Remarks by
John D. Hawke, Jr.
Comptroller of the Currency
Before a Conference Sponsored by
The Consumer Bankers Association
Robert Morris Associates
San Francisco, California
June 7, 1999

Last November, when I was awaiting the White House announcement of my appointment to serve as Comptroller of the Currency, the then Acting Comptroller, Julie Williams, made a speech on customer service. It was a speech that I'd long thought needed to be given and had been looking forward to giving myself as Comptroller.

The thrust of her remarks seemed irrefutable -- at least to me. She began by sketching the historical evolution of bank supervision -- from the days when it consisted of a simple measurement of a bank's internal management and core operations, to today's broader, more encompassing approach of assessing risk in all its manifestations -- political, social, and economic.

And that brought her to the central point. "Bankers," she said, "need to weigh their business decisions -- decisions that might be perfectly above-board from a legal or regulatory standpoint -- against the reaction those decisions might elicit from the customers and communities they are chartered to serve." "They need to be aware," she added, "that actions perceived by a customer to be unreasonable or unfriendly may trigger a backlash whose costs can easily exceed the narrow value of that customer's business." Indeed, she argued that perceptions of deterioration in bank customer service had already hurt the industry in its efforts to achieve its legislative goals. By working to improve customer service, she concluded, banks had an opportunity to swing public opinion more to their side.

Generally, the speeches of bank regulators have a short shelf life: you read about them in the trade press for a day or two, and that's that. But Julie's speech sparked a spirited debate that lasted for weeks. Some people were startled -- even offended -- that a regulator would depict customer service as a safety and soundness issue. Others suggested pointedly that regulators keep their noses out of the banks' lawful relationship with their customers and let the free market do its job. After all, they said, if customers don't like the service they're getting, they're always free to take their business somewhere else.

But most commentators called the speech timely and important. Said one banker, "we as an industry would be better off paying attention" to the customer service problem than "to deny it or make excuses about it."

I applaud that kind of candor. I belief that customer service is a subject that clearly falls within the OCC's purview -- for all the reasons Julie cited and for a few more. Of course, while it's important to generate discussion, it's even better if a speech leads to constructive action. The industry's progress -- or lack of it -- in dealing with the customer service issue since Julie delivered her speech is what I'd like to talk to you about today. And I'd like to discuss the work of the OCC's customer assistance group --

one way we're trying to help bankers to do an even better job of meeting their customers' service expectations.

First, Julie was absolutely right in affirming that customer service is a safety and soundness issue -- that is, unless you hold the view that a bank can afford to alienate its customers and damage its reputation without weakening itself. History is replete with cases of whole industries brought to the brink of extinction because a "customer be damned" attitude became embedded in the corporate culture. During the late 1970s and early 1980s, for example, the domestic auto industry's indifference to customer satisfaction and changing customer preferences cost it a huge piece of the U.S. market -- a loss it's still struggling to recoup.

Banks could afford to turn a deaf ear to their customers if there were no place else for their customers to turn. But that's clearly not the case. Just as American households turned to foreign auto manufacturers 20 years ago, consumers of financial services have a wide choice of nonbank suppliers today. Competition has never been stronger, and, more than ever, customer service is a key competitive battleground. It concerns me -- as I know it concerns you -- that an increasing number of nonbank competitors are making a selling point of their nonbank status. When advertising stresses, "we're NOT a bank," and promises a higher level of responsiveness, local decision-making, and customer service, it highlights a problem of major proportions for banks.

Customers all too frequently have negative predispositions about banks, and bank practices too often validate them. For example, some institutions' penchant for piling on fees and penalties reinforces the stereotype of the banker as Scrooge. Customers often don't understand why they should have to pay to gain access to their funds, or why talking to a teller might warrant a surcharge. <u>You</u> know that all bank services are delivered at a cost, and that you can't last long giving away products and services for nothing. But banks generally have not done a good job of explaining this fact of life to customers.

