ISSN 2508-3155 eISSN 2508-464X

The International Review of Financial Consumers

CONTENTS

Vol. 2, No. 2, 2017

The International Review of Financial Consumers, Volume.2 Issue.2(Oct., 2017), 1-13 pISSN 2508-3155 eISSN 2508-464X
https://doi.org/10.36544/irfc.2017.1-2.1

The International Review of Financial Consumers
www.eirfc.com

Development of Mutual Insurance in France: 1960-2017

Jean-Paul Louisot†

A B S T R A C T

Mutuality is the oldest social movement on French soil as the first mutual support groups were founded just before the French Revolution at the end of the 18th century, that is half a century before the first cooperatives and one century before workers' unions.

The tremendous development that the mutuality underwent in the second half of the 20th century in France, especially in the non-life insurance market where it was not a real actor until then, attracted the attention of professionals the world over. It is a reference that is even contemplated in the Islamic World where it could serve as a model for Takaful, and in developing countries where it could be adapted to micro-insurance.

Beyond their importance in the French insurance markets, both non-life and life mutuals insurance play an important role in European economy and society, providing social coverage and other types of insurance to a significant proportion of European citizens.

Some have questioned whether the liberal inspired European legal environment might threaten the future growth of mutual in the 21st century, or even the existing market shares, for a model that has proven efficient not only in its initial domain healthcare, but also in non-life insurance where it has really bloomed since World War 2. Following a presentation of the historic development of the mutuals in France since the Revolution, this article presents an overview of the specific features and roles of mutual societies in France, mentions relevant French and EU law applicable to mutuals, and considers the performance of mutuals through the financial crisis. The article takes the view that mutuals have the potential to contribute to the inclusive and sustainable growth of the European Union.

Keywords: Welfare, innovation, democracy, independence, solidarity, liberty, Solvency II, Takafuls, mutual governance, social security, change

Ⅰ. The early days of the mutuality spirit[1] and institutionalisation

The mutualist movement is rooted in the difficult social history of the 19th century. Confronted with mass poverty and governments mismanagement, citizens joined forces to create the first solidarity organisations. In a country that was still under a law that Jean Jaurès[2] called awful, short of calling it treacherous, the first initiatives in mutuality are the result of a deep yearning for Liberty, Fraternity, and Equality which is the motto of the French republic and yet far from being the reality of the society

† Université de Paris 1 Panthéon-Sorbonne
JPLOUISOT@aol.com

[1] Un engagement civique issu de l'histoire - Jean Sammut -Président de l'institut Polanyi France, fondateur de Procial, cabinet conseil en mutualité et économie sociale − The author recognises his debt to this paper which constitutes one of the founding source for the current article.

[2] Jean Jaurès was a French politician born in 1858 and assassinated on July 31, 1914 for his stance against World War 1. He was elected a member of the French Parliament in 1885. He took part in the foundation of the French Socialist party in 1905 (SFIO) and was at the forefront of workers fight for better working conditions and salaries.

at that time, when the lack of solidarity was obvious to social observers and activists.

- **From the Revolution to the Third Empire (1795 – 1970):** At the time of the final stage of the French Revolution, when Robespierre populism is definitely buried under the Thermidor liberalism and Bonaparte begins his march towards a new Empire, men and women of goodwill confronted with basic daily necessities share the little they have in excess of survival to face the unexpected. The penny for the shroud[3], one of the first mutual rescue societies to be traced, aims at making sure that corpses are not thrown naked in the mass graves, to paraphrase the words of a song popular among silk workers in Lyon in the 19th century.

  Mutuality sprung from this initial civic commitment, eluding the legal ban on coalitions, often with the active support of caring and philanthropic leaders. The pioneers, inspired by Proudhon socialist groups and autonomous groups advocating for federalist ideals, learned how to regroup the small groups to give enough impetus to the mutualist movement. It was soon a force to reckon with as it had a membership of more than three million at the end of the nineteenth century.

  The mutualist opened a market for collective protection that the first for-profit companies that were founded, capitalised on. Napoleon III[4] tried to take over the movement through the authorised mutual and strict control.
- **The Third Republic & the French State[5] (1971 – 1945):** Whereas Napoleon III and his government saw what could be gained politically and economically through the institutionalisation of the mutual movement, it was only nearly two decades after the Fall of the regime that the Third Republic granted the mutual a legal status in 1888, but it was not until 1998 that it voted a Mutuality Charter loosening the corset imposed by Imperial control.

  The French Government was fully aware of the risk that social movement might split because of the official framework the mutual movement was legally forced to comply with. In 1902, the first assembly of the national federation of French Mutuality (FNMF[6]), the Congress unifying the two branches of the General Confederation of Workers (CGT[7]), Labour Exchanges, and the Federation of Industries opened the gates for a clear separation of Unions and mutuality, each having a specific mission. As they focused on social demands, professional organisations condemned the mutual movement as a "social compromise".

  The situation will prevail all through the third republic, even during the government of the Popular Front[8] and even until the end of the 20th Century in spite of the change brought by the creation of Social Security in 1945.

Throughout this period, whatever their status, mutuals have remained true to their origin and Values; they are local structures established in a territory, a company, or an industry, and managed by committed citizens.

Ⅱ. A new start: the creation of Social Security in 1945

Whereas not all the provisions of the National Council of the Résistance[9] programme were enacted when General de Gaulle became head of the provisional government[10],

3 Le sou du Linceul

4 Emperor of France from December 2, 1852 when then president of the Second Republic he led a coup until the defeat of Sedan against Prussia on September 2,1870

5 L'Etat Français, the "collaboration" regime founded by Marshal Philippe Pétain that lasted while France was occupied by Germany during most of World War II,

6 Fédération Nationale de la Mutualité Française

7 Confédération Générale du Travail

8 "Le front Populaire" was a coalition of left leaning parties that want the 1936 general election and governed France until 1940 and enacted a number of social advances to benefit the workers; like paid vacations and limiting the number of hours worked weekly by employees and workers in spite of the number of short lived governments it went through

9 The Conseil National de la Résistance (CNR) is the body created by Jean Moulin under the guidance of General de Gaulle to unify and coordinate the different resistance movement that arose in France during the German Occupation. In March 1945 it adopted a programme for governing France upon its liberation. It was largely influenced by Communist thinking. It called for a social democracy and a planned economy including the creation of a national health and pension plan.

10 The first "gouvernement provisoire de la République" lasted from September 10,1944 to November 2,1945 and the second from November 21, 1945 until January 20, 1946. Both were headed by General de Gaulle.

and the ensuing governments until the establishment of the 4th Republic in January 1947, which did not meet all the promises for a social democracy, nevertheless one of the major points of the resistance manifesto became reality: it was this Republic that founded the Social Security that was meant to offer a universal health coverage and to be managed jointly by workers and employers' unions.

In February 1947, a specific act, Loi Morice, gave the Mutuality the right to establish local sections for social security, giving them a legal position as a body to complement the legal system. As far as civil servants' mutuals are concerned, another act dated April 9 gave them a delegation to manage the regime for state civil servants.

In spite, or maybe because of, the role the mutualist movement gained in the 1950s in the French social protection system, in the following years, it grew slowly distant from the vital labour forces. As the organisms regrouped and grew in size, the power in their midst was taken up by leadership. Therefor the social movement dimension of mutuality tended to fade away.

However, in the sixties, during the first year of the Fifth republic, a renewal started under the leadership of the president of the National Federation of workers; Louis Calisti was a leading figure of the mutuality movement in France during two decades (1970s and 1908s) and a proponent of a "mutuality of action and management". He was instrumental in bringing democracy and social commitment back to the heart of the movement.

In 1967, the move from strict political neutrality to a more elusive "independence in mutuality" represents a true overture to the other social actors that led the mutuality leaders to meet officially, for the first time in its history, the three leading workers' unions. This put an end to a long schism in the French social movement. As mentioned earlier the fraction in the labour movement was considered to be a consequence of the 1947 laws; the reality is that it dated back to the Third Empire when the control of mutuals was established as described above. Since then, the dichotomy between those who manage (mutualists) and those who demand (union activists) has been complete. Thus, the forces are united between workers' mutuals and those that are institutionalised.

The creation of the Federation of the Mutuals of France (FMF), which welcomed some mutuals that had been excluded from the FNMF, was the final act in the change of direction.

Proximity with the members, i.e. democracy, independence, solidarity and liberty are the true values, the four pillars, of the mutuality. They out-trump any numbers that can be deceiving as it seems unlikely that the leaders could call to action the membership as was the case in 1980. That was the year that over seven million signed a document denouncing the mandatory co-payment that limits the freedom of mutuals to reimburse their members as they see fit.

These founding principles are too often forgotten whereas they are the mutuality's best bulwark in its efforts to resist the increasing pressures from the insurance mega groups that see the health and social protection markets as great potential for growth in revenues and profits. Stock Insurance companies are funded on the law of large numbers but in a financial logic where each insured party should pay according to the risk he/she represents; conversely the mutuals, societies of persons are funded on solidarity.

At a time when liberal ideology is gaining momentum, when the individualisation of situations is more valued than collective efforts, when some leaders would push for biased competition rules, mutuality leaders must grow beyond the long-held certainties and face challenges they may have not anticipated. As a reminder, the 1985 reform of the code of mutuality gave a wider range of possibilities and new means for mutual companies. Have they all taken advantage of the new context?

Ⅲ. The adventure of the 1960's and the developments in Niort

So far, we have focused essentially on the mutual movement in the Health and Life markets but France is a case study of the development of non-life mutual insurance. However, the French Mutual movement has gained international attention mostly with the rapid evolution of a new breed of non-life insurers in the second half of the 20th century. They are known as MSI[11] as their distribution channel do not included intermediaries (agents or brokers) but salaried employees whose salary

[11] MSI – Mutuelles sans intermédiaire

are not related to the volume of contributions generated (note that Mutuals insist on not using the term "premium," preferring the term "contribution"). They are also known as *"Mutuelles Niortaises"* as the most important are headquarters in Niort, a town in Central France.

Jacques Vandier

Whereas the MACIF was founded through the initiative of a group of industry leaders and storekeepers in Niort, Jacques Vandier is the man behind its success story. Considered by insurance professionals as a great manager, even a visionary, he devoted the second half of his professional life to this mutual of which he was the first CEO.
Born in 1927 in the vicinity of Niort, he attended the École Polytechnique in Paris before starting his career in 1950 as an insurance supervisor, then as part of the Ministry of Finance.
In 1960, when he was offered by the founding partners to lead the MACIF he accepted on condition that the mutual would not only insure storekeepers and industrial companies, but also all the salaried personnel of commerce and industry.
He defined his business project: "At the time, insurance companies sold their products through a network of insurance agents and brokers and were charging high premiums. The rates did not reflect the reality of the risks insured, and were often highly overvalued. While working in the supervisory team, I had analysed the situation and knew how to remedy it. The solution was called risk segmentation. The key was to establish a taxonomy of risks based on a number of criteria – for automobile, territory, type of vehicle, insured profile – and then screen the good and the bad drivers to provide cover not to anyone, and not anyhow"
And he added: "Add to that a contract based on essential covers, very low overheads, and a closely monitored portfolio and the introduction of a deductible for damages to the vehicle. I wanted the insured, when responsible, to bear part of the cost of the accidents. It was both moral and empowering. This is the recipe I developed and implemented. If the MACIF business model has lasted for so long, it is because it was rooted in reality."
As he allowed the vast majority of drivers to find covers at a just cost, Jacques Vandier has democratised automobile insurance. All along his tenure at the helm of the MACIF, he multiplied initiatives in favour of the insured. He was one of the promoters of the "amicable accident report" that simplified and accelerated claim settlement. Members and the MACIF and their families were also among the first to be insured for bodily injuries occurring in the course of private life. He was also behind the regionalisation of the MACIF in 1987 so that partners be closer to decisions centres and increased substantially the number of insured representatives, the delegates.
Jacques Vandier was president of Macif until 1987, then he was chairman for 10 years; since then, he has been, and continues to serve as, Honorary Chair.

As a matter of fact, the development of mutuals in France is attached to the city of Niort whose expansion is the direct result of the large number of personnel employed by the mutuals. It remains to explained why Niort became the home of mutuality? One of the prominent explanation is that Niort became the cradle of peasants' solidarity following the phylloxera catastrophe that hit the vineyards in the 1850-1880 period. Whether this is historically true, Niort and the region saw the creation of the first peasant union in the early years of the 20th century as well as the first Agricultural Insurance.

This is the reason why Niort has grown into a "natural location for mutuals" since the 1930 as talents were present and further accompanied by the University offerings to prepare for the jobs the mutuals need to fill to ensure their future growth.

Below is a list of the major actors in Niort, each of which would justify a monograph that would go beyond the scope of this article:

- **MACIF**[12] – Mutuelle assurance des commerçants et industriels de France et des cadres et des salariés de l'industrie et du commerce. It is one of the two members of the union[13] created with the MATMUT under the name of SFEREN. It is the number 1 insurer in France for the number of insured (the prominent role played by Jacques Vandier justifies the box here above)
- **MAAF**[14] - Mutuelle d'Assurance des Artisans de France – Funded in 1950, Maaf developed in 2003 a group of insurance mutuals Covéa regrouping MAAF and MMA[15] further joined by GMF and then a welfare institution Apgis (2011) and SMI (2013). Currently Covéa insured more that 11 million French persons and employ 26,000.
- **MAIF**[16] – Mutuelle d'assurance des Instituteurs de France – The oldest actor in Niort it was funded in 1934. It has 3.5 million insured and total revenues in excess of € 3,200 million (over 80% in non-life,

[12] https://www.macif.fr/assurance/a-propos-du-groupe-macif/panorama-du.../dates-cles *https://www.macif.fr/assurance/a...du...macif/panorama-du-groupe*

[13] SGAM – Société de Groupe d'Assurance Mutuelle)

[14] *www.maaf.com/qui-sommes-nous/il-etait-une-fois-maaf*

[15] MMA – Mutuelle du Mans Assurance – A traditional Mutual Insurance using intermediaries

[16] https://fr.wikipedia.org/wiki/Mutuelle_d%27assurance_des_instituteurs_de_France

under 20% in life).

- **GMF**[17] – Mutuelle Générale des Fonctionnaires – Founded in 1934, it is specialised in civil servants and has played a leading role in the Mutuality movement
- **SMACL** – Société Mutuelle d'Assurance des Collectivités Locales – *(see development below)*

A. Mutualité Agricole

Outside of Niort, the largest professional mutual organisation in France is the Mutualité Agricole that is open to farmers and by extension to those employed in the food industry. One of the challenge of the Farmers' Mutual is the dwindling and aging population in this activity.

The group consist in many local branches, in principle one for each of the ninety departments (counties) in France, but they have been consolidated into a smaller number as the "insurable substance was diminishing" and to achieve economies of scale.

The Agricultural Mutual Benefit Fund is made up of 62 regional funds and a national fund and operates as a federation.

Recently they have formed a union with the Crédit Agricole, the Mutual Bank of the profession, which has developed both life and non-life traditional insurance companies to sell insurance through its networks of local branches. Crédit Agricole is one of the largest bank in the world in terms of total assets.

The farmers' mutual institutions would require a complete study that would be beyond the scope or this article.

B. Other professional mutuals

However, other professional mutuals offering covers to specific activities could not be left aside as they play a major role in providing coverage in sometimes niche but difficult markets like:

- **MAF** – for architects
- **SMABTP** – For construction and public work activities including, but not limited to decennial liabilitie s[18] and professional indemnity
- **SHAM** – For public hospital professional indemnity and buildings & equipment damage covers
- **MACSF** – For doctors in private practices and private hospitalisation facilities.

It is to be noted that these mutuals usually offer automobile insurance too and actively participate in risk-management development to assist their members while protecting the "mutuality".

Other trades also have generated mutuals but they are not listed here as they have a less prominent role. Also, the insurance companies, subsidiaries of mutual bank groups are not mentioned here as they really operate as traditional insurers although they are parts of the overall "mutual movement" in France.

C. Smacl - A French specialty – A mutual to ensure local authorities

It would be difficult to cover the mutual world in France without a specific mention for the SMACL at a time when the equivalent in the United Kingdom collapsed nearly two decades ago leaving at the time part of the insured without a solution for replacing their coverage except the Subsidiary of a Swiss Insurer – Zurich.

In the early seventies, school teachers, shopkeepers and artisans already had their own mutual company, but not local elected officials, in spite of the very specific exposures that local authorities and their staff are confronted with. This is this situation that prompted the creation of Smacl Assurances[19] in 1974.

After more than four decades in operation, Smacl has become the reference in France for the insurance of the "territorial family" and offers mutual protection to municipalities, department, regions, to their establishments and groupings, as well as to their elected officials and agents when the act within the scope of their functions.

Over the years, listening to the need expressed to the network of local inspectors or by the representatives elected by the members, and thanks to a very attentive study of new legal and regulatory dispositions as well as decisions by the different jurisdictions, etc. Smacl Assurances has developed an organization and coverage that are tail-

[17] https://www.gmf.fr/gmf/histoire-gmf

[18] Responsabilité Décennale - It imposes any party in the construction of buildings in France to provide a 10 years warranty, no-fault cover that must be insured for the duration of the warranty

[19] SMACL – Société Mutuelle d'Assurances des Collectivités Locales

ored to the operations, the constraints and the culture of players in the territories and local authorities.

Two mayors of Niort played a leading role in the creation and development of Smacl. M. René Gaillard was the mayor at the time of the creation and the operations were headed by an executive VP, Bernard Bellec, who later became chairman and succeeded him in the position of mayor.

Smacl has chosen to be specialised and is proud of its choices as:

- Local authorities' risks and operating modes are very different from those of industrial companies or private citizens,
- Legal protection for local authorities, their elected officials, and their agents (employees) relies on an in-depth knowledge of administrative law, specialized codes, and very specific case law,
- Private life risks are intertwined with elective or associative commitments as in the case of on-call work and the professional devotion of territorial civil servants; Smacl guarantees the consistency of all contracts covers,
- The values of Smacl, general interest, solidarity, transparency, equity, are also those that motivate the daily operations of local authority staff and elected officials.

Here below are key data to illustrate the position of the Smacl in the insurance market in France and its main recent initiatives:

Revenues:

- € 390.5 million in 2016
- € 372.6 million in 2015
- € 352.4 million in 2014
- € 341 million in 2013

Revenue split:

- Public entities: €329 million (84 %)
- Private entities *(associations & companies)*: € 44.4 million (12 %)
- Individuals: € 17.1 million (4 %) – 22000 members and 18,000 decision-makers for their private life.

SMACL Insurance penetration in Local authorities:

- 60 % of municipalities with less than 7,000 residents,
- 74 % of municipalities with between 15,000 and 40,000 residents,
- 70 % of municipalities with between 40,000 and 100,000 residents,
- 46 % of municipalities with more than 100,000 residents,
- 80 % of departmental assemblies,
- 33 % of communities of municipalities,
- 61% des communities of conglomeration,
- 39% des SDIS (firemen brigades).

Other data:

- Own funds: € 90.4 million
- Equalisation reserves: € 20.8 million
- Staff: 792 employees with an average seniority of nearly 10 years, and nearly two-third female employees, and a strong investment in further education (4.12% of salaries – twice the legal level)

Smacl-Santé: Although the historical business of the mutual is property and casualty damages for local authorities, in 2006 it created Smacl-Santé to offer health and welfare covers for local authorities' agents and it brings in over €20 Million in revenues.

"Territoires d'Avenir": As one of the increased cooperation movement induced by Solvency II, the mutual union (UGM), "Territoires d'avenir", was created on January 1, 2016. It makes sense as the partners are service providers to the same insured groups. The decision to form the Union was voted by the representatives of the *Mutuelle Nationale des Territoires* (MNT) and SMACL Assurances at the constituent general meeting on October 10, 2015 in Paris. It is a light structure to frame the cooperation between the members. A new member and two auditor-partners has been admitted at a meeting on December 5, 2016 effective January 1,2017. The new member is *Mut'Est*, and the two observers, *le Crédit social des fonctionnaires (CSF)* and the *Caisse nationale de prévoyance de la fonction publique (Préfon)*.

D. The current position of mutual institutions in the French Insurance Market

The table below summarises in a few key figures the important position that the mutuals occupy in the French insurance market.

It is clear that they have become a major actor in the economy of the country both through the coverage they offer and their investment capacity. The mergers or union movement initiated at the end of the last century gained impetus with the implementation of Solvency II and the lines are somewhat blurred between "true mutuals", the MSI, that sell directly to consumers without intermediaries and "mutual companies," which function like a traditional company, except that they do not have shareholders. The governance of both are theoretically similar but the insistence on democracy with the MSI has been somewhat lost in the other category, i.e. the mutual companies whose governance was closer to publicly traded insurance company.

Will the creation of the FFA-Assurances regrouping all insurers allow the mutuals members of the AAM preserve their values while gaining international momentum? Only time will tell but their weight in the protection of French citizens (see table below) should retain the attention of French authorities!

MAIN DATA FOR MUTUALS IN FRANCE

STAFF: 79 500

MEMBERS/INSURED: 44 Million *(French population in 2016 is close to 67 million)*

MARKET SHARES

• AUTOMOBILE:	56.0 % in 2016
• Household Insurance:	50.4 % in 2016
• Health/Welfare Insurance:	17.0 % in 2015
• Life/Assets Insurance:	13.2 % in 2015

The Association of Mutual Insurer (AAM) within the Insurance Association (FFA-Assurances) was founded on May 18, 2016

MUTUALS MEMBERS OF THE AAM: 36 including one partner-organisation; 110 companies are represented.

