1) and (2) and Regulation 7(1) and (2) specifically highlight that the credit institution is obliged to provide pre-contractual information referred to as the Standard European Consumer Credit Information ("SECCI") as per First Schedule of the aforementioned Regulations.

Part 5 of the Consumer Credit Regulations deals with the rights of the consumer when entering into a credit agreement. Regulation 11(1) states that *"The consumer shall be entitled to receive, free of charge, and upon request, a copy of the draft consumer agreement"* unless the creditor is unwilling to proceed with the conclusion of the credit agreement as per Regulation 11(2).

Another important provision is that the consumer has the right to withdraw from the credit agreement as per Regulation 14(1) and (2) of the Consumer Credit Regulations.

During the term of the loan, the consumer also has the right to early repayment as per Regulation 16(1) which states that *"A consumer shall have the right to discharge his obligations under a consumer credit agreement, in full or in part, before the agreed termination."*

Bank officials in contact with clients both at branch level or through other off-site means such as call centre or chats, are expected to be well versed with the requirements of these Regulations as well as the applicable procedures so that they are in a position to communicate the right information to clients and prospective clients.

(ii) <u>Observations</u>

The main objective of the exercise was to enquire with bank officials in relation to the granting of a personal loan (between €2,000 and €10,000) for a 3-year term in order to carry out home improvements. A list of questions was asked to bank officials. These questions were generic and open-ended, in order to avoid any prompting for certain replies. This methodology was chosen in order to analyse if clients are being provided with the required pre-contractual information and documentation (including SECCI), the full related costs (including APR) and any specific requirements which needed to be satisfied by the client in order to be granted a personal loan. The exercise also addressed whether credit protection insurance was also promoted to the client.

Onsite observations

The oral information provided by staff members during onsite visits, in the vast majority of cases, bank staff provided mystery shoppers with a full, or at least partial explanation of the costs, albeit different approaches were being adopted within the same institution.
It was observed that in most cases, credit institutions required clients to open a bank account with the institution as a prerequisite to accessing a personal loan; in 58% of the interactions, mystery shoppers were provided with information about such requirements. In fact, without exception all five (5) credit institutions had several instances where, at enquiry stage, this, or any other applicable requirements were not indicated to the client as prerequisites to obtain a personal loan.

In 40% of the interactions, it was observed that mystery shoppers were not provided, at initial enquiry stage, with any information about special requirements which need to be satisfied in order for a loan to be issued). Such requirements would eventually be disclosed later, generally, at application stage after the client has decided to formally initiate the process with the credit institution to issue the loan.

It was also observed that the SECCI was provided, at the very initial request stage, **only in 4%** of the interactions. It therefore appears that this document is not being provided upon the first interactions with the clients. In fact, the SECCI was provided to mystery shoppers only in 2 instances out of a total of 45 interactions.

Identified Good Practices

In 66% of the interactions, the credit institution's staff clearly informed the mystery shoppers that the credit was not subject to a mandatory insurance.

In 96% of the interactions, the staff did not try to increase the credit requested by the Mystery Shopper – by for example, automatically adding a payable fee, such as a commitment fee, to the amount of the loan.

Identified Bad Practices

In instances when mandatory insurance was required, the mystery shoppers were **not always** given the possibility to purchase the said insurance through another entity. Only a small percentage of shoppers were given the possibility to obtain the insurance from a separate entity.

In relation to costs, there were a few cases where shoppers did not receive any explanation in relation to costs associated with the loan or else were told to look for information on the documentation provided by the bank or on its website.

Online/Offsite Observations

Mystery shoppers could reach the banks through various offsite channels but the medium which showed the consumer satisfaction outcomes was the phone, followed by email, followed by reference to FAQs issued by credit institutions and online chat. In fact, it was observed that the most detailed information in particularly about costs was provided over the phone.

The most common information provided over the phone related to the borrowing rate and duration of credit agreement. Other details such as amount and frequency of payments, details of APR, total amount payable, etc. were noted only in few instances in other offsite media.

In non-face to face interactions, 60% of the mystery shoppers were provided at least with partial explanation of the costs in relation to the credit in question.

None of the mystery shoppers was provided with the SECCI as required by Regulation 6(1) of the Consumer Credit Regulations in non-face to face interactions.

A substantial volume (50%) of all responses to mystery shoppers through online channels provided were not informed by the bank official about the right of withdrawal from a credit agreement which may be exercised by the consumer within the 14-day period as specified in Regulation 14 (2) of the Consumer Credit Regulations (S.L.378.12), with the highest occurrences through phone calls.

It was noted that 62% of the mystery shoppers were not provided with conditions related to early repayments.