Industries that regularly win higher scores for customer service are likely to become your most significant future competitors. The computer software industry, for example, always ranks near the top in consumer surveys -- a fact that should worry traditional bankers, given the rapid growth of on-line financial transactions. Merrill, Lynch just last week announced a major move into electronic delivery of financial services. To suggest that the competitive challenges you face from those quarters are unrelated to the safety and soundness of the banking system and the value of the bank charter strikes me as woefully misinformed.

It's also the OCC's responsibility under the law to ensure that consumers are protected in their dealings with national banks. Unfortunately, there's mounting evidence of an increase in banking practices that are at least seamy, if not downright unfair and deceptive -- practices that virtually cry out for government scrutiny.

Two particularly objectionable practices have recently come to our attention. The first involves financial institutions that, without letting customers know about it, have stopped reporting consumer credit lines, high credit balances, and payment records to credit bureaus. Some lenders, in particular, appear not to be reporting their payment experiences with subprime borrowers in order to protect against good customers being picked off by the competition -- even though these customers may have been lured into a high-rate loan as a way of repairing a bad credit history. These high-interest borrowers may be rudely surprised when they discover that their good credit history as a subprime borrower isn't reflected in their credit files when they seek credit in the future and that they are unable to obtain better rates based on their good credit record.

Failure to report may not be explicitly illegal. But it can readily be characterized as unfair; it may well be deceptive, and -- in any context -- it's abusive. OCC staff has been discussing this issue with the other banking agencies and with the Federal Trade Commission staff, and is working to develop a joint supervisory response to this practice. But that may not be the end of it: Congress is already homing in on the problem.

The second item involves the sale of personal customer financial information to telemarketing firms. What's happening is basically this. A bank will enter into an agreement with an unaffiliated telemarketing firm under which the bank provides extensive confidential customer information in return for a commission on sales made by the marketing firm. And the information goes well beyond mere lists of names. It also includes addresses, telephone numbers, social security numbers, dates of birth, credit card numbers, checking account numbers, account balances, credit card purchases, last payment dates, occupations, marital status, and credit scoring information.

With this information, a telemarketer can profile bank customers and offer so-called "trial memberships" most likely to appeal to a particular customer. If a customer indicates an interest in seeing materials about the offer or expresses an interest in the trial membership, his account at the bank is automatically charged by the telemarketer -- without the customer ever divulging his account number, much less knowingly authorizing the charge or withdrawal.

In many cases, the customer may not realize that he's being charged unless he spots and questions an unfamiliar item that appears on his monthly statement. And in many cases, the "trial" membership automatically converts into a continuing series of monthly charges unless the customer affirmatively "opts out" of the program. The disclosures provided to a customer about the need to opt out in order to avoid continuing charges often leave much to be desired, and the bank's published privacy policies frequently fail to make reference to this use of confidential customer information.

In my judgment, this practice raises a number of serious legal concerns, which we and others are currently reviewing. Judging from the calls we receive from state attorney general offices around the country, the scope of the concern may be widespread.

In addition to the legal issues, however, one must be troubled about the implications of this practice for the preservation of customer confidence in the confidentiality of the bank-customer relationship. We heard loud complaints from many in the banking industry that the now-defunct Know Your Customer regulation would do severe damage to customer confidence -- as I believe it would have. But there doesn't seem to be the same sensitivity about damaging that relationship when there are commissions to be earned from the sale of confidential information.

Issues surrounding the transfer of customer information already have lent momentum to proposals for new federal legislation, and the emergence of practices such as I've described will only increase the likelihood of new legislation.

And that brings up the third reason why customer service is a legitimate public policy issue for bank regulators. What Julie warned about in her November speech -- the risk that consumer complaints would translate into legislation that the industry may view as adverse to its interests -- now seems more real than ever before.

