

Recommendation No. 9 of 2006 (XI. 7) of the Board of the Hungarian Financial Supervisory Authority

On the principles of retail crediting provision of preliminary advice to clients and consumer protection

I. Aim and effect of the recommendation

The objective of the Hungarian Financial Supervisory Authority (hereinafter 'HFSA') is the promotion and continuous supervision of the prudent and efficient operation of financial organizations and the sensible exercise of the members' rights in order to protect the clients of financial organizations, to ensure the transparency of financial market relations, to strengthen confidence in financial markets and maintain fair market competition. The Board of HFSA creates and publishes recommendations as part of its activity. The purpose of the recommendations is to increase the predictability of legal practice and support the uniform application of legal regulations.

The aim of this recommendation is to define uniform principles and requirements that are advised to be followed by financial institutions in customer relations for retail crediting purposes.

II. Reasons for issuing the recommendation

- The market practice whereby financial institutions more and more often fail to pay sufficient attention to get to know their clients' financial capabilities, their household assets and incomes, even though these are the grounds on which loans may responsibly be provided, is worrisome. This is neither in line with the prerequisites of prudent operation nor with the need to adequately inform customers.
- Furthermore, as it may be noticed, consumers' general financial culture and knowledge can hardly keep pace with the quick development of the money market sector, products that are more complex and increasingly difficult to understand for clients appear on the market due to the continuous product innovation. Consequently there is an increasing danger that in lieu of adequate information clients of financial institutions undertake long-term commitments, the advantages and disadvantages of which are not sufficiently known to them.
- in addition to that the Authority has come across market practices in the course of its activities, although not in conflict with the statutes, are objectionable from a consumer protection perspective due to the lack of information.
- Such harmful phenomena can be avoided by financial institutions delivering clear and thorough information to clients, furthermore, by financial institutions complying with certain generally expected consumer protection principles.
- in light of the above the Board of the Hungarian Financial Supervisory Authority finds it necessary to set forth the most important principles and requirements applicable to this subject in a recommendation.

Expectations from the application of the recommendation:

- More attention should be paid by financial institutions to the interests and financial capabilities of customers simultaneously improving client information and their chance of representing their interests.
- Financial institutions should take a responsible role in preventing their clients' indebtedness beyond their financial capabilities.
- Crediting by financial institutions should be done in accord with the relevant consumer protection principles.

The addressee of the recommendation

This recommendation is addressed to financial institutions and their agents (hereinafter together 'financial institutions') in respect of loans and money lending as financial services.

The norms applicable to the issues discussed in the recommendation are to be found particularly (but not exclusively) in the statutes listed below. This recommendation intends to describe the applicable legal practice in terms of the provisions to be found there notwithstanding the provisions of the referenced statutes:

- Act CXII of 1996 on credit institutions and financial enterprises (hereinafter "Credit institutions Act");
- Government Decree No. 18 of 1999 (II. 5) on conditions regarded as unfair in contracts concluded with consumers, in particular, Section 2.d) on the unfair stipulation of the right to unilaterally amend the contract;
- Sections 12 and 13 of Government Decree No. 41 of 1997 (III. 5) (hereinafter "Government Decree") on the calculation and disclosure interests on deposits, the yield of securities and the total cost of the loan[1];
- Section 8 (3) b) of Decree 14 of 2001 (iii. 9) of the Minister of Finance on the rating and evaluation of receivables, investments, off-balance sheet items and collateral (hereinafter "Minister of Finance Decree");
- 2001/139/EC [G1] Commission Recommendation of 1 March 2001 *on pre-contractual information to be given to consumers by lenders offering home loans* (hereinafter "EU Recommendation")

This Recommendation is in line with the above referenced recommendation of the European Commission, the requirements of which have been incorporated and additional advices are presented in light of the particular features of the Hungarian credit market.

No references are made to statutory provisions in this recommendation when the principles and expectations are set forth, however, the Authority continues to expect compliance with the statutes wherever they stipulate requirements that go beyond these recommendations.

The Authority has not published a recommendation on the subject discussed here before. At the same time Recommendation 15 of 2001 of the Chairman of the Authority on the information to be provided to customers by financial organizations dealt with the subject more comprehensively and universally. In this recommendation the Authority set forth the principles of informing clients (consumers) of all financial organizations, such as the principles of informing by advertisement and provision of information prior to contract negotiation. Recommendation 1 of 2006 (ii. 27) of the Board of HFSA should also be mentioned here, however, this only stipulates the principles to be employed for informing clients using investment (asset) management services.