Ⅳ. Islamic Insurance & Takafuls

Although they are not developed in France, except for a few local and limited experiments, the percentage of the population that is Islamic should awaken the MSI to the potential for a new market if they decided to found Islamic insurance companies, or Takafuls.

Let us introduce briefly what Takafuls are and how the MSI could get interested in making inroads into the Islamic population, currently over 5 million, or 7.5% of the French population. However, some projections see it rising slowly to over 8% in 2020.

Traditional insurance contains elements of uncertainty *(gharar)*, game *(maisir)* and interests *(riba)*, which are not compatible with Islamic law. Generations of Muslims have lived in countries worldwide convinced that they are barred from purchasing insurance covers, that insurance is not *sharia compliant*. However, in 1985, the Islamic academy *Fiqh* ruled that insurance is acceptable to Islam if it operates through mutual self-help and cooperation, an important social tenet of Islam. The *Takaful,* whose name is derived from the Arabic word for "mutual guarantee" offers covers in a mutual framework. The policyholders (or members) pay contributions *(tabarru)* to a fund through which participants accept to bear collectively the risk of each one so that those participants who suffer a loss are compensated by the fund. The surplus that are not kept as reserves are paid back to the participants or distributed as a gift *(zakat)* to a charitable organisation. *Zakat* is one of the five pillars of Islam—obligation of the faithful.

Clearly a Takaful could be managed following the MSI model but most Takafuls are managed by commercial entities that seek profits. The manager of the funds is also responsible for raising the necessary capital to ensure the solvency of the operations. If the fund is in deficit, the manager must find the cash needed loaned without interest *(qard hassan)*, the manager is usually himself the lender. The loan is paid back by surpluses, but if they prove insufficient the manager ears the burden of the loss.

Clearly, the MSI could easily function as a Takaful as their liability side is managed in compliance with Shariah rules, however they should be careful on the asset side to invest in Shariah-compliant assets according to Islamic finance, i.e. physical assets that produce legitimate income. That may prove a challenge within the solvency rules and the need to remain liquid to some extent, but less so in a period where interest rate are so low.

However, the final point is to appoint a supervisory Shariah board filled with independent members fully versed in the Shariah rules and that can provide the seal of approval that all operations within the Takaful are "Hallal"!

Thus, it seems that the MSI have already in their midst the main talents and competencies, including reaching out to prospects through social media, to develop a new niche, but a niche that encompasses several million people. It is true that they are also not always in the highest income range and might be candidates for micro-insurance, or in this instance micro-takafuls.

Ⅴ. Mutual organisations in the Liberal Economics & Legal Environment of the EU

As far as French Mutuals are concerned looking at the French legal environment and the mutuality code is not enough as the French authorities have to transpose into French legislation the directives published by the instances of the European Union.

As is the case for the life assurance sector, the goal of EU directives on non-life insurance is to introduce a single authorisation system; this is the founding principle that allows a company headquartered in one Member State and authorised to provide non-life insurance covers under national law, to, at the same time, open branches or carry out business activities in any of the 26 other EU member country.

The first and second generation of insurance directives only opened the European market for insurance programmes concerning "large risks", such as those associated with insurance in the field of aviation and marine insurance or very large industrial companies, the third generation established a single market for insuring all types of risks falling within the scope of direct insurance, other than life assurance, including health-related risks thus directly touching one of the main areas covered by Mutual Companies.

The legal formalities that insurance actors must conform to in order to be authorised to offer non-life insurance coverage in most EU Member States are similar to those set by life assurance directives. In general, very small companies operating in niche-markets are not covered by the non-life directives. As far as mutual associations are concerned, they may also be excluded from the scope of application of the directives if they fill some conditions that are related to the way additional contributions are collected, the size of the mutuals, types of activities and their reinsurance programmes.

As is the case for life assurance, operations of provident and mutual benefit institutions whose benefits vary according available resources and in which the contributions of the members are determined on a flat-rate basis are excluded from the scope of the non-life insurance directives. Also, provisions concerning the minimum fund and the related special treatment allowed for mutuals are similar to those in Directive 2008/83/EC.

As for all other forms of insurance companies, mutual institutions cannot offer life and non-life covers within the same organisational structure. In member states where it was allowed prior to the enforcing of those provisions, local government may allow this to continue provided that separate management was adopted by the providers concerned. It is to be noted that in France mutuals were already required to set-up separate entities for life and non-life activities, therefore these dispositions do not change their status.

A. Preferential tax treatment for Mutual Insurers – Health Additional Insurance market

However, one French specificity was in the European authorities' radar. Since 1945, preferential tax treatment was granted to mutual health insurers in France, their contracts were exempts from the tax on insurance contacts. As both organisations covered by the Insurance Code and those regulated by the "Code de la Mutualité" operate on the same markets, issues arose on the matter of compliance of such preferential treatment with EU rules on State aid.

Based on this principle, the French Federation of Insurance Companies[20] lodged two complaints against the French government in 1992 for this allegedly discriminatory tax policy, arguing that it contravened EU rules on state aid and provided the European Commission with an excuse to rule on the issue. In 2001, the Commission asked the French government to either abolish the tax exemption, or to ensure that the benefit would not exceed the costs for "the constraint of providing services of general economic interest". The Commission further noted that the provision of insurance to individuals by mutual societies could not be regarded as a service of general economic interest explicitly provided for in their articles.

In order to comply with the European Commission' requests, the French government removed the tax benefit and in 2004 introduced a new type of private health insurance contract, named "contrats solidaires" and

[20] Fédération Française des Sociétés d'Assurances (FFSA)

"contrats responsables", which are provided without a prior medical examination or other reference to an individual's risk of health issues; furthermore, private health insurers had to agree not to cover new co-payments intended to encourage patients to obtain a referral for specialist care and to adhere to protocols for the treatment of chronic illnesses.

Health insurance providers – whether they are mutuals or private insurers – would consequently receive tax benefits related to the number and proportion of "contrats solidaires" and "contrats responsables" provided. Initially it appeared that the introduction of this type of contract satisfied the European Commission. In 2007 however, it started formal investigations into the question of whether this practice could be indeed regarded as non-discriminatory and how much consumers would really benefit from the advantages granted to insurers.

On 26 January 2011, the Commission ruled that the proposed measures constituted State aid incompatible with EU rules. The Commission held that it was not possible to demonstrate that the benefits of the tax reduction would be transferred to consumers. In addition, it considered the scheme as discriminatory, as it favours certain operators, such as mutual institutions, which have an obligation to conclude this type of contracts.

This ruling by the European Commission on the contrats solidaires and contracts responsables in relation to EU law on state aid prompted the French government to reform these contracts. The reform decree was published on April 1, 2016 and took effect on January 1, 2016: the contracts have to comply with the new rules, and clauses to this effect were inserted into additional health insurance contracts.

Within the scope of these new contracts "responsables et solidaires" the health-related cost refunds granted to the insured are to remain within limits with minimums and ceilings. The same rules apply to all additional health covers whether the contact is individual or collective (via an employer) and whether contacted with a mutual or a traditional for-profit insurer.

In the case of non-compliance with these rules, there is a tax penalty as the tax rate jumps to 20.27%, against 13.27% in the case of compliance; hence the additional tax burden increases the contract cost. It is too early to assess the impact of the new limitations on the costs and price of these contracts, and whether the EU authorities might rule again.

B. The mutuals & Solvency II

The basic principles behind the directive, which was adopted in 2009 and finally entered into force on 1st January 2016, three years later than initially planned, is that insurance institutions in Europe should rest on better risk assessment, better spreading of risks and better financial foundations, so as to improve the stability of the market and reinforce consumer protection.

The main innovation introduced by this directive is that, in establishing an improved foundation for the insurance sector, the directive concerns more than only capital solvency requirements as they currently exist. It also lays down rules concerning the whole organisation of insurance undertakings in Europe. It concerns:

- the taking-up and pursuit, within the European Union, of the self-employed activities of direct insurance and reinsurance;
- the supervision of insurance and reinsurance groups;
- the reorganisation and winding-up of direct insurance undertakings.

The system set up by 'Solvency II' is based on three pillars:

- **The first pillar** contains two capital requirements, the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR), which represent different levels of supervisory intervention.
- **The second and third pillars** provide for qualitative requirements (such as risk management and supervisory activities) and supervisory reporting and disclosure respectively.

Therefore, the Directive has a direct impact on the way insurance businesses are organised, what kind of internal control mechanisms they have, how supervisors work, the way insurers report on solvency and financial conditions, how they can acquire other financial undertakings, etc. The aspect excluded from the scope of this directive is the insurance as part of a statutory system of social security.

Also for small undertakings with an annual gross written premium income not exceeding 5 million euros, the Solvency II Directive does not apply. The national supervisory authorities check whether undertakings are excluded from the directive.

For mutuals the new solvency regime can have severe effects. The increasing need for one's own funds, risk differentiation and solvency requirements could prove to be difficult for small and medium-sized insurance companies, and for mutuals in particular to comply with, since they are often focussed on niche markets and specialised in very select types of risks.

Coping with the new solvency regime has forced smaller mutuals to raise contributions from members, or to partially reject their mutualistic values by becoming a stock holding company in order to obtain additional funds or to merge with other companies. The fear of a de-mutualisation, i.e. the process of a mutual transforming into a different legal form has not really materialised so far.

Specifically, for mutual insurers and the way they acquire additional funds, it is mentioned in the directive that for mutual-type associations with variable contributions, ancillary own funds may comprise any future claims on their members by means of a call for supplementary contributions.

To facilitate the implementation of Solvency II, a five-year transition period has been negotiated to comply with the regulatory demands. If, after five years, i.e. in 2021, insurance undertakings do not comply with the Solvency II rules, they will no longer be entitled to benefit from the so-called 'single passport' authorising the insurer to sell insurance throughout the EU and EEA on the basis of authorisation in its home Member State. Let us point out here that this one of the issues raised by the Brexit for UK-based insurance companies.

C. Solvency II & a New Mutual Governance

Cooperatives and mutuals are before anything else partnership and differ from other forms of companies by their governance rooted in the democratic principle "one person, one vote" and the dual status of their members who are also customers, or associates and producers, and/or clients or employees. However, since January 1, 2016, organisations in the mutual and parity sector must demonstrate that their new directors are, according to EU requirements, *"fit and proper"*.

As evidenced by the preceding presentation, Solvency II has introduced a number of new concepts that disrupt the traditional way to conduct business, hold power and responsibilities in that mutual organisations that have to comply. Traditionally, the annual general meeting of all physical persons (participating members and honorary members) elect the directors following a basic democratic principle: one person-one vote at the general meeting.

Depending on the bylaws, the general meeting may also elect the chair person. The chair may also be elected by the board. The chairperson of the board enjoys all the powers stipulated in the code of mutuality: he/she organises and runs the board meetings, and is responsible for the overview of all the mutual bodies. When it comes to third parties, the mutual is liable for the consequences of the acts of the chairperson.

With Solvency II the conditions of mutuals' management change and the function of the administration bodies must evolve to take into account the requirement to appoint an operational leader. This person is appointed by the board on a proposal by the chairperson. This person cannot be a director and must be under a work contract with the Mutual the elements of which are approved by the board.

The operational leader ***(president or CEO?)*** operates under the control of the board and within the framework of the orientations decided by the board. He/she attends the board meetings during which the conditions of delegation of powers needed for an effective management of the mutual are discussed and approved. The Chairperson and the operational leader are *ipso jure* the effective officers of the mutual.

Other persons may be nominated "effective officers" at the initiative of the Chairperson if they enjoy sufficiently wide competencies, powers, and responsibilities over the activities of the mutual, and provided their readiness to operate for the mutual justifies the move, and that they are involved in decisions that have an important impact on the mutual, like strategy, budget and financial issues.

A new governance system must be developed to clearly delineate the responsibilities of all actors and must include the following functions: risk-management, compliance, internal audit, and actuaries. Each of the persons in charge of any of these four key functions report to the operational leader (president?) but the board can at will decide to set up specific hearings for the persons in charge of these key functions, and at least once a year for each of them.

Solvency II has introduced the concepts of "fit and proper" concerning all directors, as a whole and individually, as well as all operational persons in key functions. Their appointments and terminations must be notified to the control authority[21]. The ACPR can oppose a nomination if it deems the persons involved unfit to serve as proposed in terms of honourability, competencies, or experience.

With the requirement that next to the Chairperson who holds his/her legitimacy from a democratic election, be appointed an operational leader to share the effective management of the mutual, Solvency II has modified the balance of powers and is causing a reconfiguration of the mutualistic world.

Ⅵ. New opportunities and new territories for the mutual idea

Whereas mutuals play an important role in the insurance and welfare markets in the European Union although not always with the market shares they enjoy in France, they are welcome for their impact on individuals' and families' protection thus contributing to societal resilience, and a sustainable future through their involvements in CSR activities.

Some mutuals have spread in Africa, especially for the development of farmers' cover still at very low penetration level, in spite of the existence of informal support group including burial costs and tontine[22] for micro-investments. However, countries outside Europe could benefit from adapting the models to their specific legal, societal, and cultural environment.

The rapid development of Takafuls in countries with overwhelming Muslim majority like Indonesia, Malaysia and to a lesser degree, the Middle East and the Maghreb, has proven the need for protection among these populations. In other countries with sizeable Muslim minority and whose government do not feel the need to enact specific Takaful legislations, the mutual model adapted to micro-insurance would offer a solution within the existing regulatory framework, like the CIMA code in French speaking Africa, provided their leaders are aware of the need to invest in Shariah acceptable assets and to add an Islamic advisory board to allow practicing Muslims to gain access to insurance protections.

Furthermore, a number of traditional religions and beliefs place the values held by the mutual movement at the heart of their value system. Long held traditions in Asia like Buddhism, Zen, Confucianism, Hinduism and others have compassion consideration that are aligned with the Mutual System. Whereas the penetration of insurance remains somewhat low, mutual companies created with the mutual governance as their guide might help offer answers to the need of protection, while, at the same time, collecting long-term funds to invest in the necessary infrastructures to enhance the economic and social development in the region.

There are clear opportunities for the Mutual Movement in developing micro-finance and micro-insurance in the developing countries with the additional bonus that reserves could be invested in local economies by helping small and medium size initiatives, agricultural, industrial, as well as commercial. As can be seen in Senegal for example, the mutual model is the way to go in Rural areas where traditional insurers do not want to do business or have no personnel. They are a good place to establish mutual insurers with the assistance of local traditional chieftainships that retain a strong influence and following among local farmers.

Young Insurance professionals in all these countries that are motivated by the values shared by millennials the world around, are all too aware of their common future; they could be leaders to start and/or grow a sustainable mutual system in their countries. If an important need for mutuals can be demonstrated through robust research studies, then they will be in a position to assist regulators and authorities in developing model laws, governance, and financial solvency rules that can assure viability for mutuals by gaining experience through the European mutuals, and especially the French mutual companies, which could offer technical assistance through internships for national professionals and expatriates to assist local initiatives. It might even make sense for them to invest financial resources to help the start-ups in developing countries.

[21] Autorité de contrôle prudentiel et de résolution (ACPR)

[22] In the insurance industry, a scheme for life insurance in which the beneficiaries are those who survive and maintain a policy to the end of a given period. In Africa, a group of private persons put in common a sum of money that is loaned to one of them and then when reimbursements come in, another member may be the beneficiaries depending on priority rules defined between the members (a traditional approach to micro-loans)

Ⅶ. CONCLUSION - Future prospects for Mutual Organisations in France, and beyond

All through its history, the French Mutual movement had to adapt and change to meet the challenges of evolving environment conditions, social, economic, political, cultural. Had it not been the case, it would have probably disappeared as was the case in several European countries, and more specifically the United Kingdom where it was really powerful until the eve of World War I.

The deep divide between the managers of welfare programmes and those who lead the demands of the working-class has been a constant aspect of the French situation since the second half of the 19th Century, and it has no equivalent in Europe. The consequences are still visible today and it has endowed the leaders of the mutual movement with exceptional international responsibilities at a time when the fight for a European Mutualist Status is far from over and demands vigilance as both Insurance Mutuals Federation are all too aware.

Implementing democratic decision-making processes has remained a key mission that French mutual leadership has cherished. And they learned to use the media to interact with the general public rather than with paid advertisements, which they did not shy away from however. But, beyond price, innovation, quality service, etc. their reputation relies on the democratic process that must be preserved even through complying with Solvency II. Their share of the personal lines of the insurance markets, especially automobile and household, is a testimony to the enduring public support.

However, the new challenges with the digital revolution, and very low interest rates pose new challenges that the leadership will have to face to reinforce its relevance and sustainability in the 21st century, and that includes on-line administration and participating actively in social media to attract millennials both as staff and customers.

We could borrow a conclusion from the French philosopher and sociologist, Edgar Morin with an excerpt of his article "What remains of the European universal" published in the daily Libération on November 22, 2009 as it seems to open a wide range of new possibilities for mutuals in the second decade of the 21st century, as follows:

> "Individualism had always two faces. One face of autonomy and one egocentric and egoistic that our civilization has over-developed. All the old solidarities are disintegrating: family, couple, village solidarities, work solidarities. How could solidarity be regenerated in our society? Political thinking should deal with this crucial issue. The fundamental shortcoming of Economy is that it is a closed science that does not take into account human factors and realities, and only rests on computations.
> The road will call for a pluralistic Economy, one that is social and values solidarity, developing cooperatives, mutuals, and associations. A new culture is called for, one that will combine the idea of multiple reforms and a deep transformation, which I call the metamorphosis."

It is all too clear that the current societies are very different from the past, even the recent past. It would be all too easy to illustrate these changes, as the preceding development of the recent mutations linked to the digital economy are making the world ever more complex and volatile. However, the four pillars of the mutual movement, liberty, democracy, solidarity and independence are always valid, and validated by a thinker of Edgar Morin's calibre. All through its existence, now over two centuries long, mutuality has always found a way to adapt to changing environments, to different territories, times, and cultures.

There is no way the mutual movement could compromise on its fundamental principles, but the challenge that leaders have to face is to find new ways to implement them, as is the case in the EU with the implementation of Solvency II to all insurance organisations, including mutual institutions. What their predecessors have accomplished during the 19th and the 20th centuries, 21st century mutual leaders will no doubt find ways to continue, even if at a pace and a depth as yet unknown and will be agents of the metamorphosis that the current context requires. After all, its past is probably the strongest bond for the future in the insurance industry of the mutual model in France, and worldwide; the French mutuals might be wise to seize the opportunities offered by the developing world and its need both for protection and structural investments!

Ⅷ. Bibliography – General

- **The role of mutual societies in the 21st century** www.europarl.europa.eu/document/activities/cont/201108/...
- **Rapport Annuel 2016** – Association des Assureurs Mutualistes - www.aam-asso.fr
- **Le mutualisme : répondre aux défis assurantiels** – Arnaud Chneiweiss & Stéphane Tisserand – Fondation de l'Innovation Politique (Novembre 2015) – www.fondapol.org
- **L'histoire de la Mutualité : quatre grands défis** – Michel Dreyfus - https://www.cairn.info/revue-les-tribunes-de-la-sante-2011-2-page-49.htm
- **Comment Solvabilité II transforme la gouvernance mutualiste** – Jérôme Herbet / Avocat Associé, Winston & Strawn LLP, Les Echos January 7, 2016 – https://www.lesechos.fr/idees-debats/cercle/cercle-146473-solvabilite-ii-les-consequences-pour-les-mutuelles-ne-sont-pas-simplement-financieres-1190338.php
- **Gouvernance et légitimité : le modèle mutualiste** - Alexandrine Lapoutte – Dissertation to obtain the degree of Doctor of the University of Occidental Brittany – December 9, 2013 - https://tel.archives-ouvertes.fr/tel-01124158/document

Ⅸ. Bibliography – The history of Mutuality in France (health)

- DESGRE Stève et SOUCHET Jean-Luc, La force des solidarités vendéennes, Mutualité de Vendée, 2007.
- DESSERTINE Dominique, FAURE Olivier, NOURRISSON Didier, La Mutualité de la Loire face aux défis : enracinement local et enjeux nationaux (1850-1980), Publications de l'Université de Saint-Etienne, 2005.
- DREYFUS Michel, Liberté, Égalité, Mutualité, Éditions de l'Atelier, 2001.
- DREYFUS Michel, Traité de Sécurité sociale, tome V La Mutualité, Yves Saint-Jours (dir.), L.G.D.J., 1990.
- DREYFUS Michel, GIBAUD Bernard, GUESLIN André (dir.), Démocratie, solidarité et mutualité, autour de la loi de 1898, Economica, 1999.
- DREYFUS Michel, GIBAUD Bernard, La mutualité dans le siècle (1900-2000), Mutualité Française, 2000.
- GIBAUD Bernard, De la Mutualité à la Sécurité sociale. Conflits et convergences, Éditions ouvrières, 1986.
- GIBAUD Bernard, Mutualité-Assurances (1850-1914), les enjeux, Economica, 1998.
- GIBAUD Bernard, Fédérer autrement. Histoire de la Fédération nationale de la Mutualité française 1902-2002, Racines mutualistes, Mutualité française, 2002.
- GUESLIN André, L'invention de l'économie sociale : idées, pratiques et imaginaires coopératifs et mutualistes dans la France du XIX^{e} siècle, Economica, 1997 (reed.).
- SOUCHET Jean-Luc, La mutualité en Loire-Atlantique, dix générations de traditions et d'innovations solidaires, Les Mutuelles de Loire-Atlantique, 1996.
- TOUCAS-TRUYEN Patricia, Histoire de la Mutualité et des Assurances, Syros, 1998.
- TOUCAS-TRUYEN Patricia, La Mutualité au sein des populations littorales (1850-1946), Librairie de l'Inde, 1998.
- TOUCAS-TRUYEN Patricia, L'identité mutualiste, ENSP, 2001.
- TOUCAS-TRUYEN Patricia, Le fraternel rapprochement, Éditions Le Tiers-Livre, 2007.

