

BANK OF ISRAEL

Office of the Spokesperson and Economic Information

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Press Release

Initiated marketing of consumer credit: Examination report findings and Banking Supervision Department requirements

* **Consumer credit is a focus of the Banking Supervision Department’s work in recent years, from both consumer and prudential standpoints. Following an assessment of risk in the credit portfolio, the Banking Supervision Department has taken a number of steps—supervisory guidelines, monitoring and gathering of information, data analysis, examinations and requirements—which led to a slowdown in the growth rate of household credit.**
* **These measures are mainly intended to ensure that the credit is provided to customers who have a reasonable ability to repay, and to prevent customers without such ability or those who are financially weaker due to taking out surplus credit from getting entangled in debts.**
* **In the past year, the Banking Supervision Department has looked into the initiated marketing processes in the banking system, through examinations and other checks conducted by the bank’s internal auditors that it guided, found problems in some of the marketing processes, and required their rectification.**
* **In the coming year, the issue of consumer credit will remain a major focus as fulfillment of the Department’s requirements is monitored and a directive on the matter is published.**
* **This review provides details of the findings of the examinations the Department carried out, and sums up its requirements of the banking system in the area of initiated marketing of consumer credit.**

In recent years, the Banking Supervision Department has given greater attention to the consumer and prudential aspects of the increase in credit to households.

From the prudential aspect, the Department has taken a variety of measures to assess and limit the risk in the consumer credit portfolio. In January 2015, it required making a conservative loan loss provision in order to illustrate in advance the developing risk in this area. Additional examinations and checks were made at the banks, as part of which the underwriting, monitoring and control processes were examined. The Department showed the risks in the consumer area to the banks’ management and boards of directors to make sure that they would act as necessary. The Department also analyzed the distribution of credit in the economy by income level, and published the analysis to the banks and the public.

The Banking Supervision Department’s measures led to a slowdown in the growth rate of credit provided to households by the banks in the past year.

From the consumer aspect, the Banking Supervision Department required that credit marketing be aimed at customers with the ability to repay, in order to prevent financial entanglements among economically weaker population groups. In addition, the banks were required strictly uphold proper marketing practices toward their customers. The central credit register that is expected to go online in 2019, which is one of the important projects being led by the Bank of Israel, will make it easier for all lenders, banks and nonbank entities, to properly assess the customers’ repayment capacity based on full information, in order to prevent the provision of credit to customers who do not have the ability to repay.

The Banking Supervision Department has placed a special emphasis **on the initiated marketing of credit to households** by the banking system—a process by which the bank approached a specific customer with an offer to provide credit—at branches, through digital channels, by phone, and even during the handling of another request from the customer. While this practice exists in Israel and abroad, initiated marketing also carries risks for customers. For instance, during an initiated contact, the customer generally does not have sufficient opportunity to assess all of the conditions or to compare prices with other credit alternatives in the market, or to assess the overall burden of liability so that he can properly plan how to repay the credit.

As such, the Banking Supervision Department provided written instructions to the banks and the credit card companies in 2015 on how to make an initiated approach to customers with a credit offer. The banks are required to set out in their policy the target groups for their initiated marketing, and to exclude from it groups of customers that do not have the ability to repay, as well as other groups of customers (such as the very elderly or very young). We emphasize that these groups were excluded from initiated marketing only, but they can obviously still approach the banks to request credit at their own initiative, and each request will be judged on its own merits. In addition, the Department required the banks to make sure that the credit solutions are consistent with the needs of the customers.