III. Principles of preliminary customer information and consumer protection for crediting

1. Financial institutions shall engage in responsible crediting practices conduct, that is, they shall assess the needs and financial capabilities of their clients. Financial institutions are advised not to engage in crediting without regard to their customers' risk bearing capability in order to improve sales indicators.

A. Principles for preliminary customer information

2. Once the customers' needs and objectives are known financial institutions should clearly and unambiguously inform their clients about the products that correspond to the said objectives. The aim of this verbal or written (such as product brochure) communication is to help the client to select the product that fits his/her needs, therefore, it must include at least the following information:

A – Lender:

- a) name and address of the lender;
- b) name and address of the intermediary, if necessary;

B – The loan:

- a) possible loan purposes;
- b) application criteria;
- c) the form of other possible securities depending on loan application evaluation;
- d) possible loan amounts and terms;
- e) a brief and clear presentation of the loan with a description of the types of loans including the explanation of the differences between fixed and variable interest products and their effects on the client;
- f) types of interest rates – fixed, variable and a combination thereof;
- g) indicating the costs of loan application evaluation to be borne by customer;
- h) list of additional costs payable to third parties;
- i) different options for the repayment of the principal to lender (including the number of instalments, their frequency and amount);
- j) whether early repayment is allowed (if so, what are the conditions and the implied costs);
- k) is a property valuation necessary and if so, who must have it done;
- l) total cost of loan;
- m) name of the financial institutions offering the relevant product in case an agent contacts the client;
- n) information on tax rebates on loan interest or general information on other public finance support, furthermore, information on how further information can be obtained;
- o) the length of the balance sheet preparation period, if necessary;
- p) proof that the institution has signed 2001/139/EC Commission Recommendation of 1 March 2001 *on pre-contractual information to be given to consumers by lenders offering home loans* (the codex)

including a note that a copy of the codex is available at the institution;

3. Once the client has selected a specific loan product and defined the key features of the required loan (loan amount and term) financial institution shall inform the client in writing with respect to the given application at least about the following, provided the amount to be borrowed by the client reaches HUF 500,000 and the term is not less than a year; the client may do without the information included in this section with a written declaration.

The purpose of this paper is to furnish the customer with detailed, yet clear and lucid information prior to the conclusion of the contract based on the credit need outlined with respect to all substantial elements of the contract to be signed and the loan facility.

- a) Brief and clear description of the product (possible securities);
- b) interest rates (fixed, variable, indexing, floating point interest rate);
- c) annual cost of the loan in terms of percentage;
- d) loan amount – in case of a foreign exchange loan the loan amount shall be given both in Hungarian forints and in the foreign currency, indicating the applicable exchange rates, while ensuring that the applied exchange rate is always in accord with the transaction, also indicating whether it is possible to take or repay the loan in foreign currency;
- e) term;
- f) number and frequency of instalment payments;
- g) an itemized list of all the different kinds of charges (expenses, including those payable to third parties, separately showing the fees payable in the event the application is rejected), the amount or percentage together with the payment due date, warning the client that in respect of third parties, furthermore, depending on the nature of the transaction and in case of variable interest rate loans there may be differences in these expenses;
- h) indicating the total cost of the loan in Hungarian forints (that is the total amount to be paid by the client to the credit institution or to any third party, such as interest, service charges, valuation fee, etc.);
- i) list of costs included in and excluded from the total cost of the loan;
- j) indicating the changes the amount of which may change during the term of the loan together with the reason that underlies the change;
- k) stipulating the way clients should be informed by credit institutions about potential changes in charges;
- l) the number and size of instalments and the frequency and method of payment; this should also be illustrated with a repayment schedule showing the following particulars for each repayment due in the first year and consolidated annually for subsequent years;
- m) monthly or quarterly payments;

n) annual payments during the entire term of the loan;

furthermore:

- principal repayment;
- amount of interest;
- amount of outstanding principal;
- amount of individual instalments;
- the sum of principal and interest.