One can review the history of consumer protection legislation over the past three decades and see one common and compelling theme: consumer abuses that are allowed to continue without being addressed by the industry are eventually addressed through regulatory legislation. And this audience knows as well as any that the cure can be more painful than the disease. Truth in Lending, Fair Credit Billing, Fair Credit Reporting, and Truth in Savings were legislative responses to clear abuses the industry proved unwilling to address on its own. These enactments not only created significant compliance burdens for the industry, but vastly expanded the enforcement responsibilities of the banking agencies, and added significant complexity to the traditional process of safety and soundness examination.

While it might be unfair to burden an entire industry with legislation aimed at curbing the poor conduct of a few institutions, the persistent failure of the industry itself to address abusive conduct creates a fertile seedbed for legislation. Perhaps it's too late for industry codes of conduct, self-policing arrangements, or even statements of best practices to relieve the burdens of regulatory legislation already on the books. But it may still be possible to avoid new legislation crafted to remedy today's excesses.

What's needed, in my judgment, is for the leaders of the industry, including the Consumer Bankers Association and RMA, to speak out on these issues. You must emphasize to Congress and the American people that the banking industry stands ready to take the steps necessary to clean up its act. If you are unable or unwilling to develop an industry self-regulatory mechanism, or to promulgate codes of conduct with incentives for voluntary compliance, you can at least assist in that effort by providing guidance on the kinds of practices that are and are not acceptable. In my view, the banking industry's response must be prompt and unambiguous in order to stem the tide of corrective legislation.

This represents a significant challenge. And while it's not our job to draft standards of fair conduct, we can help banks to respond more effectively to consumer issues and concerns. In fact, over the past year, we have -- quite unexpectedly, I should add -- amassed a significant amount of information about bank-customer relationships that can be of real value to bank management seeking to upgrade its service.

In April 1998, the OCC installed a state-of-the-art consumer hotline system at our customer assistance center in Houston. Although we have not widely advertised or promoted this facility, our call volume has grown dramatically. In 1997, before we installed the new system, our customer assistance group logged some 16,000 consumer complaints. In 1998, the number rose to more than 68,000. And, if the complaint volume during the first quarter of 1999 holds for the entire year, we should be well over 100,000 this year. Again, that's without any promotion on our part.

Our approach to this operation is not regulatory- or compliance-oriented. We are not seeking out violations of law. Most of the complaints we receive are the result of a breakdown in communications between a bank and a customer. We lend our good offices to the resolution of disputes. If the customer's complaint lacks merit, we're frank to say so. In my view, this operation has been a great success, for both customers and banks.

What's most disturbing, however, is the large number of complaints we receive about bank practices -- such as those I've already mentioned -- that, intentionally or not, violate the letter or the spirit of consumer protection laws or that clearly strain the boundaries of ethical conduct.

I think of our customer assistance center as performing two critical functions. First, it provides an outlet for consumers, where their complaints will receive prompt and efficient attention. Second, it adds value to the supervisory process by giving bankers insight into their customers' assessment of the service they provide. A number of national bank CEOs to whom I've spoken have expressed surprise at learning the extent of the service problem, and I suspect most CEOs or boards of directors never learn through internal processes about bad customer assessments of their service, or about questionable practices at the marketing level. The information collected by our Houston unit can inform senior management where steps are necessary to improve the quality of the service their banks deliver. It can also point toward internal processes and control weaknesses that they should be interested in fixing.

Of course, when we find that consumer protection laws have been violated, our response will be firm. But shoddy and unethical practices, marketing schemes that overreach or exploit, and offensive sales techniques may not be currently sanctionable under the law. It's very much in the interests of the banking industry <u>and</u> its customers to eliminate such conduct. Effective self-policing should be undertaken as a matter of enlightened self interest -- not only to improve customer relationships, but to demonstrate to Congress that new regulatory legislation aimed at curbing abuses by banks is not needed. The industry's future could well depend on how it responds to this challenge.