Received/ 2017. 08. 14
Revised/ 2017. 09. 16
Accepted/ 2017. 09. 25

The International Review of Financial Consumers, Volume.2 Issue.2(Oct., 2017), 15-33 pISSN 2508-3155 eISSN 2508-464X
https://doi.org/10.36544/irfc.2017.1-2.2

The International Review of Financial Consumers

www.eirfc.com

Financial Consumer Protection in the Household Lending Sector: An Assessment of the Korean Experience

Cho, Man[1†], Seung Dong You[2], and Young Man Lee[3]

A B S T R A C T

The objective of this paper is to offer a systematic review and assessment of the policy measures adopted to date for financial consumer protection (FCP) in the household lending sector in Korea. In so doing, we focus on the "software" aspects of the policies adopted so far in terms of four particular groups of consumer issues: (1) information provision (by service providers), (2) financial literacy programs, (3) sales practices, and (4) dispute resolution (rules and processes). We also attempt to relate the FCP policies to two broader goals of financial market regulations - financial stability and financial inclusion. Our analyses indicate that; the regulatory authorities in Korea initiated the FCP policies early on, which cover a fairly comprehensive set of policy measures with almost all sub-items of the aforementioned four dimensions being included; some of the FCP policies are driven in large part by the intent of stabilizing the housing and mortgage market rather than protecting financial consumers per se, for which the regulatory authorities should weigh the anticipated benefit in terms of financial stability against the unintended cost in financial inclusion; and the Korean FCP policies tend to focus on the residential mortgage lending sector, which should be extended to other consumer lending products (e.g., credit – or non-collateralized – lending, credit card receivables, and car loans). Though seemingly comprehensive, the FCP policies in Korea should be further refined and enhanced with respect to their effectiveness, for which we discuss a series of future research topics.

Keywords: Financial consumer protection, consumer•mortgage lending, financial inclusion, financial market stability

Ⅰ. Introduction

The reasons for government intervention to protect financial consumers are well-established. On the efficiency ground, information asymmetry between service providers (financial institutions (FIs) in particular) and financial consumers represents a classic case of market failure, implicating an under-provision of consumer credit due to moral hazard and adverse selection. (Campbell et al. (2011)) Search costs for, and infrequent transactions of, certain consumer financial products, e.g. mortgage loans for home acquisition, constitute additional sources of inefficiency in the markets for consumer financing. On the distributional ground, it is demonstrated that financial knowledge and household income tend to be positively correlated such that consumers with lower income are systematically ended up in the segments of financial markets where financial charges are higher. (Campbell (2006)) The recent literature also documents a pervasive lack of basic financial literacy among consumers in general (Lusardi and Mitchell (2007), Lusardi and Tufano (2009), Lusardi, Mitchell, and Curto (2010), and Tennyson (2016)), in response to which a rationale for govern-

1† KDI School of Public Policy & Management
mancho@kdischool.ac.kr
2 Sangmyung University
3 Hansung University

ment-driven paternalism (or a "nudge") through various forms of financial consumer protection (FCP) regulation is well-founded. (Thaler and Sunstein (2009))

The objective of this paper is to offer a systematic review and assessment of the policy measures adopted to date for FCP in the household lending sector in Korea. The country represents an interesting emerging-market case in that its consumer lending sector in general, and the residential mortgage credit in particular, has been rapidly evolving and expanding since the Asian Financial Crisis (AFC) in the late 1990s, and that the regulatory authorities have been actively instituting various FCP policy measures during the last decade.

In assessing FCP policies, one has to deal with the challenging issue of multi-dimensionality. The FCP policies should cover multiple consumer finance sectors (e.g. lending, insurance, investment, and so on) and each sector tends to have a unique set of FCP policy issues. In this study, we focus on the "software" aspects[1] of the household lending sector in Korea by examining the rules, directives, and regulations governing four particular dimensions of FCP policy: (1) information provision (by service providers), (2) financial literacy programs, (3) sales practices, and (4) dispute resolution. Using the World Bank (2012) as a reference, which suggests 39 common good FCP practices, we first select those sub-items under each of four categories that are relevant to the household lending sector, and then survey and assess the Korean FCP policies by each selected sub-item. In the assessment, we also take a stance that FCP policy is a mean to an end and, as such, should contribute to such broader policy objectives as: preventing abusive or fraudulent lending-collection practices (by FIs, or their agents); inducing behavioral changes in demand-side or supply-side (or both) of the financial market in question such that the volatility of the lending sector is reduced; and enhancing financial inclusion of vulnerable consumer cohorts to the lending services.

Our analyses indicate that the regulatory authorities in Korea initiated the FCP policies early on, even before the Global Financial Crisis (GFC), and are covering a fairly comprehensive set of policy measures with almost all FCP items suggested by the World Bank (2012). To illustrate, the two main regulatory authorities - the Financial Services Commission (FSC) and the Financial Supervisory Service (FSS) – have instituted various FCP measures since 2007, including the summary statement (of the product chosen), the consumer handbook and checklist, the web-based "Mortgage Calculators," e-mail and text notifications (whenever the lending rates and other loan terms change), the 14-day cooling-off period after signing contract (during which consumers can cancel the contract), and so on. In addition, the multi-layered consumer complaint mechanisms are in place (those run by FIs, by their professional associations, and by the regulators), and the abusive (or violent) debt collection practices have largely disappeared thanks to the special law enacted in 2009. Yet, some FCP measures are in a fairly early stage in terms of implementation (e.g. the financial literacy programs, and consumer access to the credit data and credit scores), for which a more elaborate and systematic policy design appears to be warranted. The next milestone expected in the Korean lending sector will be the passage of the special FCP law that was submitted to the Congress in 2017 by the two regulatory bodies, which is currently under deliberation for enactment.

As another overall assessment, it is fair to say that the rules and regulations in the consumer lending sector is tilted toward financial stability, more so than FCP per se or financial inclusion of marginal consumer cohorts. Although that is understandable given the large and rapidly-growing household debt of the country in the recent years, one should weigh the anticipated benefit in terms of financial stability against the unintended cost in financial inclusion in designing the policy scheme in the lending sector. As a case in point, the macro-prudential regulations employed - the maximum allowable loan-to-value (LTV) and debt-to-income (DTI) ratios – work as constraints for FIs in underwriting loan applicants and, as such, inevitably steer low-income, low-wealth, and credit-impaired borrowers to a high-cost lending sector (e.g. about 5 percent lending rates by first-tier FIs such as the commercial banks vs. 24 percent interest rates by some of the tertiary FIs) or even exclude them from the financial service all together. As a related point, some FCP policy measures take a form of restriction in product offering (e.g., the quota in lending volumes of certain products such as fixed-rate or principal-amortizing mortgage loans)

[1] Chen (2018) categorizes the FCP issues into two groups - those related to "software" (relevant laws and rules, rationale and direction of FCP, and ex-ante and ex-post protection mechanisms) and others related to "hardware" (financial supervision organizations, deposit insurance corporations, and dispute settlement organizations).

or in underwriting conditions (e.g. the LTV • DTI caps). In instituting such policy measures, one should strike a balance between intended benefit in terms of FCP (or stabilizing financial market) and unintended cost in product affordability.

Up to now, the FCP policies in the consumer lending sector of Korea tend to focus on the residential mortgage lending sector, which should be extended to other consumer lending products (e.g. credit – or non-collateralized – lending, credit card receivables, and car loans). The sector takes roughly a half of the total consumer lending volume, yet receives a relatively high attention from the policy making circle as well as from general public due in large part to the importance of housing both as space consumption and as investment opportunity. But, both in terms the stability and in terms of the inclusion, the other half should receive an equal (at least) level of policy attention, as we believe that more resource-constrained borrowers and, hence, more vulnerable consumer cohorts at the time of economic shock would be concentrated in the non-mortgage sector. Finally, there is a host of future research issues for careful conceptual and empirical investigation going forward, as we discuss in Section V.

The rest of the paper consists of the following four sections: the current state and evolution of the Korean consumer lending sector along with the relevant FCP measures employed (Section 2); the international benchmarks and a survey of literature as a guidance for subsequent analyses (Section 3); the assessment of the FCP measures employed in Korea (Section 4); summary and concluding remarks (Section 5).

Ⅱ. The Consumer Lending Sector in Korea

A. brief history and current state

Before the AFC in the late 1990s, the consumer lending sector was small and under-developed, and was not a high-priority segment in the public policy point of view: that is, the scarce financial resource was away from the sector but was directed toward the trading or export-generating industries. However, as a part of the post-AFC re-structuring, the consumer lending was liberalized to the commercial banks, the dominant players in the financial markets, and the lending volume has been steadily and fairly-strongly grown since the early 2000s.[2] As shown in Figure 1, the total consumer credit rose by 7.2 percent per annum (based on a compounded annual growth rate, CAGR) between 2002 and 2017, which has accelerated in the recent years to 10.3 percent CAGR in 2014-2017. As of the 2nd quarter 2017, the total household debt takes about 85 percent of GDP, and about a half of that is the residential mortgage debt outstanding, MDO (hence, about 42 percent MDO-to-GDP ratio). The latter is relatively better documented and more closely monitored and has also been subjected to various regulations for the purpose of financial (and real estate) market stability.

In the early phase of the mortgage market development, the pre-dominant loan products were short-term (e.g. 3-year maturity) bullet-paying (with no amortization of principal) adjustable-rate mortgage (ARM) contracts, due in large part to the deposit-based (rather than whole-sale) funding by the mortgage lenders. Concerned with a potential systemic risk posed by the predominant ARM contracts, the government promulgated the yearly quota in 2014 as to the shares of two particular loan types in MDO (of each commercial bank) - the fixed-rate mortgage (FRM) contracts and the principal-amortizing loans (see Table 1 for the plan). Thanks to this fairly-strong government push and to the securitizer of FRM - the Korea Housing Finance Corporation (KHFC) created in 2004, the share of FRM and that of the amortizing loans have been steeply rising in the recent years, and the 2016 goals for both loan types are also expected to be met.

Another feature of the sector to note is the macro-prudential regulations implemented since the early 2000s, LTV and DTI ratios. That is, the overall caps for these

Table 1. Regulatory targets for FRM and amortizing mortgage contracts (%, EOY)

Loan type	2013 (observed)	Yearly target			
		2014	2015	2016	2017
FRM	15.9	20	25	30	40
Amortizing	18.7	20	25	30	40

Source: FSC (2014)

[2] There were two specific de-regulation measures that helped the rapid influx of liquidity to the consumer lending markets – liberalizing the interest rates (both deposit and lending rates) and lifting the restrictions (for the commercial banks) to real estate backed loans. See Cho and Kim (2011) for more details on these regulatory changes.

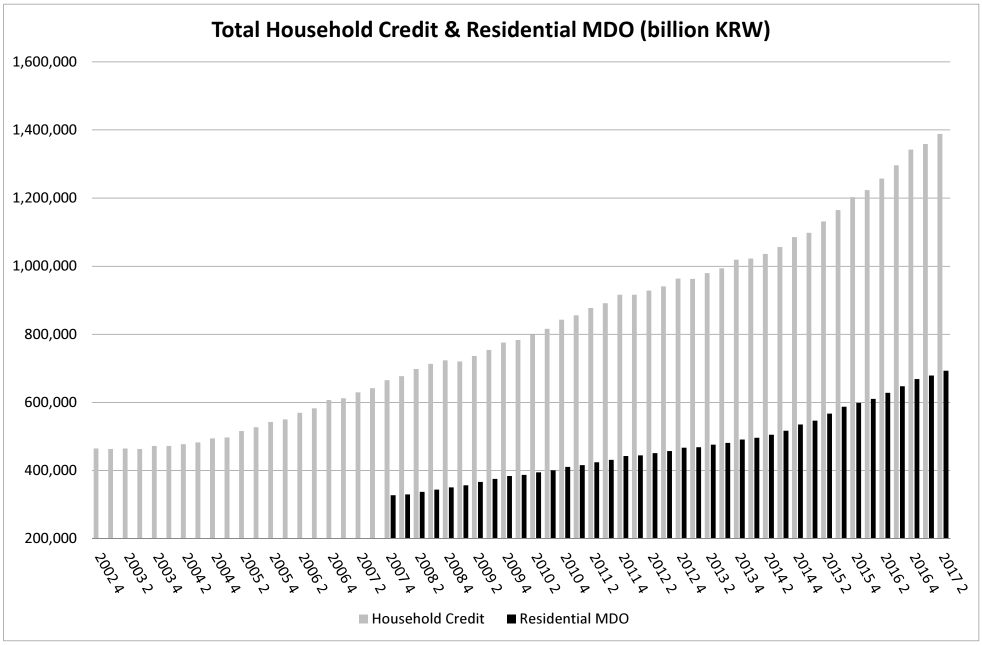


Figure 1.

Source: Bank of Korea

lending ratios are set in a conservative level (70 percent for LTV and 40~60 percent for DTI), which are also location-varying, in that they get much lower in the spatially-designated speculative zones (e.g., the 30~40 percent LTV cap in some of the seemingly over-heated housing markets within Seoul and other primate cities).[3] Relevant to the regulations, there are two additional measures that are being discussed in the context of a more prudent management of potentially vulnerable groups: that is, the planned implementation of the debt-service-ratio (DSR) - the back-end income ratio that includes all, not just one, debt obligations in computing DTI – and the definition of “marginal borrowers” - those whose DTIs exceed 40 percent AND whose financial liabilities exceed financial assets – defined for the purpose of a more close monitoring. At the same time, how to ensure proper level of financial service to the “real” mortgage demanders (e.g. first-time home buyers) given all these stability-driven regulations is the topic that is often being discussed in media as well as in academia.[4]

1. The current state of the FCP policies

It was 2007 when the two main regulatory authorities - FSC and FSS – initiated the FCP policies in the form of the regulatory directives on the several measures related to information provision on the residential mortgage products. Since then, there have been the additional policy guides, and a special law was submitted to the Congress in May 2017 that is currently under a legislative deliberation. The proposed law encompasses a fairly comprehensive set of FCP measures in all dimensions of our analysis – (1) information provision, (2) consumer education, (3) sales practices, and (4) dispute resolution. As other notable features, the proposed law categorizes consumer products into four classes - depository, investment, insurance, and lending (or loan) products, and also identifies three types of service providers - direct sellers, delegated or intermediating sellers, and advisors. As other FCP measures to note, the authorities have implemented a product comparison system for typical contracts in each

[3] See Han, Hwang, and Cho (2016) for an empirical study on the effects of LTV regulations in Korea.

[4] About 480tr KRW (about 35% of the total consumer credit) lent to self-employed borrowers and, among them, 42.8tr(696k households) being for “safety-net” loans. The cohort represents another important target for the consumer lending service in Korea.

Table 2. Product Comparison and Public Announcement

Channel	Product		Segment	Key information to provide
FSS-consolidated comparison & public announcement (CPA)	Deposit		(1)Banks, (2) Savings Banks	Interest rates (IR) by maturity, conditions
	Installment saving			Allotment conditions, IR by maturity
	Loan	Housing	(1), (2), (3) Insurance C., & (4) Capitals	IR band, prepay penalty, loan limit
		Chonsei		Above & repayment method
		Credit		IR by credit rating, average IR
	Saving, pension		(1), (3), & (5) Investment C.	Minimum freq., yield, expected payment
	Retirement pension			Minimum freq., yield
Association-driven CPA	Fund		(5)	Yield, risk grade, minimum investment
	Insurance, indemnity		(3)	Eligible age, premium by subscription condition, collateral
	Insurance, automobile			

Source: FSC & FSS (2015)

product class, as depicted in Table 2, since January 2016. And, a tailor-made consumer education plan for different socio-economic groups (e.g. retirees, college students, credit-impaired, and so on) has been announced recently (on January 23, 2017). Other details of those proposed or implemented provisions will be discussed and assessed in the subsequent sections.

Ⅲ. Analytical Issues

A. Dimensions of the FCP policy in the lending sector

The subprime mortgage debacle, followed by the severe contractions in economic activities in various countries (e.g. the "Great Recession" in the U.S.), sparked a world-wide debate on FCP. The main lesson from the recent financial crisis, in particular from the residential mortgage lending sector, is that the policy effort should be geared toward both demand-side and supply-side, given that the anomalies are in fact observed from both sides − the excessive risk-taking and improper, even predatory, lending practices by the mortgage lenders combined with the speculation-driven mortgage demand propelled by a "permanent" housing price boom assumed. In response, there have been a number of FCP-related legislations, with the Dodd-Frank Act in the U.S. being a notable example. The multilateral international agencies also suggest a series of the good FCP practices, e.g. the OECD (2011), the World Bank (2012), and CFPB (2016). In particular, the World Bank (2012) put forth the 39 common good practices (or "principles") around three themes: (1) providing appropriate information for financial consumers to make informed decisions, (2) protecting financial consumers from unfair or deceptive (lending) practices, and (3) ensuring them access to recourse mechanisms to resolve disputes.

In our survey, a template of a desirable FCP policy measures in the case of consumer lending products is developed by selecting those good practices suggested in the World Bank (2012) that we believe as directly relevant to the sector. The selected measures are listed in the table below (see Appendix 1 for a more detailed description of each item). Using this template, we first collect the data to compile the current FCP policies adopted in Korea in all 13 dimensions - (a) through (m) in Table 3 - under the four categories.

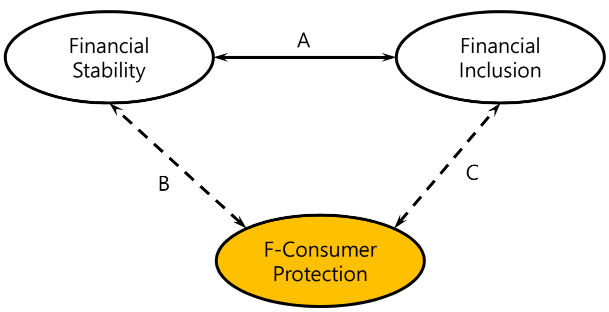
B. FCP vs. financial stability vs. financial inclusion

In this study, we take a stance that a good FCP policy should contribute to achieving two conventional policy objectives in financial markets - financial stability and financial inclusion. As a case in point, an enhanced consumer capability for product selection via an effective education program along with an appropriate (i.e. risk-based and non-predatory) sales practice by the lenders can lead to a counter-cyclical lending pattern, which in turn will reduce a chance of a systemic risk driven by

Table 3. Relevant FCP Measures Suggested (for the Consumer Lending Sector)

	FCP measure suggested	Description
A. Information provision	Summary statement	A short one or two page summary statement on the product (Principle 8)
	Qualification of FI staff	Adequate training for FI staff on products & services (Principle 14)
	Change in lending terms	Individual & immediate notification in writing of changes in products (Principle 16)
	Consumer credit data	Ready and free access to their credit reports from credit registers, and provides procedures for correcting mistakes in credit reports (Principle 20)
B. Financial literacy	Programs for financial literacy	Developing and implementing the financial literacy programs by a wide range of organizations (Principle 33)
	Monitoring financial literacy	Measurement of financial literacy of consumers through broad-based household surveys (Principle 36)
	Financial advisor	On forward and reverse mortgage contracts; For low-income, low-wealth, and less creditworthy borrowers
C. Sales practices	Cooling-off period	A period during which the consumer may cancel the contract without penalty (Principle 11)
	Code of Conduct	A principles-based code of conduct that is devised by (by all banks, by all non-bank credit institutions, or by their associations) (Sector-specific Principle)
	Affordability of product	Product recommended being in line with the need of the consumer; Consumer's credit worthiness being properly assessed (Sector-specific Principle)
D. Dispute resolution	Collection practice; & Debt Recovery	Prohibition of abusive collection or debt recovery practices (Principle 19); & as a Sector-specific Principle
	Consumer complaint; & Ombudsman and other conflict resolution mechanisms	Designated contact point with clear procedures for handling customer complaints; Up-to-date records of all complaints received (Principle 25); Access to an affordable, efficient, respected, professionally qualified and adequately resourced mechanism for dispute resolution (Principle 26)
	Foreclosure of mortgaged or charged property	Informing in writing in advance of the procedures involved, and of the legal remedies and options available (Sector-specific Principle)

Source: World Bank (2012)



A. Financial stability vs. financial inclusion: Housing boom & pro-cyclical lending → demand for leverage↑ (by consumers) → excessive risk-taking & predatory lending (by FIs) → bad news (e.g. asset price bust & NPL↑) → liquidity trap → contraction in real economy (C↓ & I↓)
B. FCP vs. financial stability: Financial literacy (of consumers)↑ → sound loan selection & leverage↑ → risk-taking & predatory lending (by FIs)↓ → (sector-driven) systemic risk↓
C. FCP vs. financial inclusion: Information provision & "sound" lending practices↑ → credit risk↓ & better loan matching → more prudent risk management → "serving more underserved" (or extending the service to more "marginal" borrowers)

Figure 2. FCP vs. Financial Stability vs. Financial Inclusion

the lending sector, the linkage B in Figure 2. Also, a prudent (or efficient) risk management by FIs backed by real data and historical evidences can lead to a better matching between lending products and borrower cohorts, which will result in an extended financial services to more marginal (or underserved) consumers in the lending system, the linkage C in Figure 2.