**In the past year, the Banking Supervision Department has examined the initiated marketing of consumer credit in the banking system through examinations and other checks.**

**These examinations showed that in general, credit is marketed to customers with a reasonable repayment capacity, and there was no phenomenon of “pushing” credit to customers who could not repay it or to financially weaker customers.**

**However, the Banking Supervision Department did identify other problems in the marketing processes in some cases, and it is monitoring their rectification in accordance with its requirements:**

* Banking corporations are required to make sure that their employees, at branches and call centers, **do not apply any pressure** on customers to obtain credit services. Examinations conducted by the Banking Supervision Department found certain cases where call center employees acted to convince customers to take a loan even though the customers had said they were not interested. It was found that the improper convincing in those cases included repeated offers, applying pressure on customers to decide “today”, and the use of inappropriate verbal coercion.
* The Banking Supervision Department is requiring the banking corporations to prepare for a mechanism that **will prevent the harassment of customers** with repeated offers of credit after they have said they are not interested in the service, and is even instructing the banking corporations to prepare for the implementation of a mechanism that will allow customers to give prior notice that they are not interested in initiated contact from the bank. This is due to cases that were found where call center employees contacted customers with repeated offers to obtain loans, even after the customers said they were not interested or refused the offers.
* The Banking Supervision Department is requiring the banking corporations **to increase the disclosure they provide to customers** by improving guidelines for conducting a conversation with a customer and increasing controls over the conversations in practice:
  + The banks must bring to the customer’s attention, at the beginning of the conversation, **the customer’s financial state in the account, both on the debit side and on the credit side.** In particular, the banks must bring to the customers attention details about deposits that are available to them, including their date of repayment and their interest rate. The objective is to enable the customers to make an informed decision on whether to take out a loan or to withdraw a deposit, in view of the interest rate differentials between the two. In financial terms, the use of a deposit is generally more worthwhile for the customer than taking out a loan, since the interest that the customer receives on a deposit is much lower than the interest he would pay on a loan.
  + Another example is the requirement to **advance disclosure of the interest rate on the loan** offered at the beginning of the marketing conversation, and before the customer has formed his opinion on the offer. This requirement is due to the work process in some cases where the sale is comprised of two stages: In the first conversation, the customer gives his agreement in principle to submit a request for credit before the bank tells him what the interest rate is, and the bank updates him regarding the approved interest rate only in the second conversation. The Banking Supervision Department wants to make sure that the customer understands what the interest rate is and considers it at an early stage of the sales process, before giving his agreement in principle to submit a request for credit.
  + The disclosure of the interest rate is especially important in cases where the customer is offered a loan to fully or partially pay back previous loans. From a financial standpoint, it is generally not worthwhile for a customer to recycle existing loans with a more expensive loan. The exception to this is a customer that is having difficulties repaying the loans, and the recycling is required in order to spread out the payments.
  + The banks must make sure to bring interest rate benefits to the customer’s attention, insofar as an existing customer is entitled to such a benefit based on a general arrangement (belonging to a certain segment of the population, such as soldiers, students, and so forth), or based on special agreements (for instance agreements that apply to certain groups of workers).
* The Banking Supervision Department is requiring that the banks make sure that loans offered through direct channels **are not more expensive** than loans offered to customers at branches. The Department’s position is that technological improvements enable the banking corporations to streamline and to offer their customers services at lower prices. This position also applies to the price of consumer loans.
* The Banking Supervision Department is requiring the banking corporations to make sure that **the variable pay mechanisms for employees who market credit are not based on personal credit sales targets** or on other targets that may encourage aggressive marketing and increase risk. The Department found that variable pay based on personal targets may increase the risk of marketing that does not meet the appropriate disclosure and fairness standards.
* Another material requirement of the Banking Supervision Department is intended to ensure **an organizational culture of the customer’s best interest** in the bank’s operations. As such, a requirement was presented **to increase control and examination of the consumer credit provision processes**, and particularly the initiated marketing conversations, by gatekeepers at the banking corporations—controllers, legal counsel, compliance, risk management, and internal audit—in order to ensure that all of the banking corporations’ obligations toward their customers are met.

The Banking Supervision Department is continuing its work on consumer credit, and in the coming year, it will monitor the rectifications of the deficiencies that were found. It is also preparing for the publication of a specific directive on the marketing of consumer credit by the banking system.

**Summary of the Banking Supervision Department’s requirements:**

**The “Do”s and “Don’t”s of initiated marketing of consumer credit**

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