it must be clearly indicated that the schedule is for illustration only, furthermore, if the loan has a variable interest rate, there must be a warning to that effect;

o) advance payment option, its terms and conditions and method of use and cost, or the lack of an advance payment option;

p) grace period, if any;

q) Other liabilities, such as: current account or insurance;

r) potential product risks (in particular foreign exchange risk, or in case of home loans the possibility of losing the property when purchase rights are required);

s) the documents to be submitted (number of copies indicating the type of document, furthermore, whether originals or copies of originals are to be submitted);

t) time needed for loan application evaluation (starting from the date when all necessary documents are submitted/made available);

u) persons at the credit institution (address, phone number) or organizations (such as conciliation body, mediator, etc.) the customer could turn to with his/her complaints.

B Principles for consumer protection

Based on the experience of the Authority in connection with certain crediting related consumer protection problems the following recommendations and principles to be followed may be offered.

4. In the event the financial institution makes a special loan offer the advantages of the promoted offer over the standard loans should be clearly shown and the duration of the referenced benefits should be indicated accurately, together with the quantifiable savings this could mean for the client.

5. Section 13 (4) of the Government Decree contains a provision, according to which the interest, any charge or instalment amount is shown in the advertisement of the financial institution, or in any third party's advertisement intermediating the loan of the financial institution, then the total cost of loan must also be shown using at least letters of the same size and identical display. For the purpose of this rule the expressions referring to "free loan", "discount interest" "no valuation fee" are also regarded as credit costs, therefore, whenever these expressions are used, the total cost of loan must be indicated displayed at least as these expressions are displayed. Obviously this shall not apply to information pertaining to the duration of the loan or to the own capital required, or pertaining to any other characteristics of the loan (such as "loan application evaluation in 24 hours" or "no employer certification is needed"). Financial institutions should publish their advertisements accordingly.

6. No financial institution shall regard the age of the customer automatically as a criterion of eligibility. institutions should consider various ways they could offer loans to elderly customers (e.g. requiring additional securities).

7. Agents of financial institutions shall inform their clients about the financial institution(s) they are acting on behalf upon meeting in person.

8. When being listed in the Central Credit information System (Központi Hitelinformációs Rendszer, KHR) is likely to imply the rejection the loan application the financial institution should confirm that the given customer is not included in the KHR list prior to submitting the loan application to spare the client from unnecessary expenditures. One way of doing that is to warn the client that inclusion on the KHR list is likely to result in the rejection of the loan application, therefore, the client is advised to take advantage of the once a year free check, if it is believed to be necessary. if the loan application evaluation is free for the client, inclusion on the KHR list does not have to be checked prior to the loan application, avoiding an unnecessary extension of the time taken by loan application evaluation and an increase in the bank's expenses.

9. All communication to the client prescribed by law in respect of KHR shall be clearly worded and presented in an easily readable format by the financial institution. Communication that is limited to statutory references instead of substantive information should be avoided. in case of personal customer contact all written communication should be supplemented by verbal explanation by the institution's staff, which should be clearly separated from the loan application or the contract negotiation. (in case of written communication using bold letters and/or italics, perhaps using a text box, in case of verbal communication in a way to make it clear for the client and the bank should confirm that the client has understood that.) in case information is forwarded the client should be informed in detail about the actually transferred information, not only about the range of data available for transfer in general.

10. Financial institutions shall stipulate the maximum length of loan application evaluation in their by-laws (from the date all the documents are submitted by the client and institutions other than the bank) and inform the client about this deadline.

11. Financial institutions shall strive to make the cost structure of their lending products as simple as possible and to charge fees under as few titles as possible. The main objective of that is to make the product and all related costs transparent for the client. The concepts employed must be clearly defined. Financial institutions shall simultaneously make sure that they do not make their products appear to be more attractive by highlighting the reduction of one type of fee, when the sum of all charges payable by the client do not decrease as other fees have increased.

12. in the event the prerequisite of lending is to have a life insurance policy as collateral (not including cases when the customer concludes a life insurance contract for the purpose of borrowing prior to the loan application), then this should be concluded only after the approval of the loan application in order to avoid a situation where the customer concluded a life insurance contract in vain with his/her loan application rejected. Furthermore, financial institutions shall make an effort to enable customers to select from the life insurance products of several insurance companies, if possible (e.g. it is not a group insurance built into the product).