Only in 50% of the cases did the bank staff through general online/offsite interactions indicated to the consumer the right of getting a copy of the credit agreement before signing. Such information was mostly provided over the phone to mystery shoppers, with 60% of the responses given out by call centre agents informing that the customer will be provided with a copy of the credit agreement before signing, as stipulated by the Consumer Credit Regulations (S.L. 378.12).

Identified Bad Practices.

There were instances when no explanation was provided in relation to costs of the loan. There were also other instances when the mystery shopper was told to refer to the bank's website for more information. Such instances represented 40% of the responses.

It was also noted by the mystery shoppers that chats provided the least level of information such that rarely any product-specific information was available via online chat.

Conclusion and Expectations

With respect to provision of pre-contractual documentation, the Consumer Credit Regulations require that the SECCI is provided to the client or potential client in "good time" before an agreement is concluded. In this context, the Authority considers that a SECCI should also be provided at the very initial stage of a client's enquiry, even if a client is still undecided on the amount of the loan needed. A client might ask for quotes for different loan amounts and in this case, a SECCI for every loan amount should be provided by the credit institution, for comparison purposes. Indeed, in its Mystery Shopping Report, referred to earlier on in this letter, the EBA has also pointed out that providing such a document during the client's first visit is a practice that can be considered to comply with the requirements of the Consumer Credit Directive.

The SECCI would assist the customer to compare different offers by different credit institutions and make an informed decision before applying for the loan and eventually signing the credit agreement.

Indeed, the SECCI may also serve as guidance to the bank official when explaining the salient details to the client, to ensure that a full explanation of the terms of the loan is given. Therefore, by following the SECCI in the explanations provided to clients, the bank official would ensure that it provides all the necessary information and reduces the risk of omission of certain important information.

If any type of insurance is mandatory for the granting of the loan, bank officials should disclose this to the customer at this early stage, with specific emphasis on the fact that the insurance could be purchased through other entities. Bank officials should be trained to be able to clearly explain the difference between a life insurance providing only death cover and credit protection insurance.

It can be noted that throughout the industry, there is inconsistency in relation to the provision of the information to clients when credit institutions are first approached for consumer credit. Bank staff are to ensure that any requirements which the customer must satisfy before being granted a personal loan are to be immediately disclosed in full and explained in detail to the consumer at enquiry stage. Furthermore, the associated costs incurred, the clients' rights to withdraw from the contract and the conditions to effect extra repayments are to be always provided to clients at enquiry stage without exceptions. This will enable the client to compare offers between banks before taking a final decision as to which credit institutions to choose from the available options in the market.

It is imperative that the same level of information is provided irrespective of whether a client opts to visit a branch or else contact the bank remotely by means of a phone call or through other online services available. In this regard, credit institutions are expected to ensure that front line staff are fully aware of their disclosure obligations, even at mere enquiry stage, and that there are the necessary procedures in place to ensure a uniform service across all the branches of the credit institutions.

The Authority recommends that periodic training is provided regularly to all staff members involved in the granting of consumer loans, irrespective at which contact point they work at. Furthermore, regular internal audits should be conducted, including internal mystery shopping exercises. New staff members should be monitored for a period of time before attending to clients' queries on their own.

B. <u>Payment Accounts</u>

A total of 50 interactions were made in relation to Payment account (including accounts with basic features) 35 of which were onsite and 15 of which were off-site.

(i) <u>Regulatory requirements.</u>

The Payment Accounts Regulations (S.L. 371.18) which transpose the requirements of the Payments Account Directive, apply to payment accounts through which consumers are able at least to:

(a) place funds in a payment account;
(b) withdraw cash from a payment account; and
(c) execute and receive payment transactions, including credit transfers, to and from a third party.

Additionally, Regulation 2(1) of the abovementioned Regulations clearly defines that "fees" means all charges, tariffs, and penalties, if any, payable by the consumer to the payment service provider for or in relation to services linked to a payment account.

Consumers are to be provided with the Fee Information Document ("FID") in good time before entering a contract for a payment account as per Regulation 8 of the Payment Accounts Regulations, while the said FID shall meet the requirements set out in Schedule 1 of the same Regulations. This document is necessary for the client to be able to compare fees for the setting up of payment accounts, charged by different credit institutions.

In addition, as stated in Regulation 9, the payment service provider is required to ensure that the FID and the glossary of terms are made available at any time, in both electronic form on the Institution's website and also made accessible to consumers when visiting the premises of the payment services provider. Furthermore, the FID is to be provided to clients upon their request and free of charge, in hard copy or another durable medium.