Since the global financial crisis, there has been a rising volume of the academic studies on various topics related to the housing-driven systemic risk, e.g. those on the pro-cyclical mortgage lending patterns (Geanakoplos (2010) and Brunnermeier and Oehmke (2014)), on the wealth effects of housing and mortgage market boom-busts (Iacoviello and Pavan (2013), Mian and Sufi (2011), Carroll, Otsuka, and Slacalek (2011), Case, Quigley, and Shiller (2011), and Mian, Rao, and Sufi (2013)), and on the micro- and macro-prudential regulations to help prevent a similar event from happening again (Crowe et al. (2011) and Wachter, Cho, and Tcha (2014)).[5] Though challenging, the effectiveness of FCP policies should be judged, as we argue, with respect to whether or not, and to what extent, they contribute to stabilizing the consumer lending sector by changing behaviors of both service providers (FIs and their agents) and consumers such that the systemic risk (or a contagious lending cycle) is better contained.

At the same time, a good FCP policy is also about an inclusive financial intermediation: that is, relating financial consumers of diverse socio-economic characteristics in terms of income, wealth, and demographics to optimal (or welfare-maximizing) financial products and services; and, in so doing, serving more underserved households (i.e. extending financial inclusion) in a prudent fashion. To this end, a series of studies has documented various policy issues in the context of making the residential mortgage lending sector more complete and inclusive (Miles (2003) and (2004), Mercer Oliver Wyman (2005), and Kim and Cho (2014)).

In this study, our effort to assess the FCP measures adopted in the lending sector in Korea will largely be conceptual, rather than empirical, given the lack of proper micro data set. As such, this study should be viewed as an initial effort to set the stage for more full-blown empirical tests of different elements of good FCP policies as to how effective they are in achieving those two policy objectives discussed in this section in the contexts of Korea and other countries.

[5] See Cho (2017) for a survey of the recent studies.

Ⅳ. Assessing the Korean System

A. Information provision

1. Current state and the FCP measures adopted

Given the fact that the ARMs were the dominant mortgage contracts and the growth of MDO was surprisingly fast in the early 2000s, the regulatory authorities formed a task force (TF) in 2004 to review and highlight potential risks associated with the mortgage lending sector.[6] Out of the TF deliberation, a series of policy measures was introduced, in a large part for stabilizing the mortgage market and the macroeconomy rather than for protecting financial consumers. The specific measures promulgated were along the same line of argument put forth by Miles (2004) in UK: that is, in their choices among competing mortgage products, consumers tended to be myopic in that they prefer variable-rate mortgages (over fixed-rate loans) and bullet mortgages (over amortizing loans) due in large part to lower payment burdens in initial years of loan lives, without much considering a potential risk of payment shock in later phases of loan terms. The phenomenon is also labeled as “the present-(time)-bias” by Campbell et al. (2011).[7]

The regulatory intent embedded in the first FCP measure was to have borrowers realize the risks associated with the certain mortgage products by issuing several guidelines for the lenders. First, upon signing a variable-rate mortgage

[6] The team was composed of bankers, policy makers, and academics and focused on a development of practical guidelines for mortgage originators.

[7] What is interesting was the fact the Korean consumers indicated their preferences that were opposite to their actual product choices. In particular, You (2006) reported that more than 70 per cent of future home buyers who planned to take out a mortgage loan in 2005 showed their preference for fixed-rate mortgages. In the same year, however, the market share of fixed-rate mortgages was less than 15 per cent. They also wanted to obtain amortizing mortgages, the market share of which was less than 30 percent, even though more than 70 percent mortgages were (short-term) bullet loans.

Figure 3. Mortgage Financial Offered by FSC and Commercial Banks

Note: the English translations were added by the authors.
Source: FSC and Woori Bank (Accessed Aug 24, 2017)

contract, lenders (or underwriters) were asked to expressly and openly state risks of rising interest rates and to have them sign on the parts of the contract to verify that the borrowers acknowledged and understood the risks. Second, borrowers should be given the information (in the so-called "passbook") based on which they could track their monthly interest rates and interest payments. Related to the second guideline, FSC released an interesting survey in 2007, showing that, while most borrowers who received an email message to alert an interest rate change did not tend to read the message (only 30 percent even checked the message), those who received a mobile text were more likely to read the alert. Based on this finding, all lenders were required to have both methods of the alert, for which borrowers could choose one or both. Third, FSS required financial institutions to provide a mortgage calculator on their website by launching a standard system of its own (Figure 3). These calculators are quite similar to those in other websites provided by the Money Advisor Service in UK and the Financial Consumer Agency of Canada.

One important policy measure introduced by the authorities in April 2007 was the requirement to provide a summary statement on the mortgage loan to be issued, whose length was limited to two pages at the maximum. Since then, its contents have been updated several times with the current version containing a fairly detailed set of basic facts and descriptions of terms on the mortgage contracts – an overview of the product, the amount of the mortgage loan, types of interest rates, other fees or costs, maturity and amortizing information, prepayment or late payment penalty, tax deduction for qualified borrowers, the lender's contact information, the borrower's income, the value of the collateral, and spreads for borrowers with low credit scores as well as effective interest rates (along with its calculation methods) and both prepayment and delinquent penalties.[8] The updates were done in response to consumers' comments and complaints. In addition, the summary statement includes examples for late penalty calculations, legal ceiling of penalty and official stamp tax, reasons for why interest rates for FRMs being generally higher than those of ARMs.

In 2015, FSC and FSS jointly proposed announced that from Apr 2016 financial institutions should not request more than eight documents at the time of mortgage origination, a fairly significant reduction from around 20 documents collected at that time as some of them were deemed to be redundant or trivial, and that some loan information

[8] According to the press release at that time, upon obtaining a mortgage loan, borrowers had to sign a loan contract that was 30 to 40 pages long with various terms and conditions that were complicated enough so that those consumers with little professional knowledge in finance or law were hard to comprehend. The summary statement should explicitly state at the outset, "this document is to protect the consumer's interests and its contents provides the consumer with key facts of the financial product. After reviewing the document and understanding the contents, the consumer should select the product."

should be included to the summary statement.

As one more policy measure adopted in the recent years, the regulatory authorities issued the standard terms and conditions of the credit business that contains a borrower's right to seek a loan modification such a reduction in interest rate when her financial conditions improve after loan origination. However, most borrowers do not know about this, and lenders are generally passive in informing them on this provision by arguing that they do not have specific guidelines for "improved financial conditions." Furthermore, the right was limited to consumer loans excluding mortgages. In Apr 2014, as a result, the FSS asked banks to provide the detailed guidelines, and to provide borrowers information on the right by sending text messages. From Jan 2017, all the lenders are required to explain a borrower's option to negotiate loan terms when her financial conditions have improved upon loan origination.

2. Assessment and Policy Implications

Although the regulatory authorities in Korea have initiated the information provision part of FCP policies early on in a fairly comprehensive fashion, there are several areas of further strengthening with this respect. First, it appears that training of the staff in financial institutions should be more systematically and specifically designed for different consumer lending products. Given that actual communication to consumers on risk-return profiles of different financial products is generally done by FI staff, we believe that capability to convey accurate, unbiased, and professional product information by them is crucial, for which a systematic training program is necessary. Currently, FI staff members have a general training on consumer lending, designed by individual institution or by their professional association. We believe that it is more desirable to have such training program to be product-specific given that the mortgage products (due to their long-term maturities and other special product attributes) tend to be different from our consumer lending products (e.g., credit card receivables and other non-collateralized lending). As a case in point, while the performance of non-collateralized credit lending is mainly influenced by future income streams (or human capital) of borrowers, that of the residential mortgage loans is closely correlated with housing price cycles, which represents an unique systematic risk factor that should be considered in the underwriting and should be explained clearly its prospective borrowers.

Second, given its importance in helping consumers understand products' risk-return profiles, the "optimal" contents of summary statement should be properly designed and should also be empirically tested as to its effectiveness. The Korean experience shows that, though it originally starts as a short synopsis (with two pages maximum), the current version contains a lot more, probably too much, data points, which are difficult to be comprehended by most households who do not have professional knowledge about mortgage terms and transactions. Hence, it appears to be necessary to conduct a further research in determining what set of loan characteristics along with how much descriptions thereof are clear and concise, yet detailed, enough to assist consumers' comprehension and their efficient loan selections.

Third, financial consumers should have an easy and efficient way to check their creditworthiness and to modify their loan terms if that is feasible. One information issue in that regard is the checking of consumer credit information: that is, there is little guidelines or laws that specify obligations that lenders need to provide their consumers with updated credit information and resulting credit score. Consumers should be able to check changes in credit information along with other loan characteristics (e.g., interest rates) easily and should have a efficient medium to reflect them in their scheduled repayments.

B. Financial literacy

1. Current state and the FCP measures adopted

After the FCP policy measures were initiated in 2007, the banking association in Korea (KFB) developed and published a consumer handbook and a check list for mortgage borrowers as a consumer education tool. The handbook contains various mortgage-related information such as the determination of an adequate mortgage loan amount, the selection of mortgage products, and types and risks of mortgage products. The information also includes mortgage terms, fees and penalties, available market information, and strategies for managing unexpected incidences. The checklist enables borrowers to compare different mortgage products from several institutions and to help them reach an optimal choice among the products. The handbook book and the check list have been being distributed through government organizations, websites and branches of banks, and that of KFB.

In January 2017, the government announced an overall plan to beef up the financial education for consumers, the details of which will have to be refined in coming years. The plan was based on two previous tasks that the regulatory authorities undertook in this vein, one in 2013 and another in 2015; the former proposed surveys of financial literary and the latter designed consumer education programs based on the survey results. The survey exhibits that consumers of different age-cohorts tend to have different appetites for financial products and, using that as an evidence, the supervisory authorities proposed the education programs by age cohort in 2017. Nonetheless, the programs are still in an infant stage in the sense that the government put together the existing programs designed by government agencies, public associations, consumer advocate groups, and banking or non-bank financial institution organizations, and there should be more specific standards or industry-wide norms for an effective consumer education program.

Financial advisors are generally not common for the consumer lending products unlike the insurance or investment products. Nonetheless, for some complicated consumer loans such as the reverse annuity mortgage (RAM), it is mandatory for consumers to take a counseling session from the advisors who are specialized with the product. To that end, the KHFC issued the handbook for RAM borrowers, similar to the one in the U.S. for the Home Equity Conversion Mortgage (HECM) borrowers. RAM applicants are required to consult financial advisors employed by KHFC and the advisors should take training programs to acquire their qualification.

2. Assessment and Policy Implications

The handbook and the checklist developed in 2007 are mainly for consumers of residential mortgage loans, even though they take slightly more than a half of total household debt.[9] Although it is likely that borrowers for other consumer loans face the same information issues, only limited educational materials (e.g. brochures) are available for credit card receivables and automobile loans. Hence, the programs to enhance financial literacy should become more broad-based by covering those non-mortgage lending sectors as well.

Although FSC and FSS announced several consumer education programs by age cohorts in 2017, their implementation is still in a very early stage. It appears to be necessary for the regulatory authorities to take a more active role in designing the best practice education modules that are tailored for different age-product combinations. To this end, the government recently announced that they plan to establish the Council for Financial Education and Financial Education Council (for Youth), which is mandated to develop and implement financial literacy programs. In sum, the regulatory bodies will have to lead or coordinate the education programs provided by a wide range of financial organizations more effectively and efficiently.

As to the advisors, financial consumers in Korea are generally not advised to get counseling from them. However, there always exist vulnerable groups in the consumer lending sector, for whom a professional counseling will lead to a welfare-enhancing loan choice. To this end, some of the international benchmarks will have to be examined, such as the consumer counseling program administered by the Federal Housing Administration (FHA) in the U.S.

C. Sales practices

1. Current state and the FCP measures adopted

Since 2016, those qualified borrowers in Korea are allowed to cancel loan contracts within 14 calendar days after signing. The Word Bank (2012) suggests that instituting this cooling-off period is one of the suggested good FCP practices. Nonetheless, the length of the period varies across the countries - 14 days in France and Germany but 3 days in the U.S. In order to exercise this option, the qualified borrowers in Korea need to notify the intention through mail, email, online banking account, or visiting to bank branch. During the cooling-off period, the borrowers do not pay prepayment penalty. However, the original loan contract agreement is not treated as being null or void because the borrowers must reimburse costs incurred by their lender such as stamp tax, appraisal

[9] Delinquent or default rates for other consumer debt are higher than those for mortgage debt. In August 2017, for example, the delinquent rate for consumer loans was 0.28 per cent, even though the delinquent rate for mortgage loans 0.19 per cent.

fee, and legal fee for registration. In addition, the borrowers are not allowed to exercise the option more than three times within a year from the same lender or only once per a month for all the lenders.

The World Bank (2011) reports that the sector-specific "principle-based" codes of conduct in the banking sector, which are available in some countries such as Australia. In Korea, however, there doesn't seem to be such codes of conduct, although each bank as well as the KFB has a general code of ethics. For financial brokers, however, a code of conduct was implemented in 2010, which was devised by financial brokers in consultation with the FSC.[10]

In Korea, financial supervisory bodies have been proposing underwriting guidelines that financial institution should follow. For example, they have instituted the LTV limit since 2002 and the DTI cap since 2005, based on which the mortgage lenders are supposed to originate the loans. One critical issue that should be examined carefully is the fact that that those guidelines have been changing frequently according to housing market conditions or sometimes to public opinion as reported in media, which makes it difficult for borrowers as well as lenders to predict affordable loan products in different locations and time periods.

In 2011, financial supervisory bodies set the quota (or the minimum market shares to achieve) for FRM and for the amortizing mortgage loans, as 30 percent for each loan type. One point to make in this vein is that the definition of FRM (or "amortizing" to that matter) is not crystal clear as lenders can combine those product features to create various hybrid loan products. For example, Fernández de Lis et al. (2013) classify a mortgage loan into three categories: fixed-rate mortgage, initial period fixed-rate mortgage, and variable mortgage; an initial period fixed-rate mortgage includes a rollover mortgage, interest rate of which is renegotiable and a hybrid mortgage, interest rate of which is fixed for a year after origination. In practice, the Korean lenders developed a hybrid mortgage, interest rate of which is fixed for initial five years and is variable after the years, and financial supervisory bodies also acknowledged the hybrid mortgage as a fixed-rate mortgage. According to the Bank of Korea, the market share of the hybrid mortgage reached 43.8 per cent in 2015.

2. *Assessment and Policy Implications*

The cooling-off period is a cost factor for lenders. Hence, the commercial banks in Korea have generally been hesitant in providing the consumers with an option to cancel a loan contract. Furthermore, the option is given only to a very limited group of qualified borrowers, e.g. those who have a contract of mortgage loan with the amount not exceeding 200 million KRW or a contract of non-mortgage loan with the amount less than 40 million KRW.[11] Even worse, a borrower who cancels a loan contract needs to reimburse the most costs incurred, which should be re-examined with various alternative options that are less costly to both parties of loan transaction (e.g. a shorter cooling off period such as 3 days without any penalty or costs borne by the consumers).

There should be a sector-specific principle-based code of conduct as articulated by the World Bank (2012), for which the Australian case can serve as a benchmark. In Australia, there are two different industry professional bodies - Mortgage and Finance Association of Australia (MFAA) and Finance Brokers Association of Australia (FBAA) – which treat mortgage brokers differently from general financial brokers.

As to the product offering, we argue that the mortgage lenders in Korea should have a more leeway in terms of product development and risk assessment via underwriting and other loss-mitigation activities. Currently, the regulatory bodies take a hands-on approach by directly limiting the product offering through the LTV • DTI caps and other lending restrictions. That should be relaxed over time so that FIs should be geared to develop and institute their own products and risk assessment matrices under broad guidelines by the supervisory organizations.

D. Dispute resolution and debt recovery

1. *Current state and the FCP measures adopted*

In Korea, the abusive or violent debt collection practices

---

[10] The FSS articulated that the code of conduct could prevent illegal behaviors for financial brokers such as releasing information on customers, misleading or false adverting, or charging illegal fees.

[11] Note that a median price for medium-size condominiums (62.8 m^2-95.9m^2) is KRW 336 million as of Sep 2017 according to the KB Kookmin Bank.

by banks or their agents – such actions as threats, uses of physical power, repeated visits toward debtors or their related parties - are prohibited by the Fair Debt Collection Practices Act of 2009. In addition, other related activities that can be construed as misrepresentation, unfair conduct, and divulgence of personal information are also prohibited. If any party is found guilty on any illegal debt collection practice as specified by the law, both the person who conducted such action as well as the legal representative of his company will be penalized according to the joint penalty provision specified in the law. While there were some abusive practices existed before the enactment of the law (that received a fair amount of public attention), they are largely disappeared thanks to the 2009 law as well as the enforced civil penalties since then.

As to the dispute resolution mechanisms, the financial consumers in Korea can raise the issue through three main channels: (1) the complaint systems run by individual FIs, (2) those run by the professional associations of FIs (e.g. the KFB), and (3) e-Consumer Complaint Center jointly run by FSC and FSS. In general, the complaints are filed through the first channel, and, if not resolved there, then they tend to go to the next channels. But, in case that there is a dispute between FI and consumer, the case most likely goes to the third channel because the consumer tends to believe that a direct consultation with FIs will not solve such case. If either party (FI or consumer) is not satisfied with the arbitration by e-Consumer Complaint Center, then the case can be resolved via a lawsuit. The statistics on consumer complaints are currently compiled by both FIs and the regulators (FSS), and are released to public periodically.

For the mortgage loans, lenders can liquidate the collaterals (housing or other property) to recover unpaid loan principal at the time of consumer default, mostly through the public auction administered by the court. In this case, the FI notifies the consumer about the procedure to be initiated for the liquidation. Given the fact that most consumer loans in Korea have the recourse provisions, the lender can still recover a deficiency after the collateral sale through a legal procedure. On this issue, the consumer can demand a loan modification either before (called as “a pre-workout deal”) or during the delinquency (called as “an individual work-out deal”). However, this seemingly more efficient resolution method is rarely used due to the low LTV level and, hence, a low probability of positive credit loss after the collateral sale.

In the case of non-collateral lending, if a loan is under a less than three months’ delinquency, the consumer can apply for the pre-workout deal to FIs or to a special council, the Credit Counseling and Recovery Service (which is established under the law to assist financial service for low-income households). In the case that FIs conduct sale or transfer of consumer loans, they should notify and get agreement from the borrowers.

2. Assessment and Policy Implications

Given that the abusive and violent debt collection practices are largely disappeared since the 2009 Act, the legislation appears to be effective. There have been some subtle ways through which the agents attempted to threat borrowers to collect debt, but the law was amended over time to prohibit additional practices as illegal.

As to the consumer complaint and dispute resolution mechanisms, most FIs in Korea have their own contact point with clear procedures for handling consumer complaints; the related statistics are updated and released in a transparent fashion. There are also multiple layers of dispute resolution, all the way to e-Consumer Complaint Center before a lawsuit. However, the current use of the mechanisms doesn’t appear to be efficient in that, when there is a dispute, the case tends to go directly to the regulators’ channel rather than first utilizing the FIs or the associations’ systems. That is mainly caused by the fact that the first two resolution mechanisms do not have a power for binding arbitration, which is currently being debated as a part of the pending FCP law.

Finally, the pre-foreclosure workout options can be utilized more as they can offer more efficient (or less costly) ways to resolve borrowers’ defaults. As mentioned earlier, due to the low LTV levels and the recourse provision, the lenders in Korea are generally reluctant to use the workout routes. But given the time length of a full-blown foreclosure as well as the financial and psychological burden put on the consumer involved, a more active utilization of the workout options will be welfare-enhancing, for which the regulatory authorities in cooperation with other market participants may develop and implement an industry-wide standard procedure.