13. Financial institutions shall not attach any other product or service to the contracted loan product as being mandatory, which by its nature does not belong to the given loan product, furthermore, the use of which cannot be justified with fair and rational market reasons (such as bank card with an annual fee). The financial institution should leave the use of such linked products / services to the clients' discretion and should not force clients to undertake unnecessary obligations. Exceptions are

when financial institutions make the use of some linked product mandatory proportionately to and as a prerequisite of providing certain benefits or discounts.

14. Financial institutions shall pay special attention to the presentation of risks that may lead to increasing the size of the instalment payments (such as interest risk) and warn the client about possible existential problems the potential increase of the amount of instalment payments may cause in the future.

15. In the contract concluded with clients financial institutions shall stipulate the due causes, in case of which they become entitled to unilaterally modify the terms and conditions of the contract. Financial institutions shall exercise their right to unilaterally modify the contract, only if the conditions stipulated in the contract effectively prevail. Simultaneously they should notify the client about the unilateral amendment of the contract adverse for the client (e.g. in a separate letter or on the statement and not only by way of a public announcement). Such a notice should include the reference to the amended document and the new provision as well.

16. Financial institutions shall determine the reasons and events for which they exercise their right to unilaterally modify the contract connected to specific individual charges or interests. The reason or event indicated shall be inherently tied to the cost implications of the given contractual elements at the financial institutions. (For example a change in the central bank rate cannot justify an increase in service charges.) The prevalence of the cause of the occurrence of the event must be clearly recognizable.

17. Implementing a unilateral contract amendment financial institutions shall always detail the economic and market reasons that persuaded them to modify the contracts (e.g. in press release or in briefing published on the institutions' website). Special care must be taken to ensure that the (increased) expenses are proportionate to the services provided. The fee increase should be used to cover effective expenditures and should not be employed to simply increase revenues or finance other losses.

18. If the contract provides the option for financial institutions to unilaterally modify certain fees in the event certain objective conditions change, then financial institutions shall strive to also take advantage of this opportunity when as a consequence of changes in such objective conditions a fee modification (decrease) favourable to the client is justified.

19. Financial institutions should forego advance loan repayment charges in the even a unilateral contract amendment by the financial institution causes significant disadvantage to the client and the client exercises his/her statutory right to terminate the contract. in the event the client asks for the modification of the contract (e.g. extension of the term), financial institutions should forego the contact amendment fee.

20. If an appraisal is prepared in connection with the borrowing and the client pays for that, then the client should have the chance to get to know the results of the appraisal prepared. Furthermore, one copy of the appraisal should be made available to the client.

21. Financial institutions shall allow ample time for the study of the draft contract and related documents (general terms of contract, general business terms and conditions, announcements).

22. Financial institutions shall make sure that their agents have all necessary client information brochures in sufficient numbers (general terms of contract and general business terms and conditions) and regularly check whether their agents duly inform their clients in accord with the relevant

regulations.

23. In case of contracts to be concluded new including purchase right to real property financial institutions shall allow their clients to sell their properties themselves during a predefined period (e.g. 90 days) before exercising the purchase right and make it possible to have the option price revised, for example by way of appraisal.

24. Should the client wish to transfer his/her loan to another financial institution, financial institutions should do everything they can not to hinder that process.

25. Financial institutions should do everything they can to correctly and quickly settle customer complaints in a fair manner. Should direct complaint settlement remain unsuccessful, financial institutions should cooperate with alternative forms of arbitration invited by the client.

III. Closing provisions

Recommendation is a legal tool issued pursuant to Article 9/C (1) c) of Act CXXIV of 1999 on the Hungarian Financial Supervisory Authority.

The content of the recommendation issued by the Board of HFSA reflects the requirements set forth in the statutes, the principles, methods, market standards and customs recommended based on the Authority's legal practice. The Board of HFSA stresses that financial organizations may incorporate the recommendation into their regulations. Should that be the case the financial organization shall be entitled to indicate that the concerned regulation corresponds to the relevant number of recommendation issued by the Hungarian Financial Supervisory Authority.

[1] "Teljes Hiteldíj Mutató" or "THM" a standard indicator, which stands for 'total cost of the loan'.

Attached contents

 [Annex 1 - Sample table \(46KB\)](#)



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 [Annex 2 - Sample table \(15KB\)](#)



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