The above-mentioned Regulations also defines *"Bundling"* as the offering of one or more ancillary service with a payment account in a package, where the payment account or the ancillary service may also be made available to the consumer separately, but not necessary on the same terms or conditions as when offered bundled. Regulation 14 tackles such scenarios and payment service providers are required to clearly provide all the necessary information to clients while also reflecting fees applicable in the context of such bundled products or services in the FID.

Part 4 of the Payment Accounts Regulations relates to access to payment accounts.

Regulation 17(1) specifies that credit institutions shall not discriminate against consumers legally residing in Malta or in another Member State by reason of their nationality or place of residence or by any other reason referred to in Article 21 of the Charter, the Equality for Men and Women Act.

Additionally, Regulation 19 highlights the eligibility criteria for clients to open a payment account with basic features.

Credit institutions should also provide the consumer with detailed information about the application process for the opening of a payment account with basic features. Such information is to include the application form as well as a list of documents required to be submitted with the application form, as required by Regulation 20 of the Payment Accounts Regulations.

On the other hand, Regulation 24 specifies that a credit institution shall not give access to a payment account with basic features on condition that a consumer is to purchase any additional services.

Credit institutions should adopt and follow the Payment Accounts Regulations, so that clients are provided with the necessary information to be in a good position to take an informed decision when deciding which payment account best suits their needs. In addition, all individuals residing in Malta or in another Member State have the right to a payment account with basic features irrespective of the nationality, financial background and if he/she has a fixed address as per the definition of *"legally resident in Malta or in another Member State"* in Part 1 and in Regulation 19 of the Payment Accounts Regulations (S.L. 371.18).

(ii) <u>Objective</u>

The main objective of the exercise was to assess whether clients, when approaching a credit institution to enquire about opening a payment account, are being provided with the full portfolio of payments accounts available (including the payment account with basic features) and whether the clients' needs are being identified. Following this, the FID related to the payment account which best meets the clients' needs is to be provided. The Mystery Shoppers investigated the information provided by credit institutions on the conditions required to open a payment account, the personal information which needs to be provided to the bank by the client, the disclosure of the costs associated with the accounts and respective services together with any reference to optional services offered with the account.

(iii) Onsite Observations

During the face-to-face interactions, it was observed that basic prerequisites to open an account were required, namely ID card number, payslips and a minimum deposit. It was noted that the personal information asked for by the credit institutions was necessary to build a client's profile for both identification purposes and to identify the level of expected activity in the payment account.

It was observed that that in 43% of the interactions, mystery shoppers were provided with information about only one main type of payment account, while 40% were informed on a portfolio of accounts **but no reference** to the payment account with basic features was made in this case. Only 11% of mystery shoppers were provided with information about the banks' full portfolio of payment accounts provided, including the payment account with basic features.

The Payment Account with Basic Features was rarely offered to mystery shoppers. In fact, only 11% of the mystery shoppers were introduced to the said account.

Client facing staff at credit instructions tend not to go through all the fees associated with the payment accounts when explaining such accounts. Staff in 40% of the interactions actually stated that there are no applicable fees. Only 34% went through associated costs with a payment account while only 11% went through the costs associated with the services offered with the account.

Although the FID provided by credit institutions to the mystery shoppers during the exercise included all the services provided, linked to payment account, the mystery shopping exercise revealed that, during onsite visits, 63% of credit institutions included in the sample **did not** provide the FID to mystery shoppers.

Identified Bad Practices

In nearly 75% of the interactions, the mystery shoppers were not offered the optional services which the banks provided with other payment accounts. This practice hinders the clients from being informed about the full features associated with payment accounts, hence limiting the potential available to execute both local and international payment transactions.

(iv) Offsite Observations

The results of the mystery shopping exercise show that more detailed information was provided to clients during phone calls, followed by email and chat. The Authority noted that the level of information obtained by mystery shoppers through these channels differed from the level of information obtained through an on-site visit. This shows that there is inconsistency in the level of information provided depending on the medium which the client choses to communicate with the credit institution.

Mystery shoppers were not consistently informed about the payment account with basic features when discussing the different types of payment accounts available. A low percentage of credit institutions mentioned the payment account with basic features as part of their portfolio together with other types of accounts. Mystery shoppers were also not always provided with the full array of products for the client to take an informed decision when choosing the most appropriate payment account which meets the client's needs.

Additionally, similar to the situation in face-to-face interactions, information on costs was generally provided but there was no consistency in the level of information provided. There were instances when staff explained that the account has no fees. In very few instances, mystery shoppers were informed of costs associated with the services offered with the account.

Online Chats emerged as the least accessible informative means of communication for clients to be provided with essential information.