Table 4. The FCP measures being employed in Korea

	FCP measure suggested	FCP policies being employed	Assessment
A. Information provision	**a. (Summary statement)** A short one or two page summary statement on the product (Principle 8)	A summary statement being required by FSS and FSC through a policy directive in 2007, along with other guides to properly express the interest risk borne by ARM contracts "Mortgage Calculator" being launched in FIs' websites (in 2007), for which FSS introduced an example system The number of documents required for mortgage contract being reduced from 20 to 8 (via the directive issued by FSC and FSS in 2015)	The FCP measures being adopted early on, even before the Global Financial Crisis (GFC), driven in large part by the intent to stabilize the mortgage market rather than to protect financial consumers per se How effective those policies employed are should be a topic of careful investigation (e.g., Are the current contents of the summary statement too detailed or reasonably easy to understand to consumers?) Non-mortgage (residential) consumer lending sectors should have their own FCP measures as well
	b. (Qualification of FI staff) Adequate training for FI staff on products & services (Principle 14)	General training for FI staff on consumer lending being offered by individual FIs (to our knowledge, no particular policy directive on this)	A more systematic training program (for FI staff) should be devised, either by regulatory authority or by FI association; a sector-specific training program (e.g. mortgage loans vs. non-collateralized loans) appears to be preferable
	c. (Change in lending terms) Individual& immediate notification in writing of changes in products (Principle 16)	An e-mail and/or text notification to borrowers for changes in the lending rates or other loan terms being required by the policy directive (in 2007) A guideline on the borrowers' right to seek a modification in loan term to benefit from "improved financial conditions" (first in 2014 and updated in 2017)	A proper notification system, which reflects the consumer preference, appears to be in place; how effective the system is (i.e. whether or not borrowers actually request the modifications in their lending terms to benefit from "improved financial conditions") should be periodically monitored
	d. (Consumer credit data) Ready and free access to their credit reports from credit registers, and provides procedures for correcting mistakes in credit reports (Principle 20)	No specific guidance currently being in place in this regard, although the consumer credit data (along with the 10-digit credit scores) being utilized more and more	A ready and easy access to check consumer credit history along with his/her credit score should be developed; the role of FI and the credit data compiler (the Korea Credit Bureau and others) should be clearly specified The mechanism of compiling the credit score (the CB ratings) should be shared more to promote appropriate research and enhancement
B. Financial literacy	**e. (Programs for financial literacy)** Developing and implementing the financial literacy programs by a wide range of organizations (Principle 33)	The consumer handbook and the check list being issued by individual FIs or by their professional associations since in 2007 A plan to institute a comprehensive program being announced in 2017 by FSC and FSS	An industry-wide norm for education programs for financial literacy should be developed, under a partnership among parties involved (FIs, regulators, consumer groups, academia, and so on) The programs, including the consumer handbooks and check lists, should be developed and updated for both mortgage-lending and other sectors of consumer finance (e.g. credit card loans, auto loans, micro credits)
	f. (Monitoring financial literacy) Measurement of financial literacy of consumers through broad-based household surveys (Principle 36)	Two consumer surveys being done in the recent years - the survey of financial literary (in 2013) and the survey of consumer education programs (in 2015)	The designs and findings of, and future plans for, the two surveys conducted should be share with general public, so that more research for future enhancement can be conducted
	g. (Financial advisor) On forward and reverse mortgage contracts, and for low-income, low-wealth, and less creditworthy borrowers	A mandatory advisory service being required for borrowers of the RAMs	Financial advisory (or counseling) services for more diverse groups of vulnerable consumers should be designed and implemented (e.g. for those borrowers of the government-supported loan programs)

	FCP measure suggested	FCP policies being employed	Assessment
C. Sales practices	**h. (Cooling-off period)** A period during which the consumer may cancel the contract without penalty (Principle 11)	For qualified mortgage borrowers (in terms of loan amount, size of collateral, and so on), a 14 calendar days cooling period being given since 2016;	The qualification conditions should be relaxed or even be abolished, for which the period itself can shortened (as in Germany and other countries) The costs to be reimbursed by the borrowers (at the time of cancelation) should be re-examined to judge their appropriateness as to consumers' (rather than lenders') costs
	I. (Code of Conduct) A principles-based code of conduct that is devised by (by all banks, by all non-bank credit institutions, or by their associations) (Sector-specific Principle)	Individual FIs having their own codes of conduct, mostly designed for general (rather than sector-specific) consumer lending	A systematic review, and a guidance if needed, should be done to explore any area of improvement
	j. (Affordability of product) Product recommended being in line with the need of the consumer; consumer's credit worthiness being properly assessed (Sector-specific Principle)	As a part of the macro-prudential regulations, an industry-wide restrictions on the maximum LTV and DTI being in place (that are quite restrictive in some locations with the max LTV of 40 percent) The above regulations working as constraints for FIs in their underwriting of mortgage applications	Those prudential regulations should be weighed against the issue of financial exclusion as well, in that less credit worthy borrowers are inevitably steered to a high-cost lending sector (e.g. about 5 percent lending rates by first-tier FIs such as the commercial banks vs. 24 percent interest rates by some of the tertiary FIs) The frequent changes in the above regulations, which expose borrowers and banks alike to the uncertainty in lending, should be re-examined
D. Dispute resolution	**k. (Collection practice)** Prohibition of abusive collection or debt recovery practices (Principle 19); **(Debt Recovery)** as Sector-specific Principle	Abusive (or violent) debt collection practices being prohibited by the Fair Debt Collection Practices Act of 2009	The law appears to be effective in that the abusive practices have been declining in number and being monitored closely by the regulatory authorities
	l. (Consumer complaint) Designated contact point with clear procedures for handling customer complaints; up-to-date records of all complaints received (Principle 25); & **(Ombudsman and other conflict resolution mechanisms)** Access to an affordable, efficient, respected, professionally qualified and adequately resourced mechanism for dispute resolution (Principle 26)	The system to process consumer complaints being operated in both FI-level and the FSS-level; statistics on consumer complaints being periodically updated and released Through e-Consumer Complaint Center, jointly-run by FSC and FSS, a binding arbitration on consumer complaint being possible; if not satisfactory, consumer can file a lawsuit	The FIs' dispute resolution systems are less frequently used by the consumers, which can be ameliorated by an independent dispute resolution mechanism inside FIs A binding arbitration power to be given to "alternative" dispute resolution body
	m. (Foreclosure of mortgaged or charged property) Informing in writing in advance of the procedures involved, and of the legal remedies and options available (Sector-specific Principle)	A clear and objective procedure of liquidating collateral (at the time of borrower's default) being in place, which is notified to the borrower before initiating the procedure Options for pre-foreclosure workout (via loan modification) being available, either before or during mortgage delinquency; Consumers can consult with lenders (FIs) or with the Credit Restoration Committee on those options	FIs are in general reluctant (or passive) in using the pre-foreclosure workout options; a more standardized workout procedure should be devised so as for FIs to be incentivized to use the options more actively and to avoid the costly full-blown foreclosure procedures

Ⅴ. Summary and Concluding Remarks

In this study, we attempt to survey and assess the FCP measures adopted in the household lending sector in Korea, out of which we report several key findings: first, the FCP policies in the sector are fairly comprehensive in that they cover almost all good practices suggested in the literature, although some measures are in a fairly early stage, the financial literacy programs in particular; second, the rules and regulations in the consumer lending (e.g. various macro-prudential regulations employed) tend to focus more on the issue of financial stability, and one should weigh the anticipated benefit in that regard against the unintended cost in financial inclusion; third, the FCP policies in the consumer lending sector of Korea tend to focus on the residential mortgage lending sector, which should be extended to other consumer lending products (e.g. credit – or non-collateralized – lending, credit card receivables, and car loans).

In addition, there is a host of implementation and monitoring issues, some of which we list below as the topics of future research:

- The summary statement ~ Does it contain too much information and details? Do they actually help the understanding of consumers on the product in question?
- The financial literacy programs ~ Are they effective in that they help consumers make a more informed decision? Should an industry-wide norm for the programs be developed?
- The training programs for FI staff ~ Do they have to be sector-specific such that they provide a meaningful help for consumers of different lending sectors?
- The rules and procedures to check the consumer credit data ~ Are they ready and easy enough for consumers? Are enough details being shared on the widely-used consumer credit scores (as to their input data and methodologies) such that future research for enhancement can be fostered?
- The cooling-off period after contract signing ~ Are the qualification conditions and the costs involved appropriate given the practices in other countries (e.g. Germany, and the U.S.)?
- The financial advisory (or counseling) services ~ Do they cover diverse-enough groups of vulnerable consumers (e.g. for those borrowers of the government-supported loan programs)?
- The dispute resolution mechanisms (by FIs and by the regulators) ~ Are they working effectively as a pre-lawsuit conflict resolution mechanism? Are the pre-foreclosure workout options being utilized enough both by FIs and by the consumers?

We also want to reiterate the importance of a timely passage of the special FCP law in the Congress, which will put various FCP issues in the lending sector, both the software aspects (rules and procedures) and the hardware dimensions (governance structure), into a more firm ground.

Two particular issues are worth mentioning as our conclusion remarks. First, we believe that a sound FCP policy is almost all about a proper matching between various loan products and different consumer segments, which should in turn consider to two particular dimensions – product affordability and risk management. To illustrate, one can lay out a baseline consumer segmentation in terms of income and lifecycle stage as follows:

Table 5.

Income level	20s & 30s	40s & 50s	60s & 70s	Over 70s
Very low	C_{11}	-	-	C_{41}
Low	-	C_{22}	-	
Moderate	-	-	C_{33}	
High	C_{41}	-	-	C_{44}

An initial question to pose is, for each cell in Table 3, C_{ij}, which product - whether it is collateralized or not – will be affordable and welfare-maximizing in the demand-side and, at the same time, will that be in-scope in terms of a risk management capability in the supply-side? As to the residential mortgage lending, there has been a fairly long history of research on consumer choice on mortgage products, between FRM vs. ARM (numerous early studies plus Campbel and Cocco (2003), Miles (2004)), and between the prime vs. sub-prime mortgage contacts (to be quoted). Although it is difficult to pinpoint which product is most welfare-enhancing for a particular consumer segment (say, C_{ij} in the table) based on those studies, a good FCP policy, as we claim, should enhance consumer capability for product selection via effective education programs and other means and should also induce risk-based lending via a proper regulatory and monitoring scheme.

However, a real-world consumer segmentation tends to be more complicated as it should encompasses various other dimensions, e.g. loan purpose (those primary residence vs. those for investment in the case of residential mortgage), demographic factors of importance (first-time home buyers, family size, marital status, and so on), consumer credit ratings (FICO scores in the U.S. and the CB ratings in Korea), and other underwriting conditions (LTV • DTI caps, default insurance, and so on). In the supply-side, there are also various differentiating factors in developing and intermediating the products, e.g. lending channels (direct lending vs. third-party lending vs. on-line lending), product attributes (maturities, interest variability, principal amortization, and prepayment penalty), and funding method (deposit-based vs. whole-sale based). It is documented in the literature that financial consumers are in general not that informed about risk profiles of available financial products (Miles (2004) for the UK case, Agawal et al. (2010) for the U.S. case), and that the various education programs to enhance financial literacy for consumers tend to be ineffective (Tennyson (2016)). Hence, a more micro, or segment-specific, approach is warranted in designing an FCP policy to better match loan products to various consumer cohorts, which consider both dimensions of product affordability and of prudent risk management.

Another issue to comment on is reflecting a process view in designing the FCP policies. That is, the consumer lending business takes multiple steps – from loan application, to underwriting, contracting, servicing, and all the way to loan termination; and different FCP and risk management issues usually come about and may have to be subjects to a policy consideration. We believe that this process-driven view can make the FCP policies in the sector more relevant and realistic, and expect to see careful analyses both from academia and policy circle to be done going forward to make the policy regime in the country more complete and effective.

Reference

Agarwal, S., G. Amromin, Z Ben-David, S. Chomsisengphet, and D. Evanoff, 2010, "Learning to Cope: Voluntary Financial Education Programs and the Housing Crisis," American Economic Review Papers and Proceedings, Vol. 100(2), 495-500.

Brunnermeier, M.K, and M. Oehmke, 2014, "Bubbles, Financial Crises, and Systemic Risk," Working Paper, Princeton University.

Campbell, J., 2006. "Household Finance,", Journal of Finance 61 (4): 1553-1604.

Campbell, J., H. Jackson, B. Madrian, and P. Tufano, 2011, "Consumer Financial Protection", Journal of Economic Perspectives, V25(1), 91-114.

Carroll, C. D., M. Otsuka, and J. Slacalek. 2011." How Large are Housing and Financial Wealth Effects? A New Approach. Journal of Money", Credit and Banking 43: 55-79.

Case, K. E., J. M. Quigley, and R. J. Shiller. 2011. Wealth Effects Revisited 1978-2009, Cambridge, MA: National Bureau of Economic Research.

Chen, T., 2018, "Introduction and Overview of the Book," Chapter 1 in Chen ed., "Comparative Studies of FCP Policies: Cases of the 14 Countries," IAFICO.

Cho, M., 2017, "Contagious Housing Price Cycles: Drivers", Contagion Channels, and Policy Responses," Real Estate Finance, V33(3), Winter 2017.

Cho, M., and K.H. Kim, 2011, "Housing Sector Reform: Contrasting Real Sector vs. Financial Sector," in Young Jae Lim eds. Making Reform Happen (MRH) in Korea, KDI Research Monograph, 2011.

Consumer Finance Protection Board (CFPB), 2016, "Advisory for financial institutions on preventing and responding to elder financial exploitation."

Crowe, C., Dell' Ariccia, G., Igan, D. and Rabanal, P. 2013. "How to deal with real estate booms: lessons from country experiences," Journal of Financial Stability, 9(3): 300-319.

Geanakoplos, John. 2010. "Solving the Present Crisis and Managing the Leverage Cycle." FRBNY Economic Policy Review 16:1, 101-131.

Fernandez de Lis, Santiago, Saifeddine Chaibi, Jose Felix Izquierdo, Felix Lores, Ana Rubio, and Jaime Zurita. 2013. "Some international trends in the regulation of mortgage markets: Implications for Spain." BBVA Bank, Economic Research Department. Working Paper 1317,

Han, J., M. Hwang, and M. Cho, 2016, "Credit Constraints and Synchronous House Price Movements: Evidence Based on from the Mortgage Credit Regulations in Korea," *mimeo.*

Iacoviello, M. (2005). "House prices, borrowing constraints, and monetary policy in the business cycle." American Economic Review 95 (3), 739-764.

Iacoviello, M and Pagan. (2013). "Housing and debt over the life cycle and over the business cycle." Journal of Monetary Economics 60 (2), 221-238.

Kim, K.H., and M. Cho, 2014, "Mortgage Markets International," in K. Baker and P. Chinloy ed. "Public Real Estate Markets and Investments," Oxford University Press.

Lusardi, A., and O. Mitchell, 2007, "Baby Boomer Retirement Security: The Roles of Planning, Financial Literacy, and Housing Wealth." Journal of Monetary Economics, 54(1): 205-24.

Lusardi, A., O. Mitchell, and V. Curto, 2010, "Financial Literacy among the Young." Journal of Consumer Affairs, 44(2): 358-80.

Lusardi, A., and P. Tufano, 2009, "Debt Literacy, Financial Experiences, and Overindebtedness," NBER Working Paper 14808.

Mian, Atif, and Amir Sufi. 2011. "House Prices, Home Equity Based Borrowing, and the U.S. Household Leverage Crisis." American Economic Review 101:5, 2132-2156.

Mercer Oliver Weiman, 2005, "Risk and Funding in European Residential Mortgages: Responding to Changes in Mortgage Demand." Mortgage Insurance Trade Association.

Miles, D. 2004. "The UK Mortgage Market: Taking a Long-Term View; Final Report"Imperial College of London (Report Submitted to Chancellor of Treasury).

Miles, D. 2003. "The UK Mortgage Market: Taking a Long-Term View; Interim Report" Imperial College of London (Report Submitted to Chancellor of Treasury).

OECD, 2011, "High-Level Principles on Financial Consumer Protection."

Tennyson, Sharon, 2016, "Can Regulations Improve Financial Information and Advice", *International Review of Financial Consumers* 1 (1): 1-8.

Thaler, R., and C. Sunstein, 2008, "Nudge: Improving Decisions about Health, Wealth, and Happiness." New Haven, CT: Yale University Press.

The World Bank, 2012, "Good Practices for Financial Consumer Protection," The World Bank, June 2012.

You, S. D., An Analysis of Borrower's Mortgage Debt-servicing Burdens (in Korean), Financial Stability Studies 7(1), 2006, 135-170.

Wachter, S., M. Cho, and M. Tcha, 2014 "The Global Financial Crisis and Housing: A New Policy Paradigm," KDI-Edward Elgar.

Received/ 2017 .09 .20
Revised/ 2017 .10 .20
Accepted/ 2017 .10 .23

Appendix 1. Good FCP practices (selected from the World Bank (2012))

A. (Mandatory) information provision

a. **(Summary statement)** For all financial products or services, consumers receive a short one or two page summary statement (or electronic equivalent), presented in a legible font and written in plain language, describing the key terms and conditions, including recourse mechanisms, applicable to the financial product or service (Principle 8)

b. **(Qualification of FI staff)** Staff of financial institutions who deal directly with consumers receive adequate training, suitable for the complexity of the products or services they sell. In particular, financial intermediaries are qualified as appropriate for the complexity of the financial product or service they sell (Principle 14)

c. **(Change in lending terms)** As early as possible, customers are individually notified in writing (or by electronic means) of changes in interest rates, fees, and charges or other key terms and conditions of their financial products or services (Principle 16)

d. **(Consumer credit data)** For credit registries, the law specifies the extent and timeliness of the updating of customer information, gives customers ready and free access to their credit reports from credit registers (at least once a year), and provides procedures for correcting mistakes in credit reports (Principle 20)

B. Financial literacy

e. **(Programs for financial literacy)** A wide range of organizations (including government, state agencies and non-governmental organization) are involved in developing and implementing the financial literacy program. The government appoints a ministry (e.g. the Ministry of Finance), the central bank or a financial regulator to lead and coordinate the development and implementation of the program (Principle 33)

f. **(Monitoring financial literacy)** The financial literacy of consumers and the impact of consumer empowerment measures are measured through broad-based household surveys that are repeated from time to time to see if the current policies are having the desired impact on the financial marketplace (Principle 36)

g. **(Financial advisor)** An independent financial advisor is needed, especially for vulnerable groups (low-income, low-wealth, and less creditworthy borrower cohorts) or for particularly complex mortgage contracts, e.g. Reverse Annuity Mortgage *(Refer the UK and other cases)*

C. Sales practices

h. **(Cooling-off period)** Except for securities and derivatives, financial products or services with a long-term savings component—or those subject to high-pressure sales practices—have a —cooling-off‖ period, during which the consumer may cancel the contract without penalty (Principle 11)

i. **(Code of Conduct)** There should be a principles-based code of conduct that is devised by (by all banks, by all non-bank credit institutions, or by their associations) in consultation with the financial supervisory agency and consumer associations, if possible. Monitored by a statutory agency or an effective self-regulatory agency, this code should be formally adhered to by all sector-specific institutions (Sector-specific Principle)

j. **(Affordability of product)** When a bank makes a recommendation regarding a product or service to a consumer, the product or service it offers to that consumer should be in line with the need of the consumer; The consumer should be given a range of options to choose from to meet his or her requirements; When offering a new credit product or service significantly increasing the amount of debt assumed by the consumer, the consumer's credit worthiness should be properly assessed (Sector-specific Principle)

D. Dispute resolution

k. **(Collection practice)** Financial institutions are prohibited from employing abusive collection or debt recovery practices against their customers (Principle 19)

l. **(Consumer complaint)** Every financial institution has a designated contact point with clear procedures for handling customer complaints, including complaints submitted verbally. Financial institutions also maintain up-to-date records of all complaints they receive and develop internal dispute resolution policies and practices, including processing time deadlines, complaint response, and customer access (Principle 25)

m. **(Ombudsman and other conflict resolution mechanisms)** Consumers have access to an affordable, efficient, respected, professionally qualified and adequately resourced mechanism for dispute resolution, such as an independent financial ombudsman or equivalent institution with effective enforcement capacity (Principle 26)

n. **(Debt Recovery)** A bank, agent of a bank and any third party should be prohibited from employing any abusive debt collection practice against any customer of the bank, including the use of any false statement, any unfair practice or the giving of false credit information to others (Sector-specific Principle)

o. **(Foreclosure of mortgaged or charged property)** In the event that a bank exercises its right to foreclose on a property that serves as collateral for a loan, the bank should inform the consumer in writing in advance of the procedures involved, and the process to be employed by the bank to foreclose on the property it holds as collateral and the consequences thereof to the consumer; At the same time, the bank should inform the consumer of the legal remedies and options available to him or her in respect of the foreclosure process (Sector-specific Principle)

The International Review of Financial Consumers, Volume.2 Issue.2(Oct., 2017), 35-48 pISSN 2508-3155 eISSN 2508-464X
https://doi.org/10.36544/irfc.2017.1-2.3

The International Review of Financial Consumers
www.eirfc.com

Understanding Gen Y and Their Complaint Behavior towards Bank

Melia Retno Astrini†

A B S T R A C T

In banking industry where company has various direct service delivery moments with consumers, complaints seem inevitable. In Indonesia, banking industry has always been ranked as the top 5 industries that get a lot of complaints from consumers. In this study, we interested to discuss about complaint behavior intentions, specifically within Generation Y consumers. In this study, we particularly interested to discuss about complaint behavior intentions of Generation Y consumers. This is important as an effort to predict future market trends, since nowadays, consumers are dominated by digital consumers like Generation Y. Thus, identifying whether the unique characteristics of Generation affects their complaint behavior will be beneficial for company in creating an appropriate complaint handling strategy.

The data in this study were collected using online survey questionnaire to a total of 131 banking customers. A regression analysis was performed to examine the effect of Generation Y characteristics towards their intention to complain. The results showed that from five Generation Y's characteristics tested in this study, only characteristics of tech savvy and desire to engage in social media were proved to significantly affect Generation Y's intention to complaint. Meanwhile, all the characteristics of Generation Y do not have effects on to their intention to repurchase after service recovery effort from service provider. Moreover, the study also provides managerial implications to suggest ways for banks to manage customers' complaint, particularly that comes from Generation Y.

Keywords: consumer protection; complaints handling; financial services in Indonesia; consumer unpleasant experiences

Ⅰ. Introduction

The study about consumer complaint behavior has begun since 1970s, however, this topic has remained interesting to be discussed nowadays both for business and research (Velázquez, Blasco, and Contrí, 2010). Especially in banking industry where company has various direct service delivery moments with consumers, complaints seem inevitable. There is numerous service encounter during the delivery of banking services, and in each of the service encounter, people might have expectations towards the banking services that they receive. If these expectations are not met by banking institution, consumers might see it as a service delivery failure, and it will have resulted in consumer dissatisfaction and potential complaints (Ngai, Heung, and Chan, 2007). Traditionally, complaint behavior had been regarded as a negative response from dissatisfied consumers to the company; however, nowadays researchers and managers consider complaints as a useful feedback from consumers, and those "useful feedbacks" enabled companies to become aware of problems in service (Oh, 2005). If the bank treats complaints as a valuable feedback and correct the mistakes early in the process, the bank will be able to avoid the spread of negative word of mouth from dissatisfied consumers, and consumer might also give positive reports

† University of Indonesia
melia.retno@ui.ac.id

about the bank to others (Keng, Richmond, and Han, 1995). Eventually, complaints from customers shall prevent the bank from losing its customers, encourage repeat business, and sustain their success in a competitive banking industry (Ngai et. Al., 2007). Therefore, both from theoretical and practical perspectives, understanding consumer complaint behavior in the banking industry is essential for the banks to deliver sustainable prosperity (Meng, 2010).

Specifically, in the case of Indonesia, banking industry has always been ranked as the top 5 industries that get a lot of complaints from consumers. In 2016 alone, out of a total of 1819 complaints submitted to Yayasan Lembaga Konsumen Indonesia (YLKI)--an Indonesian Consumers Foundation-- 56% were dominated by three main sectors that are banking, real-estate, and online shopping (Nabhani, 2017). There are 249 consumer complaints associated with banking services. On the other hand, as of October 2016, the Indonesian Financial Services Authority (OJK) recorded 913,092 reports to OJK in relation complaints against the banking service provider (Nabhani, 2017).

In order to understand consumer behavior, many researches use generational differences since generational cohorts often show similar behavioral characteristics reflecting their similar experiences, technologies, and adaptation to cultural and environmental changes. Thus, generational cohorts usually share similar values and beliefs, which then influence their behavior (Brosdahl and Carpenter, 2017). Harrington et. al. (2012) stated that the similar values and beliefs might also affect consumers' intention to complain or reactions to service, considering that values and beliefs will strongly affect consumers' perceptions of service recovery and justice (Sharma et al., 2012). However, despite substantial research about generational differences, there were not many studies explicitly explain the effects of generational differences in the context of customer complaint behavior (Soares et. al., 2017). According to previous study (Bolton et. al. (2013); Brosdahl and Carpenter (2011)), generational categorization can be divided as follows: The Silent Generation (1925-1945), the Baby Boomers (1946-1960), Generation X (1961-1981) and Generation Y (1981-1999).

In this study, we particularly interested to discuss about complaint behavior intentions of Generation Y consumers. In an effort to predict the future market trends, researchers and companies have been actively investigate the behavioral patterns of this generation of consumers (Nusair et al., 2011 in Soares et. al., 2017). Generation Y has been regarded as an important segment in banking service since this generation is the future of banking business in Indonesia. They are digitally native consumers; thus, represent characteristics of current digital consumers. They are also the generations who will become early adopters and main users of banking digital services. However, there still not much of study that examine the complaint behavior of Generation Y consumers, especially in the context of banking industry in developing countries such as Indonesia. Furthermore, as a digitally native consumer, Generation Y tend to spread negative word-of-mouth quickly when they feel dissatisfied towards company. The consequences will be extensive and costly if company fails to listen and to take appropriate action to manage the complaints of Generation Y. Hence, identifying whether the unique characteristics of Generation affects their complaint behavior will be beneficial for company in creating an appropriate complaint handling strategy. For the purpose of this study, Generation Y rendered as a people within the age group of 18-36 years old. This generation accounts for ± 100 million[1] people in Indonesia (Indonesian Statistics Bureau, 2010).

The purpose of this study is in turn as follows: to investigate factors that relate to Generation Y consumers' complaints about a service failure and service recovery responses. This paper will be organized as follows: the first section will report the literature that we use as a theoretical foundation of this study and to present the proposed model. Then, the methodology section provides details related to measurement, data collection, and sampling. After discussing the results from data analysis, this study concludes with managerial implications, limitations, and outlook for future research.

[1] The exact number is 100,418,626 people. However, the numbers are for people in an age group of 15 – 39, not necessarily 18 – 36 as this study proposed.

Ⅱ. Theoretical background and research hypotheses

A. Customer Complaint Behavior

According to Singh and Widing (1991), consumer complaint behavior can be defined as all potential behavioral responses that consumers may utilize to deal with his/her dissatisfaction. It is commonly understood that consumers have the right to take action or not take action after they experience service failure. If they decided to take action, consumers usually have different style to communicate their dissatisfaction. They may, among others, switching patronage, telling friends and family, or complaining to a consumer agent (Ndubisi and Ling, 2006).

The literature generally categorized the complaining behavior constructs into two dimensions, which are public complaining response and private response (Varela, 1992; Crié, 2001 in Velázquez et. al., 2010). Blodgett et. al. (2006) explains that private responses include word of mouth comments and change behavior, and recently it also includes web site communications. Meanwhile, public responses refer to complaints directed at the parties involved in the transaction, could be the companies involved in the transaction or third parties, such as consumer protection bodies, the media or legal action (Singh, 1988, 1990; Singh and Pandya, 1991; Blodgett and Granbois, 1992 in Velázquez et. al., 2010). Given that both types of complaints may have very different causes and consequences, another complaint behavior classifications consider them as different dimensions, hence, added another dimension to the classification, which then consists of three dimensions including private responses, complaining responses and third-party responses (Singh, 1988, 1990; Liu and McClure, 2001). To offer a more detail analysis into complaint behavior, this study will measure complaint behavior constructs using those three dimensions that are private responses, complaint responses, and third-party responses.

1. Complaint Behavior and Demographic Characteristics

Previous studies on consumer complaint behavior have shown that consumer characteristics were important in predicting consumer complaint behavior. This characteristic includes demographics variable, factors that are associated primarily by the consumer (Keng et. al., 1995). Some of the demographic variables are found to influence consumer complaint behavior. In the 1970s, it was confirmed that public complainers tend to be younger in age, had better education, and higher income (Warland et. al., 1975; Day and Landon, 1977). Beardon and Mason (1984) supported the previous results that age had inverse relation with complaint behavior, and income and education positively related to complaint behavior. However, other variables such as race, family type, and employment status did not prove to have significant relationship with complaint behavior.

Keng et. al. (1995) studied complaint behavior in Asian setting--using Singapore shoppers as respondents and identified the different characteristics of complainers and non-complainers. The study found that complainers who resorted public actions tend to be older age groups, better educated, and earned higher incomes. Keng et. al. (1995) confirmed that three demographic variables, which are age, income, and the level of education were positively influenced consumer complaint behavior, while the other demographic variables (marital status, ethnic, and language medium in which respondents received his/her education) do not have influenced on complaint behavior. They also found that there is significant relationship between gender and consumer complaint behavior, and women were more inclined to make complaints than their male counterparts.

Lam and Tang (2003) studied complaint behaviors in Hongkong restaurant industry context and found that customers who were younger, better educated, and had higher income tended to complaint more than those who were older, less educated, and had lower income. Also, in Hongkong, Heung and Lam (2003) revealed in their studies that young and middle-aged consumers (18-44 years old) complained publicly more than older consumers, and female and higher educated customers complained more than male and less educated customers. However, different from previous studies, DeFranco et. al. (2002) found that gender has no significant relation with consumer private actions to complain; however, significant difference was found between male and female when a public action was taken. In addition, DeFranco et. al. (2002) found that age, education, and income have no significant relationship with complaint behavior, either publicly or privately in hotel restaurant services context. Another study conducted by Sujhitamrak and Lam (2004) found that only age, education, and income affect the complaint behavior of customers, while gender has no significant effect towards complaint behavior. Based on previous studies, it appears that there was no consistent relationship between complaint behavior and consumer demographic characteristics (gender, age, education, income) (Sujhitamrak and Lam, 2005).

2. Complaint Behavior and Generational Differences

Some of previous studies have confirmed that younger consumers tend to complain more rather than older consumers (Warland et. al., 1975; Day and Landon, 1977; Heung and Lam, 2003). Roschk et. al. (2003) also found that consumers in the middle and final stage of adulthood (silent generation and baby boomer) tend to be less demanding and less impatient with regards to their complaint behavior. It might be because those older generation have modest personality, low professional status, or low financial liabilities, which make them more prepared in accepting service failure.

The study conducted by Soares et. al. (2017) further confirmed that generational differences were significant predictors of consumers' complaint behavior. According to Soares et. al. (2017), older generations were less likely to complain than Generation Y, but then, the Generation Y consumers most likely to repurchase when service providers offered an effective service recovery strategy. Consequently, it is reasonable to assume that people in different generations exhibit different type of complaint behavior (Soares et. al., 2017).

In Indonesia, studies about Generation Y reveals several characteristics specific to that generation. The most prominent characteristics of Generation Y in Indonesia is they are very familiar with technology, hence, almost all their characteristics are consequences from their ability to operate those digital devices. First and foremost, Generation Y is comfortable in using social media in the daily basis, unlike Silent Generation or Baby Boomers who rarely use social media. Thus, Generation Y prefers to read news via online media rather than conservative media (e.g. newspapers) (Centre for Strategic and International Studies, 2017). Moreover, Generation Y likes to communicate with their peers via social media and online chatting (e.g. Whatsapp, Line, Instagram, etc). In terms of shopping behavior, Generation Y buys something via online shop and often use cashless means to do transaction.

B. Generation Y consumers

There is limited consensus among researches regarding the precise start and end points for Generation Y (Soares et. al., 2017). However, in this study, we follow Bolton et. al. (2013) categorization, which stated that Generation Y is people who born between 1981 to 1999. This means that when the study is conducted, this people will be in the age range of 18 – 36 years old. Researchers have proposed other categorization scheme because they have not agreed on precisely the characteristics that differentiate one generational group to the others, plus there are also within-generation differences (Bolton et. al., 2013). Hence, the characteristics of Gen Y are sometimes discussed in overly broad terms. Nevertheless, for the purpose of this study, the characteristics of Generation Y consumer will be briefly summarized and only some of the characteristics will be used such as tech savvy, being heavily influenced by peers, prolific use of social media, and desire to engage in social network.

1. Tech Savvy

Generation Y was born and raised in the technologically advanced era. This generation is tech savvy and familiar with the use digital devices and technology (Bolton et. al. (2013) in Soares et. al. (2017). Hence, technology has been incorporated into their daily life from their reliance on social media (e.g. Facebook, Instagram), smartphone, and chatting, watching and creating videos via youtube, blogging on the internet, or video chatting with people across the globe. They are the first generation that spent their entire life in the digital environment; thus, they often called as Digital Natives rather than Digital Immigrants (Prensky, 2001).

Todays, the development of technology has increased the range of communication channels between consumers and firms (Camarinha-Matos, 2011 in Soares et. al., 2017), including Bank. The development has encouraged Bank to also use digital communication channels, including social media, to communicate with their consumers. These new digital channels are fast developing and widely adopted, especially by Generation Y who are highly prone to adopting new technologies. In turn, using these new digital channels, Generation Y consumers are able to share their evaluations or service quality experience more easily (Muskat et. al., 2013 in Soares et. al., 2017), including complaints following service failure. In this sense, it is expected that Generation Y consumers are more likely to complain about a service failure that they experienced because they have greater and easier access to use technology-supported media. The same is also applied to the company. Since they have an advanced communication channels that enables them to hear their consumers directly, they should be able to prompt rapid response to recover the consumers' service failure, which may lead to greater consumer satisfaction and increase the likelihood of consumers to repurchase from them. Hence:

H1: Generation Y consumers' tech savviness is positively related to (a) the likelihood of complaining after service failure, and (b) repurchasing after receiving satisfactory service recovery

2. Heavily influenced by peers

In general, it is known that social environment such as peers and relatives could influence consumer behavior. In theory of planned behavior research, this statement is widely accepted since researches has proven that individuals are likely to hear opinion from their significant others before they perform certain behavior (Ajzen, 1991). Specifically for generation Y consumers, they were said to be community minded, meaning that they tend to strongly value their friends and relatives. In their survey, Boston Consulting Group (2012) found that for Generation Y, the definition of "expert"- a person with credibility to give opinion about brand, products, and services- has shifted from someone with professional or academic credentials to potentially anyone with firsthand experience, ideally their peer or relatives. Generation Y consumers' active participation in social networking, either virtual or physical networking, contributed to their interpersonal connectedness. This vast connections towards each other provides Generation Y with a voice that is louder and more impactful than that achieved by previous generations. Based on theory explain above and study conducted by Soares et. al. (2017), this study expects that Generation Y will rely on their peers or relatives when considering whether to complaint, accept the service recovery effort from company, or decided to stay with the service provider (Soares et. al., 2017). If peers hold favorable view toward complaining or accepting service recovery from service provider, then, Generation Y consumers will likely adopt similar view. Furthermore, since Generation Y consumers are tech savvy, it is easy for them to access others' opinion in the internet or in other social media that they have. Hence:

H2: Generation Y consumers' being heavily influenced by their peers, is positively related to (a) the likelihood of complaining after service failure, and (b) repurchasing after receiving satisfactory service recovery

3. Low trust in brand

There are considerable amount of evidence that shows Generation Y tends to be immune towards advertisement or other branding efforts. They practically grew up in an environment where information about products is abundant and easy to be accessed, hence, they might see round-the-clock advertisement on their smartphones and social networking sites (Soares et. al., 2016). Generation Y consumers' purchases are more benefit-driven than brand-driven. This generation, also called Millenial generation, is much more willing to experiment with new brands, hence, they thrive on options—the more the merrier (Pasquarelli, 2017). This notion is also supported by previous research, which found that Generation Y consumers exhibit relatively low trust towards brands and advertising (Obercam, 2013 in Soares et. al., 2017).

Judgment related to service failure is partly influenced by brand trust and brand loyalty (Brady et. al., 2008 in Soares et. al., 2017), so that consumers with greater brand loyalty or trust is incline to forgive service failures and continue in their relationship with the service providers. Nonetheless, since Generation Y has low trust in brand, this generation tends to be more sensitive to and dissatisfied with the service failure they experience, thus they should be more likely to complain after they experience service failure. In addition, Generation Y decision-making judgment depends mainly on the value that they received from the service provider. If Generation Y satisfied with the service recovery efforts given by the service provider, these consumers tend to stay with the firm and repurchase from it. Hence:

H3: Generation Y consumers' low trust in brand, is positively related to (a) the likelihood of complaining after service failure, and (b) repurchasing after receiving satisfactory service recovery

4. Prolific use of social media

Previous research indicates that Generation Y consumers are obsessed with social media (Bolton et. al., 2013). Driven largely by their strong need to interact with other people, his generation regularly updates their social profile in their online social network (Bolton et. al., 2013). Since they were growing up in a technologically advanced environment, they were already mastered using social media, computers, or internet for most aspect of their lives, including communication in particular (Leggett, 2013 in Soares et. al., 2017). Generation Y consumers are prone to value other opinions in social media, and they feel important when they provide feedback for their peers related to the experience using products or services. They believe that by providing feedback, they can influence how others view the brand or services (Savage et. al., 2011 in Soares et. al., 2017). In addition, Generation Y consumers has stronger beliefs, compare with Baby boomers, that service providers should offer consumers more ways to share their opinions online (Forrester, 2013). Therefore, Generation Y, with their heavy dependence on social media to support their decision-making, is expected to share more of their experience, either positive or negative, to their peers or the service providers, as well as to repurchase after service recovery efforts from service provider. Hence:

H4: Generation Y consumers' prolific use of social media, is positively related to (a) the likelihood of complaining after service failure, and (b) repurchasing after receiving satisfactory service recovery

5. Desire to engage in social network

Most of Generation Y regarded social networks as a necessity for their daily existence, both offline and online. The results from BCG research shows that Millennials use social-media platforms more than non-Millennials (79 percent versus 59 percent), and they maintain significantly larger networks; 46 percent have 200 or more "friends" on Facebook, compared with 19 percent of non-Millennials (Boston Consulting Group, 2012). They use technology to connect with a greater number of people, more frequently, and in real-time. Generation Y thinks that they are missing out if they do not share moments on social media, and they feel accepted when the community "likes' their posts (Boston Consulting Group, 2012).

Previous research has shown that the main reasons Generation Y use social media are for social needs and social networks. This desire for connection and shared experience also extends offline. Millennials are much more likely than non-Millennials to engage in group activities—especially with people outside their immediate family (Boston Consulting Group, 2012). In today's market,

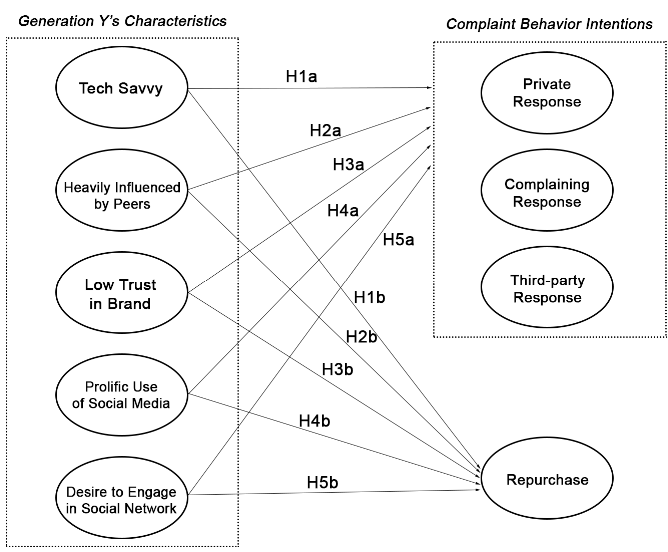


Figure 1. Proposed Model

companies are increasingly providing not only quality service to consumers but also creating a community of people with shared interest, which can be regarded as social networks (Soares et. al., 2017). Since Generation Y consumers do not want to lose these social networks, they are reluctant to switch to another firm. Hence:

H5: Generation Y consumers' desire to engage in social network, is positively related to (a) the likelihood of complaining after service failure, and (b) repurchasing after receiving satisfactory service recovery

Ⅲ. Research methodology

A. Data source and measurement scale

The data has been collected through a structured questionnaire. The items in the questionnaire were adopted from previous studies, measured using a 7-point Likert scale (1= "strongly disagree to 7= "strongly agree"). The items to measure generation Y characteristics including tech savvy (three items), heavily influenced by peers (three items), low trust in brands (four items), prolific use of social media (three items), and desire to engage in social network (three items) were adopted from the scales used by Soares et. al (2014).

Complaint behavior intentions constructs were measured using scales from Velazquez et. al. (2010). Moreover, the three-item repurchase scale was derived from Soares et. al (2017). The socio-demographic profiles of the respondents such as gender, age, monthly expenditure, and education level were also recorded. In the last part of the questionnaire, the questions related to respondents' real service failure and complaint experience were also asked. Thus, there were a total of 39 questions in the questionnaire included a service failure and service recovery scenario in the banking context. The scenarios were self-developed and examined by the experts and the potential respondents for clarity and appropriateness. The questionnaire was subsequently piloted with 30 Bank consumers to ensure that the questions and response format were clear. Minor adjustments were made based on feedback received from the pilot study.

B. Data collection procedure and data analysis

To data were collected in September 2017 using an online survey. A convenience sampling method was used to collect the data. A link to the survey was posted and advertised to invite people to participate in the study. In the survey, participants are explicitly informed that this study wanted to examine the behavioral intention of Generation Y toward service failure and service recovery situation. Since the intended respondents for this study are people who are define as Generation Y (be aged within the ranged of 19 - 36 years old in year 2017), a screening question was given to the respondents to filter out those who are not age between 19 – 36 years old. The survey was opened for almost one week, and a total of 160 respondents obtained, however; only 131 responses qualified to be analyzed further. The reliability and validity of the data was examined using Cronbach's alpha and Factor analysis. Then, multiple regression analysis was used to test the hypotheses in this study. The data was being analyzed using Statistical Package for Social Sciences (SPSS) version 22.

Ⅳ. Results and discussion

A. Description of the sample

The summary for demographic features of respondents is presented in Table 1. The results show that majority of respondents were female (68%), while remaining 32% of respondents were male. The age range is extended from19 – 36 years old, in line with our definition of Gen Y consumers. The results also show that most of respondents are undergraduate (67%), followed by high-school (24%), master (7%), and diploma (2%). Related to the monthly expenditure, most of the respondents (46%) have an expenditure of Rp. 2,000,000 – Rp. 5,0000,000, 23% respondents have an expenditure of Rp. 1,000,000 - Rp. 2,000,000, 15% respondents have an expenditure of Rp. 5,000,000 - Rp. 7,000,000, 7% respondents have an expenditure of < Rp. 1,000,000, closely followed by 6% of respondents who have expenditure of Rp. 7,000,000 – Rp.. 10,000,000, and only 2% respondents with an expenditure of > Rp. 10,000,000. Furthermore, most of

Table 1. Socio-demographic profile of respondents

Variables	Frequency	Percentage (%)
Gender		
Male	43	32.8
Female	88	67.2
Age (years)		
18-22	55	42
23-26	63	48.1
27-30	10	7.6
30-36	3	2.3
Education		
Highschool	30	22.9
Diploma	3	2.3
Undergraduate	90	68.7
Master	8	6.1
Expenditure (in a month)		
< Rp. 1,000,000	10	7.6
Rp. 1,000,000 - Rp. 2,000,000	29	22.1
Rp. 2,000,000 - Rp. 5,000,000	62	47.3
Rp. 5,000,000 - Rp. 7,000,000	18	13.7
Rp. 7,000,000 - Rp. 10,000,000	9	6.9
> Rp. 10,000,000	3	2.3
Frequency in using bank services		
Rarely (could be less than once a month)	2	1.5
Less than 3 times a week	35	26.7
3-5 times a week	78	59.5
Very often (minimum once a day)	16	12.2

the respondents (59.5%) in this study use banking services 3 – 5 times a week, and 26.7% of respondents use banking services for less than 3 times a week.