As was the case with onsite interactions, basic information to open a payment account was required, namely ID card, payslip and residency. Such requirements are essential for identification purposes and to meet AML obligations.

(v) <u>Identified Bad Practices</u>

The Authority observed that the channels used by credit institutions for the provision of FIDs to prospective customers were in most of the cases either through publication in their respective website or provided to mystery shoppers through email or chat only following a prompt by the mystery shopper.

Conclusions and Expectations

It can be noted that in general, bank staff are not providing the FID at enquiry stage. Offering the FID at such an early enquiry stage would enable the clients to easily compare similar information with respect to other accounts in order to take a fully informed decision which payment account to choose from a portfolio of payments accounts available. Furthermore, it appears that the optional services linked to the accounts are not being discussed with clients (e.g. the possibility of effecting outward payments and the use of a debit card), hence clients are not being made aware of the potential services they can use associated with the accounts being discussed in order to have more accessibility to the financial services sector.

Costs need to be clearly discussed and highlighted, while it may be the case that there are no administration fees associated with the accounts, there may be other fees which account holders may be liable for in the context of the operation of the account itself which should also be disclosed. Such fees may relate, for example, to dormant deposits, overdrawn balances, etc. Furthermore, the account holder may also be subject to fees when utilising services associated with the accounts such as online payments. The latter fees must still be explained to the client when discussing the product, as otherwise, there is a risk that a client may get the wrong impression that there are no fees whatsoever associated with such accounts. Once the client is inclined towards one or more payment accounts, the respective FID is to be provided to help the client in taking a concrete, sensible and informed decision. It is expected that such fees are also disclosed at a very early enquiry stage.

The Authority noted that the level of information provided by credit institutions through off-site options needs improvement, so that clients would be provided with clear and concise information irrespective through which medium information is sought. Information from websites is to be more easily accessible especially since the industry in general is encouraging clients to access information without the need to physically visit the bank's premises. The Authority expects that all call centre agents need to pro-actively provide full information to clients without prompting. Even at enquiry stage, bank staff should provide the FID to clients either electronically or in hardcopy so clients can conduct their own research before selecting the account depending on their specific requirements. In this context, it is expected that credit institutions provide frequent and ongoing training to staff members, especially those engaging in non-face to face interactions with clients and prospective clients, in order to ensure that they are in a position to provide full and accurate information at all times.

When discussing with clients the payment account options available, bank staff are expected to highlight the spectrum of options including the payment account with basic features, where this is offered by the credit institution. Only once the client has clearly indicated that s/he requires certain services which are not offered through a payment account with basic features, can the credit institution consider offering more sophisticated accounts to meet the client's needs.

3.0 Other General Conclusions and Expectations

In order to ensure that customers are being treated fairly, institutions should ensure that consistent approaches are being applied both in terms of the level of service and level of information being provided. This is applicable both to the services provided through different branches of the same institution and also for the information and services offered through off-site interactions (i.e. phone, email and chat), in view of the differences noted in the level of service. This is particularly important in the context of the move towards digitisation as the customer should be provided with the same level of information about products, irrespective of whether the interaction is face-to-face or virtual/off-site.

Institutions should also remain mindful of the need to invest in competent and professional staff who possess a sufficient level of knowledge about products when dealing with customers. Continuous training to ensure that staff knowledge remains up to standard is a must and will also lead to more consistent approaches being adopted across the same institution.

Further to the above credit institutions are further encouraged to train staff in conducting a fact-finding exercise while gathering as much information as possible from the client, at initial stage, in order to be in a position to identify their customers' needs, so as to be able to propose the best options for the customer at the earliest stage.

4.0 Way forward

The ultimate aim of this exercise was to enable institutions to become more compliant with regulatory requirements, thereby enhancing consumer protection. The interactions carried out as part of this mystery shopping exercise have shown that there are gaps in effective compliance with the Payment Accounts Directive and the Consumer Credit Directive, as transposed locally through the Payment Accounts Regulations (S.L.371.18) and the Consumer Credit Regulations (S.L.378.12). In this regard, all credit institutions offering personal credit and/or payment accounts are expected to conduct a gap analysis in order to update their processes and procedures in order to come in line with the requirements emanating from such regulations. The Authority will engage with credit institutions in the future through other supervisory interactions in order to assess remediation to the above-mentioned observations.

Credit Institutions are encouraged to also go through the full EBA Report: Mystery shopping exercise into Personal Loan and Payment Accounts (EBA/REP/2023/30) referred to earlier in this letter.

Kindly be guided accordingly.

Yours faithfully
Malta Financial Services Authority

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