B. Complaint Behavior

As shown in table 2, respondents in this study were in favor in taking private responses and complaint responses to third-party responses. Highest scores were achieved for “I would tell my friends and/or relatives...” (mean = 6.37), followed by “I would complaint to bank personnel who is responsible⋯” (mean = 5.99), and “I would rather use financial products/services from another bank” (mean = 5.72). Third-party responses including “I would tell a consumer protection body⋯” (mean = 4.09), “I would write a letter to local newspaper⋯” (mean = 3.5), and “I would take legal action against the bank” received the lowest scores. The results in this study showed that when consumers experienced service failure from bank, they prefer to complain privately rather than publicly via third-party. Such findings were consistent with previous study by Lam and Tang (2003) which found that complaint behavior in restaurant industry context in Hongkong were mainly private rather than public responses.

Furthermore, of all the total respondents in this study, 55% of them (72 respondents) had real service failure experience with bank. Among 72 respondents who had service failure experience, 80% of them stated that they complaint about their bad experience to the bank. The other 20% said that they were not reported their service failure experience to the bank. The type of banking products/services that are the source of the service failure they experienced. According to the respondents, the three biggest source of service failure are automated teller machine (ATM), mobile banking, and savings account, respectively. Moreover, specifically most of the respondents said that the facility of the bank (including ATM, Internet Banking, SMS Banking, Mobile Banking, etc) is not functioned correctly, and often times they fail to do the transaction via ATM or mobile banking. Some of the respondents also mention that the service that they received from the bank staff was not satisfactory.

Table 3 shows the t-test differences between respondents who had previous service failure experience and respondents who never experience service failure on their intention to exert complaint behavior. In all the types of complaint behavior (private, complain, or third-party responses), there were no significant differences between the two groups, with experience and no experience. The mean responses between the two groups are also almost identical, which indicates that prior service failure experience did not increase the likelihood of consumer to complaint.

C. Results

1. Reliability and validity

Prior to testing the hypothesis, the reliability and validity of the items used in this study is examined. To measure reliability, cronbach’s alpha is used. The sug-

Table 2. Customer Complaint Behavior

Customer Complaint Behavior	Type of Complaint Behavior	Mean	Ranking
I would tell my friends and/or relatives about my bad experience in using financial product/services from that Bank	PR	6.37	1
I would complain about my bad experience to related bank personnel who is responsible in giving me such bad experience, and asking for solution	CR	5.99	2
I would rather use financial product/services from another Bank	PR	5.72	3
I would have commented on my bad experience so that the Bank could improve	CR	5.4	4
I would complain about my bad experience to the manager or other top management position of that Bank	CR	5.28	5
I would not use financial product/services from that Bank again	PR	5.26	6
I would persuade my friends and/or relations not to use financial product/services from that Bank	PR	5.06	7
I would tell a consumer protection body regarding my bad experience	TR	4.09	8
I would write a letter to a local newspaper describing my bad experience	TR	3.5	9
I would take legal action against the bank	TR	3.2	10

Table 3. Complaint Behavior by Service Failure Experience

Complaint Behavior	Mean		Sig.
	Real Service Failure Experience	No Service Failure Experience	
I would tell my friends and/or relatives about my bad experience in using financial product/services from that Bank	5.55	5.67	0.471
I would rather use financial product/services from other Bank			
I would not use financial product/services from that Bank again			
I would persuade my friends and/or relations not to use financial product/services from that Bank			
I would complain about my bad experience to related bank personnel, that is people who responsible in giving me such bad experience, and asking for solution	5.55	5.57	0.638
I would comment on my bad experience so that the Bank could improve			
I would complain about my bad experience to the manager or other top management position of that Bank			
I would tell a consumer protection body regarding my bad experience	3.65	3.53	0.943
I would write a letter to a local newspaper describing my bad experience			
I would take legal action against the bank			

gested cut-off value for cronbach's alpha is 0.6 (Malhotra, 2010). Meanwhile, factor analysis method is used to analyze the validity of the items. Before the factor analysis, the suitability of the data was checked using Kaiser Mayer Olkin (KMO) of sampling adequacy and Bartlett's test of spherecity.

All the variables in this study had a cronbach's alpha (μ) higher than the threshold value of 0.6 ensuring the scale reliability. The Kaiser Mayer Olkin (KMO) for all the factors shows a number greater than the cut off value of 0.5, and the Bartlett's test of spherecity was also significant ($p = 0.000$) for all factors. These numbers indicate that the inter item correlation were sufficiently large for factor analysis to be conducted. Furthermore, all the items has a factor loadings greater than 0.5, hence, the items in this study are valid (see Table 2).

Table 4. Reliability and Validity of Constructs

Construct	Indicator	Factor Loadings	Cronbach's Alpha
Tech savvy (TS)	TS1	0.833	0.765
	TS2	0.907	
	TS3	0.729	
Heavily influenced by peers (HIBP)	HIBP1	0.842	0.840
	HIBP2	0.661	
	HIBP3	0.887	
	HIBP4	0.881	
Low trust in brand (LTIB)	LTIB1	0.878	0.910
	LTIB2	0.910	
	LTIB3	0.907	
	LTIB4	0.857	
Prolific use of social media (PUSM)	PUSM1	0.912	0.868
	PUSM2	0.936	
	PUSM3	0.849	
Desire to engage in social media (DESN)	DESN1	0.922	0.911
	DESN2	0.952	
	DESN3	0.896	
Complaint behavior intentions			
Dimension 1: Private responses (PR)	PR1	0.774	0.688
	PR2	0.504	
	PR3	0.838	
	PR4	0.742	
Dimension 2: Complaint responses (CR)	CR1	0.747	0.696
	CR2	0.832	
	CR3	0.794	
Dimension 3: Third-party responses (TR)	TR1	0.865	0.862
	TR2	0.905	
	TR3	0.887	
Repurchase	REP1	0.783	0.764
	REP2	0.799	
	REP3	0.889	

2. Hypotheses testing and discussion

To test the hypotheses, multiple regression analysis was performed. The regression models predict the effect of Generation Y consumers' tech savvines (TS), being heavily influenced by their peers (HIBP), low trust in brand (LTIB), prolific use of social media (PUSM), and desire to engage in social network (DESN) on likelihood to complaint (CBI) and to repurchase (REP). Table 5 and 6 show the results of regression analysis used to assess the relationship between Generation Y's characteristics and intention to complaint.

In the first regression model (table 5), the independent variables account for 13.5% of explained variances for consumers' intention to complaint (F=2.892, p = 0.017, R^2 = 0.135). To test the hypotheses, a one-tailed critical value, which is 1.645 (μ = 5%), is used. The results show that characteristics of tech savvy and desire to engage in social network contribute significantly to consumer's intention to complaint, thus, H1a (t = 1.763) and H5a (t = 1.822) are accepted. Meanwhile, H2a (t = 0.947), H3a (t = 1.246), and H4a (t = -0.543) are not supported. From the beta estimates, it is observed that Generation Y's desire to engage in social network (beta = 0.282) is more strongly predict customer's intention to complaint than their tech savviness (beta = 0.166).

In the second regression model, the independent variables account for 10.4% of explained variances for consumer's intention to repurchase after service recovery. The results shown in Table 6 indicate that all hypotheses (H1b – H5b) are not supported. Gen Y characteristics' (tech savviness, heavily influenced by peers, low trust in brand, prolific use of social media, and desire to engage in social network) do not have effects towards Gen Y's repurchase intention after service recovery.

Overall, the results show different outcome from pre-

Table 5. Multiple regression analysis predicting consumer complaint intentions

Predictors	Mean	Regression Analysis			Collinearity	
		SE	t - value	Beta	TOL	VIF
Tech savvy	6.28	0.094	1.763	0.166	0.779	1.283
Heavily influenced by peers	4.71	0.093	0.947	0.088	0.803	1.245
Low trust in brand	4.84	0.088	1.246	0.109	0.898	1.114
Prolific use of social media	6.05	0.154	-0.543	-0.084	0.291	3.433
Desire to engage in social network	5.82	0.155	1.822	0.282	0.289	3.457

Notes: R2 = 0.135

Table 6. Multiple regression analysis predicting repurchase

Predictors	Regression Analysis			Collinearity	
	SE	t - value	Beta	TOL	VIF
TS	0.096	-0.286	-0.028	0.777	1.287
HIBP	0.095	1.061	0.101	0.802	1.247
LTIB	0.089	0.625	0.056	0.898	1.113
PUSM	0.159	0.642	0.102	0.285	3.504
DESN	0.159	1.222	0.195	0.285	3.508

Notes: R2 = 0.104

vious study conducted by Soares et. al. (2017). In previous study, researchers found that Generation Y's tech savviness, being heavily influenced by peers, low trust in brand, and desire to engage in social network have significant effect towards complain behavior intention and repurchase after service recovery. They found that only one characteristic, which is prolific use of social media, did not have significant effect on complain behavior intention among Generation Y consumers. Meanwhile in this study, tech savvy and desire to engage social network proved to significantly influenced consumer's intention to complain. Regarding the repurchase intention after recovery, the study did not support the notion that Generation Y tend to stay with service provider after experiencing service recovery effort. In this sense, service provider should be cautious in dealing with Generation Y's complain, since they tend to lose their trust to service provider and not wanting to repurchase the same products/services, even after service provider exhibit service recovery efforts to correct the mistakes.

The different results between similar study conducted by Soares et. al. (2017) could be attributed to: 1) different industry context (Soares et. al. (2017) conduct the study in telecommunication industry context, while this study in banking industry context) and 2) different cultural context (Soares et. al. (2017) conduct the study in Portugal—western country, while this study in Indonesia—eastern country). Prior research conducted by Ngai et. al. (2006) found that there are differences in complaint behavior between Asian and Non-Asian consumers. In their study, hotel guest's collectivist cultures (Asians) tend to "find it disturbing to voice a complaint" compared with guests from individualistic cultures (non-Asians). Furthermore, customers who are tech savvy and prone to adopt new digital technology and are engaged in social networks are more likely to complain. These results might suggest that Generation Y prefer to exert private action when they are experiencing service failure using multiple, technologically-supported communication channels. These channels are fast-developing and widely adopted, which makes it easy for Generation Y to communicate their bad experience to the people that belongs to the same community or shared the same interest with them. It is also supported by previous study which stated that Asian consumers are more likely to engage in private complaining action such as negative word-of-mouth and telling their friends/relatives about the bad experience (Ngai et. al., 2007). Therefore, although generation Y characteristics are quite similar globally, there were evidences from previous research that consumers in different cultures could demonstrate different types of complaint behavior and intentions (Ngai et. al., 2006; Huang et. al., 1996).

Ⅴ. Conclusion and implication

This study designed to gain better understanding of complaint behavior intention and repurchase intention after service recovery. The major findings from this study indicate that only partial characteristics of Generation Y, tech savvy and desire to engage in social network, explain as a precursor of Generation Y's complaint intention. Their desire to engage in social networks might suggest that they are more likely to complaint privately by telling their relatives/friends about their bad experience, online or offline. Furthermore, because they are digital native consumers, they preferably use digital communication channels which are easy to use and widely adopted by their peers, such as Whatsapp, Line, etc to voice their complaints. Consumers who do not voice their complaint directly to company are more threatening to the business, since they could decide to just stop using company's products/services or even worse, they create negative word of mouth to public in general about the company. Hence, company should encourage Generation Y to voice their complaint by making convenient and easy to access channel, ideally private channel that connects company directly with their consumers. Company could also make one site dedicated for consumers who wants to make comment (either negative or positive) to the company. By creating that kind of site, the company indirectly establish social network for their Generation Y consumers and at the same time the company will be able to control and reply directly to the comments from their customers. Furthermore, Bank should increase the awareness of consumers' complaint procedure and the channels they might use to voice their complaint, so that the consumers will not submit their complaint to third party. In conclusion, Bank should treat complaints as opportunities to learn about problems that can help firms provide better quality products and services.

Ⅵ. Limitations and future studies

The main shortcoming of this study is that the size of the sample is small (131 respondents) and not demographically represented, such as most of the respondents are in their early 20s. These could lower the reliability and generalizability of the results regarding the impact of Generation Y characteristics on complaint behavior intention. Moreover, this study only consider Generation Y characteristics as an antecedent of complaint behavior intentions, while previous research has shown that complaint behavior was influenced by other factors such as consumers' cultural values, importance of situation, level of dissatisfaction, etc.

Therefore, we believe that future research should attempt to increase the sample size of Generation Y. It will be useful to add other constructs that likely have an effect on Generation Y customers' complaint and repurchase behavior, such as cultural values since culture might also be one of the biggest predictor of how consumer in certain culture behave. It would be also interesting to investigate whether there are differences in Generation Y's complaint behavior intentions in different service industry and different cultural context. It should be noted that this study only covers consumers' intention to complaint not the real complain behavior, however, intention to behave is believed to be a representation of actual behavior. Furthermore, the study will give much more impact by incorporating the kind of complaint handling procedure preferred by Generation Y consumers.

References

Ajzen, I. (1991). The theory of planned behavior, *Organizational Behavior and Human Decision Processes*, pp. 179-211.

Bearden, W. O. & Mason, J. B. (1984), "An Investigation of Influences on Consumer Complaint Reports," Advances in Consumer Research, Thomas Kinnear, ed., Association for Consumer Research, Vol. 11, 490-495.

Blodgett, J.G. and Granbois, D.H. (1992), "Towards an integrated conceptual model of consumer complaining behavior", Journal of Consumer Satisfaction, Dissatisfaction and Complaining Behavior, Vol. 5, pp. 93-103.

Blodgett, J.G., Hill, D.J. and Tax, S.S. (1997), "The effects of distributive, procedural and interactional justice on postcomplaint behavior", Journal of Retailing, Vol. 73 No. 2, pp. 185-210.

Blodgett, J.G., Hill, D.J. and Bakir, A. (2006), "Cross-cultural complaining behavior? An alternative explanation", Journal of Consumer Satisfaction, Dissatisfaction and Complaining Behavior, Vol. 19, pp. 103-17.

Boston Consulting Group. (2012, 04 16). *The Millennial Consumer Debunking Stereotypes*. Retrieved 10 15, 2017, from https://www.bcgperspectives.com: https://www.bcgperspectives.com/content/articles/consumer_insight_marketing_millennial_consumer/#chapter1

Brady, M.K., Cronin, J.J. Jr, Fox, G.L. and Roehm, M.L. (2008), "Strategies to offset performance failures: the role of brand equity", Journal of Retailing, Vol. 84 No. 2, pp. 151-164.

Brosdahl, D. J. C. and Carpenter, J. M. (2011) "Shopping orientations of US males: A generational cohort comparison", Journal of Retailing and Consumer Services, Vol. 18 No. 6, pp. 548-554.

Camarinha-Matos, L.M. (2011), Technological Innovation for Sustainability, Springer, Costa de Caparica, available at: http://link.springer.com/content/pdf/10.1007/978-3-642-19170-1.pdf (accessed October 22, 2014).

Centre for Strategic and International Studies. (2017, 11, 02). *Ada Apa dengan Milenial? Orientasi Sosial, Ekonomi dan Politik.* Retrieved 02 18, 2018, from https://www.csis.or.id/uploaded_file/event/ada_ap a_dengan_milenial____paparan_survei_nasional_csis_mengenai_orientasi_ekonomi__sosial_dan_politik_generasi_milenial_indonesia__notulen.pdf

Crie´, D. (2001), "Un cadre conceptuel d'analyse du comportement de re´clamation", Recherche et Applications en Marketing, Vol. 16 No. 1, pp. 45-63.

Day, R.L. & Landon, E.L. (1977), "Towards a Theory of Consumer Complaining Behaviour," Consumer and Industrial Buying Behavior, A.G. Woodside, J.N. Sheth and P.D. Bennett, ed., New York: North-Holland.

DeFranco, A., Wortman, J. & Lam, T. (2002). Demographic characteristic differences in customer complaint behavior: An exploratory comparison of hotel restaurants in Hong Kong and Houston. Proceedings of the Fifth Biennial Conference Tourism in Asia: Development, Marketing, and Sustainability, Hong Kong, May 23-25, 2002, 672-681.

Eric W.T. Ngai, Vincent C.S. Heung, Y.H. Wong, Fanny K.Y. Chan, (2007) "Consumer complaint behaviour of Asians and non‐Asians about hotel services: An empirical analysis", European Journal of Marketing, Vol. 41 Issue: 11/12, pp.1375-1391.

Ernst and Young. (2016, - -). *Customer trust: without it, you're just another bank Part of a series of articles exploring key themes from EY's Global Consumer Banking Survey.* Retrieved 10 15, 2017, from http://www.ey.com/: http://www.ey.com/Publication/vwLUAssets/ey-trust-without-it-youre-just-another-bank/$FILE/ey-trust-without-it-youre-just-another-bank.pdf

Forrester (2013), " Generation Y" Leads the Way on Smartphones (industry report), New York, NY, available at: www.emarketer.com/Article/Generation-Y-Leads-Way-on-Smartphones/1009604 (accessed November 8, 2014).

Harrington, R. J. *et al.* (2012) 'Generation Y Consumers: Key Restaurant Attributes Affecting Positive and Negative Experiences', Journal of Hospitality & Tourism Research, Vol. 36 No. 4, pp. 431-449.

Heung, V. C. S. & Lam, T. (2003). Customer complaint behavior towards hotel restaurant services. International Journal of Contemporary Hospitality Management, Vol. 15 No. 5, pp. 283-289.

Huang, C.T. and Wu, S. (1996), "National character and response to unsatisfactory hotel service", International Journal of Hospitality Management, Vol. 15 No. 3, pp. 229-43.

Indonesian Statistics Bureau. (2010, - -). *Sensus Penduduk 2010*. Retrieved 10 15, 2017, from http://sp2010.bps.go.id/: http://sp2010.bps.go.id/index.php/site/tabel?tid=336&wid=0

Keng, K.A., Richmond, D., and Han, S. (1995) "Determinants of Consumer Complaint Behaviour", Journal of International Consumer Marketing, Vol. 8 No. 2, pp. 59-76.

Lam, T. & Tang, V. (2003). Recognizing demographic characteristic differences in customer complaint beha- vior: The case of Hong Kong hotels restaurants. Journal of Travel and Tourism Marketing, Vol. 14 No. 1, pp. 69-86.

Leggett, K. (2013), Understand Communication Channel Needs to Craft Your Customer Service Strategy (industry report), Forrester, New York, NY.

Liu, R.R. and McClure, P. (2001), "Recognizing cross-cultural differences in consumer complaint behavior and intentions: an empirical examination", Journal of Consumer Marketing, Vol. 18 No. 1, pp. 54-74.

Malhotra, N. K. (2010) *Marketing Research: An Applied Orientation*, *Pearson*.

Meng, L., 2010. Exploration of Chinese consumer complaint behaviour in the hospitality industry. International Journal of Business and Social Science, Vol. 12 No. 9, pp. 42-48.

Muskat, M., Muskat, B., Zehrer, A. and Johns, R. (2013), "Generation Y: evaluating services experiences through mobile ethnography", Tourism Review, Vol. 68 No. 3, pp. 55-71.

Nabhani, A. (2017, 01 24). *Keluhan Layanan Perbankan Mendominasi di 2016*. Retrieved 10 15, 2017, from http://www.neraca.co.id/: http://www.neraca.co.id/article/80229/keluhan-layanan-perbankan-mendominasi-di-2016

Ndubisi, N. O. and Ling, T. Y. (2006) 'Complaint behaviour of Malaysian consumers', *Management Research News*, 29(1/2), pp. 65-76. doi: 10.1108/01409170610645457.

Ngai, E. W. T. *et al.* (2007) 'Consumer complaint behaviour of Asians and non-Asians about hotel services: an empirical analysis', European Journal of Marketing, 4112(1), pp. 1375-1391.

Nusair, K., Bilgihan, A. and Okumus, F. (2013), "The role of online social network travel websites in creating social interaction for Gen Y travelers", International Journal of Tourism Research, Vol. 15 No. 5, pp. 458-472.

Obercam, S. (2013), "Gen Y: they're broke & may not trust people or institutions, but they haven't thrown in the towel.. yet", Clutch Magazine, March, 3, pp. 1-3, available at: www.clutchmagonline.com/2014/0 3/millennials-may-trust-people-institutions-havent-thrown-in-the-towel/ (accessed November 8, 2014).

Pasquarelli, A. (2017, 08 21). *Marketers' Milennial Dilemma*. Retrieved 10 15, 2017, from www.adage.com: http://adage.com/article/news/millennials/310152/

Prensky, M. (2001) 'Digital Natives,Digital Immigrants Part 1', *On the Horizon*, 9, pp. 1-6.

Roschk, H., Müller, J. and Gelbrich, K. (2013), "Age matters: how developmental stages of adulthood affect customer reaction to complaint handling efforts", Journal of Retailing and Consumer Services, Vol. 20 No. 2, pp. 154-164.

Savage, S., Collins-Mayo, S., Mayo, B. and Cray, G. (2011), Making Sense of Generation Y: The World View of 15-25 Year Olds, Church House Publishing, London, available at: http://books.google.com/ books?hl=en&lr=&id=ps0w5etXBTMC&oi=fnd&pg=PR7&dq=generation+Y+emotion&ots= U11AbyufzI&sig=mI7i2xbq_X9CF7k9sJeRBvVSlXI (accessed November 8, 2014).

Singh, J. (1988), "Consumer complaint intentions and behavior: definitional and taxonomical issues", Journal of Marketing, Vol. 52 No. 1, pp. 93-107.

Singh, J. (1990), "Voice, exit and negative word-of-mouth behaviors: an investigation across three service categories", Journal of the Academy of Marketing Science, Vol. 18 No. 1, pp. 1-15.

Singh, J. and Pandya, S. (1991), "Exploring the effects of consumers' dissatisfaction level on complaint behaviours", European Journal of Marketing, Vol. 25 No. 9, pp. 7-21.

Singh, J. and Widing II, R.E. (1991), ''What occurs once consumers complain? a theoretical model for understanding satisfaction/dissatisfaction outcomes of complaint responses'', European Journal of Marketing, Vol. 25 No. 5, pp. 30-46.

Soares, R. R., Zhang, T. T., Proenca, J.F., and Kandampully, J. K. (2017), ''Why are Generation Y consumers the most likely to complain and repurchase?'', Journal of Service Management, Vol. 28 No. 3, pp. 520-540.

Sujithamrak, S., & Lam, T. (2005). Relationship between customer complaint behavior and demographic characteristics: A study of hotel restaurants' patrons. Asia Pacific Journal of Tourism Research, Vol. 10 No. 3, pp. 289-307.

Varela, J.A. (1992), "Satisfaccio´n/insatisfaccio´ n de los consumidores y comportamientos postconsumo derivados", Estudios sobre Consumo, Vol. 23, pp. 65-78.

Velázquez *et al.* (2010), 'Causes for complaining behaviour intentions: the moderator effect of previous customer experience of the restaurant', Journal of Services Marketing, Vol. 24 No. 7, pp. 532-545.

Zhang, T. (Christina), Abound Omran, B. and Cobanoglu, C. (2017) 'Generation Y's positive and negative eWOM: use of social media and mobile technology', International Journal of Contemporary Hospitality Management, 29(2), pp. 732-761.

Warland, R. H., Herrman, R. O., and Willits, J. (1975), "Dissatisfied Consumer: Who Gets Upset & Who Takes Action", Journal of Consumer Affair, Vol. 6, pp. 148-168.

Received/ 2017. 05. 31
Revised/ 2017. 07. 02
Accepted/ 2017. 07. 05

The International Review of Financial Consumers, Volume.2 Issue.2(Oct., 2017), 49-56 pISSN 2508-3155 eISSN 2508-464X
https://doi.org/10.36544/irfc.2017.1-2.4

The International Review of Financial Consumers

www.eirfc.com

The Willingness to Invest Under The New Compensation Limit of Investor Protection Fund in Capital Market: Evidence from Indonesia

Wardatul Adawiyah†

A B S T R A C T

This paper aims to see the willingness of people, both existing investor and non-investor, to invest their money in capital market after the new regulation about new compensation limit of investor protection fund. Moderated regression analysis is used to analyze the willingness to invest in existing investors and non-investors. The data are from a field survey of 110 respondents. The regression result shows that the expenditure and education level of existing investor is negatively and significantly associated with the willingness to invest under the new compensation limit of investor protection fund in capital market, contrary to our initial hypothesis. As well as existing investor side, the expenditure variable of non-investor has statistically significant negative effect on the non-investor willingness to invest. Confirming this study initial hypothesis, education level of non-investor has positive effect on the non-investor willingness to invest but the effect is not statistically significant.

Keywords: willingness to invest, Investor Protection, New compensation limit of investor protection fund

Ⅰ. Introduction

Capital market plays an important role in economic growth for every country in the world including Indonesia. It can enhance the function of financial intermediaries between excess and demand of fund apart from banking industry. Capital market is one of the essential elements and benchmarks of the country's economy (Karami, 2015). Capital market, especially stock markets perform many important functions. It performs an "act of magic" which is individuals provide funds to be invested in the long-term investment and many of whom wish to be able to withdraw it at will (Baumol, 1960; El-Wassal, 2013). A determinant of the decision to invest in capital market especially in the stock market is an assessment of the risk-return trade off given the existing data. Beside that, the other important factor in the decision to invest in capital market is investor trust. Many people, especially people unfamiliar with finance, need to have trust in the fairness of the game and in the reliability of the numbers to invest in it (Guiso, et.al, 2008). Investors' trust can be realized if they feel secure to do transaction in the capital market because there is a protection fund for their funds in capital market (Suharjo, 2011). Moreover, investors in good investor protection countries are willing to provide more funds to finance firms that could reduce the cost of capital and increase firm valuation (Cheng & Shiu, 2007). Several researches were conducted within the period of 2010 – 2012 in the preparation for the establishment of Investor Protection Fund in Indonesia. Finally, PT. Penyelenggara Program Perlindungan Investor Efek Indonesia (PPPIEI or ISIPF) was drawn up by the Notary as the company that administers Investor Protection Fund program at the end of 2012 and started to enforce institutions to implement

† University of Indonesia
adawiyah@ui.ac.id

on early 2014. In the beginning of implementation, the maximum compensation fund is Rp25 million per investor. However, after August 2015, the government increased the compensation limit of investor protection fund from Rp25 million per investor to Rp100 million per investor. This study aims to see the willingness of people, both existing investor and non-investor, to invest their money in capital market after the new regulation about new compensation limit of investor protection fund.

II. Literature Review

This section explained about investor protection fund, regulation of investor protection fund in Indonesia and come countries, and previous studies related to willingness to invest in capital market.

A. Investor Protection Fund

Investor protection fund is a fund created by institution to provide protection for capital market investor who lost their fund or stocks because of fraud conducted by the brokerage management to whom they are dealing with (ISIPF, 2017).

Considering the importance of investor protection fund in capital market, several countries already established institution for protecting investor fund. Table below describes about investor protection fund in some countries:

B. Indonesia Securities Investor Protection Fund (SIPF)

Considering the importance of investor protection fund makes government in this case Financial Services Authority (OJK) launches Indonesia Securities Investor Protection Fund (DPP). It aims to provide trust of investor, so they will keep their investment in capital market. After conducted several researches related to investor protection fund and comparison studies to other countries, Indonesia established new institution for the Investor Protection Fund on September 23, 2012, called as PT Penyelenggara Program Perlindungan Investor Efek Indonesia (PPPIEI or ISIPF). ISIPF was set up as a subsidiary of three Self-Regulatory Organizations (BEI, KSEI and KPEI) with the same portion of paid in capital.

Table 1. Investor Protection Fund in Some Countries

Country	*Institution*	*Year*	*Coverage*
Canada	Canada Investor Protection Fund	1969	$1 million
United States	Securities Investor Protection Corporation	1970	$500,000
Australia	National Guarantee Fund by Securities Exchanges Guarantee Corporation Limited (SEGC)	1987	No maximum for individual
South Korea	Korea Deposit Insurance Corporation	1996	KRW50,000
Malaysia	Compensation Fund of Bursa Securities	1997	RM100,000
Japan	Japan Investor Protection Fund	1998 (1968)	JPY10 million
Russia	Investor Protection Association	1999	na
Hong Kong	Investor Compensation Fund by Investor Compensation Company	2003	HK$150,000
Singapore	(Securities Exchange) Fidelity Funds	2001	SGD50,000
Thailand	Securities Investor Protection Fund	2004	THB1 million
China	China Securities Investor Protection Fund	2005	RMB100,000
Nigeria	Investor Protection Fund by Nigerian Stock Exchange (NSE)	2007	na
Indonesia	Indonesia Securities Investor Protection Fund	2012	IDR 100 million
Europe	Investor Protection	Na	
India	Investor Protection Fund	Na	

Source: Rokhim, 2017

C. Willingness to invest and Investor protection fund

There are several empirical studies conducted to examine the implementation of investor protection. Rokhim, et.al (2017) found that that increasing coverage value of SIPF in Indonesia capital market in August 2015 does not have any effect on market return because investors do not perceive that the new coverage value is worth enough to be considered. Moreover, changes of sign before and after the new coverage on the market return when the types of investors are traded among their types. There is a shift to positive sign as for the after implementation of new coverage, although it is statistically insignificant, implying that there is a shift of perception from the investors regarding the new regulation.

McLean, et.al (2012) stated that if there is a law related to investor protection fund, it would encourage efficient investment, increase the accuracy of share price in the market and better access to get external financing. Still in the same year, Haw, et.al (2012) stated that stock price in the market will be more informative if there are strong investor protection, higher financial disclosure, quality earning, and information dissemination.

Chiou, et.al (2010) stated that countries with strong investor rights protection tend to have lower risk and greater mean-variance efficiency. It is also supported by Jirasakuldech, et. al (2010) who argue that large market in countries with low disclosure and investor protection rights tend to decline more frequently, which then causing higher level of stock market volatility.

Cyrus, et.al (2006) found that strong investor protection is conducive to global financial integration. As countries improve their creditor and shareholder rights and foreign investors learn of these institutional changes, financial openness may well reach the levels observed in the early 20th century.

Ⅲ. Data, Research Methodology, and Hypotheses

Data were collected through questionnaires with individual investors and non-investors in the regions of JABODETABEK (Jakarta, Bogor, Depok, Tangerang and Bekasi). From now on, "investor" will refer to person who invested their money and "non-investor" will refer to person who not invested their money in any financial and non-financial instruments. Respondents were selected by simple random sampling. The number of the respondents was 110 respondents.

Investor and non-investor will have different questions. The respondents were asked to fill a two-part questionnaire. All respondents will have same question in the first section. The first section consist of the respondent's demographic profile as well as organizational and economic data (gender, monthly expenditure, age, level of education and occupation).

A separated question probed the possibility that the investor know about Securities Investor Protection Fund (SIPF). Based on their answers, the respondents will be asked whether they know that SIPF increased the investor protection fund with the maximum compensation limit of Rp100 million per investor or Rp50 billion per custodian. Later, the investor will be asked whether he/she would increase the investment after the increasing of maximum compensation limit. Due to data limitation, the study intentionally chose to measure the willingness to invest instead of the actual investment. Based on their answers, the respondents were categorized as either "willing to invest" or "unwilling to invest".

The second section of questionnaire for non-investor probed the possibility that they will have willingness to invest in capital market if their investment fund were protected by investor protection fund. Same as in the investor's questionnaire part, the respondents were categorized as either "willing to invest" or "unwilling to invest".

Identification, operationalization definition and research variable measurements are explain as the following:

a. Dependent variable: The willingness to invest. The willingness to invest refers to the willingness of investor to increase their investment and/or the willingness of non-investor to start their investment.
b. Independent variable: Expenditure and Level of education. Expenditure variable is a variable to know about respondent expenditure every month. This variable is used to disguise the direct question about income, where many respondents reluctant to answer it. Expenditure variable uses interval scale with five scales. Level of education refers to level of their past formal education.
c. Moderate Variable: Knowledge about the new max-

imum compensation limit issued by SIPF. It will be valued 1 if they know and 2 if they don't know.

The study uses Moderated Analysis Regression (MRA). MRA is type of regression-based technique used to identify the moderator variable. Before applying regression, the validity and reliability test should be done. Validity is a degree in which the research test is truly measuring what supposed to measure. While, reliability is a measure to indicate whether the instruments reliable or not to be used as a means of collecting data. There are some testing should be done to get the best estimation for linear regression, one of them is testing classical assumptions i.e. normality, heteroscedasticity and multicolinearity.

The study will divide the sample of data analysis into two classifications, the first one is investor and the other is non-investor.

The independent variables for MRA model were chosen based on the existing literature, which led to the formulation of hypotheses.

Hypothesis 1: willingness to invest varies with respondents' demographic characteristics. Demographic in this study is education (Kontogeorgos, 2014). Education is expected to have a positive effect on willingness to invest.

Hypothesis 2: willingness to invest varies with respondents' income. Expenditure is considered as a proxy for income of respondents, because higher expenditure may have higher incomes. Thus, respondents with higher income are expected to be more willing to invest their money. Moreover, Atkinson stated that the pattern of financial asset ownership affects income status. It has been observed on his article that for the higher income groups a greater proportion of the amount of asset holdings is in high-paying corporate equities than for the low income groups, who tend to favor direct debt and deposit types of claims, assets which in good times tend to be less remunerative than corporate stocks (Atkinson, 1956).

Hypothesis 3: willingness to invest under the new compensation limit of investor protection fund in capital market. The increasing of new compensation limit of investor protection fund in capital market is considered as a proxy for safeness. Safety is also one of the essential and crucial elements of investment. Investors prefer to place their fund on a safe territory (Burke, 2009). Thus, the investor is expected to increase or start their investment in capital market if they know the investor protection fund is increase.

Research model consist of three models. Model 1 and 2 are used for investor measurement. While, non-investor measurement will use model 3.

Model 1:

$$\begin{aligned} Willingness &= \alpha + \ \beta_1 \mathrm{Exp} + \beta_2 \\ &\neq wlimit + \beta_3 \mathrm{Exp}^* \\ &\neq wlimit + \epsilon \end{aligned} \tag{1}$$

Where,

Exp = expenditure of respondents

Newlimit = the level of knowledge from investor whether they know that Indonesia SIPF increase the maximum compensation limit

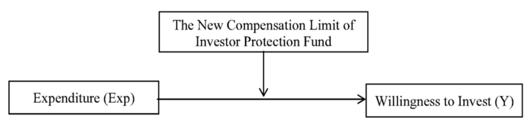
β_1 = coefficient of Expenditure variable

β_2 = coefficient of Newlimit variable

β_3 = coefficient of Exp*Newlimit variable

ε = error of regression

Research design for model 1 is shown in the figure below:



Source: author, 2017

Model 2:

$$\begin{aligned} Willingness &= \alpha + \ \beta_1 Edu + \beta_2 \\ &\neq wlimit + \beta_3 Edu^* \\ &\neq wlimit + \epsilon \end{aligned} \tag{2}$$

Where,

Edu = level of education of respondents

Newlimit = the level of knowledge from investor whether they know that Indonesia SIPF increase the maximum compensation limit

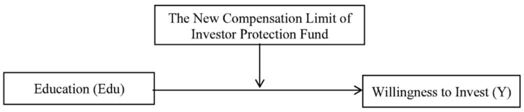
β_1 = coefficient of Education variable

β_2 = coefficient of Newlimit variable

β_3 = coefficient of Edu*Newlimit variable

ε = error of regression

Research design for model 2 is shown as the following figure:



Source: author, 2017

Model 3:

$$Willingness = \alpha + \beta_1 Edu + \beta_2 \mathrm{Exp} + \epsilon \qquad (2)$$

Where,

Edu = level of education of respondents

Exp = expenditure of respondents

β_1 = coefficient of Education variable

β_2 = coefficient of expenditure variable

ε = error of regression

Figures below show that there is 108 respondents that consist of 37 respondents are investor in capital market, 17 respondents are investor in non-capital market and 56 respondents are non-investors either in capital market or any other instruments.

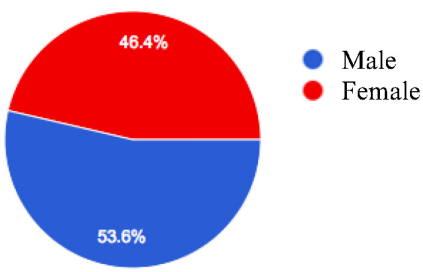


Figure 1. Gender of Respondents

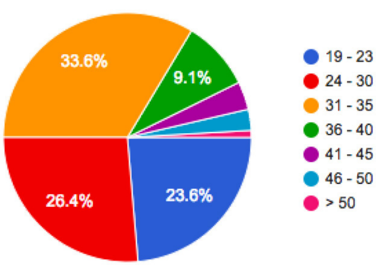


Figure 2. Age of Respondents

The percentage of male respondents is slightly above the percentage of female respondents (53.6% male vs 46.4% female) (figure 1). Half of respondents are under the age of 30. The percentage of respondent in the age of 31-35 is about 33.6%, 9.1% of respondents is in the age of 36-40, and the rest of percentage is respondents above 40 years old (figure 2).

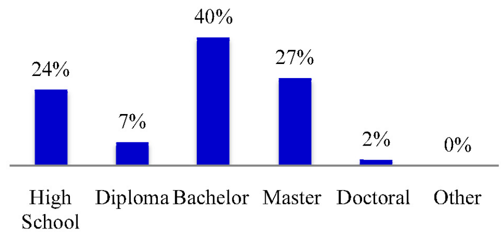


Figure 3. Level of Education

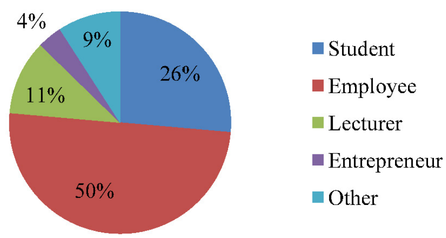


Figure 4. Occupation

About 31% of respondents have education under bachelor degree. More than third have bachelor degree (40%). 27% respondents are master degree. Only 2% advanced through doctoral degree (figure 3). Half of respondents are employee. 26% respondents are student, and about 24% of respondents are lecturer, entrepreneurs and other.

Ⅳ. Empirical Result

Most of independent variables for the moderated regression analysis of the willingness to invest are provided directly by the question in the survey. The first regression is to know about relationship between expenditure of respondents as a proxy of income respondents and also the willingness to invest in capital market. The relationship also wants to know how strong the willingness of investor to invest their money in capital market after new compensation limit in investor protection fund.

Table 2. F-Statistic Test Model 1

Model Summary (Willingness)

R	R Square	Adjusted R Square	Std. Error of the Estimate
.70	.50	.45	.21

ANOVA (Willingness)

	Sum of Squares	df	Mean Square	F	Sig.
Regression	1.37	3	.46	10.86	.000
Residual	1.39	33	.04		
Total	2.76	36			

Source: author, 2017

Adjusted R-square is 0.45. It shows that only 45% of willingness to invest under new compensation limit of investor protection fund in capital market can be explained by expenditure. However, about 55% of dependent variable is explained by other variables outside the model.

ANOVA table in table above shows that F-value is 10.86 at the significant level of 0.000. The significant level is lower than 0.05, which means that expenditure and new maximum compensation limit variable is simultaneously affect willingness to invest variable.

Table 3. Regression Result Model 1

Coefficients (Willingness)

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	3.27	.39	.00	8.47	.000
Expenditure	-.73	.13	-2.89	-5.51	.000
CE	.38	.07	3.28	5.26	.000
NewLimit	-1.17	.21	-2.07	-5.46	.000

Source: author, 2017

Based on table above, the regression shows that the variable of expenditure has the significant level below 0.05 and coefficient regression negative 0.73. It means that expenditure has significantly negative relationship with the willingness to invest in the capital market and reject H_1. Interaction test for variable Newlimit (CE) as moderator variable shows significant level about 0.00. This value is lower than 0.05, thus it should accept H_3. It means that new maximum compensation limit is a moderator variable and it is stronger the relationship between expenditure and the willingness to invest.

Test for hypothesis 1 shows that expenditure has negative relationship with the willingness to invest, which means that investor with lower expenditure will be more eager to invest in capital market.

Table 4. F-Statistic Test Model 2

Model Summary (Willingness)

R	R Square	Adjusted R Square	Std. Error of the Estimate
.72	.52	.47	.20

ANOVA (Willingness)

	Sum of Squares	df	Mean Square	F	Sig.
Regression	1.42	3	.47	11.72	.000
Residual	1.33	33	.04		
Total	2.76	36			

Source: author, 2017

Adjusted R-square is 0.47. It shows that only 47% of willingness to invest under new compensation limit of investor protection fund in capital market can be explained by level of education of respondents. However, about 53% of dependent variable is explained by other variables outside the model.

ANOVA table in table above shows that F-value is 11.72 at the significant level of 0.000. The significant level is lower than 0.05, which means that level of education and new maximum compensation limit variable is simultaneously affect willingness to invest variable.

Table 5. Regression Result Model 2

Coefficients (Willingness)

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	3.86	.49	.00	7.90	.000
Level_of_education	-.77	.14	-2.64	-5.57	.000
NewLimit	-1.62	.27	-2.87	-5.92	.000
DE	.45	.08	3.41	5.75	.000

Source: author, 2017

Based on table above, the regression shows that the level of education variable has the significant level below 0.05 and coefficient regression negative 0.77. It means that expenditure has significantly negative relationship with the willingness to invest in the capital market and reject H_2. Interaction test for variable Newlimit (DE) as moderator variable shows significant level about 0.000. This value is lower than 0.05, thus it should accept H_3. It means that new maximum compensation limit is a moderator variable and it is stronger the relationship between level of education and the willingness to invest.

Test for hypothesis 2 shows that level of education has negative relationship with the willingness to invest, which means that investor with lower level of education will be more eager to invest in capital market. The result shows different result from Kontogoergos et.al (2014), which state that education is expected to have a positive effect on willingness to invest. Depth analysis about characteristic of respondent show that the respondents in lower level of education is mostly students with the age between 19 and 23 years old.

Table 6. F-Statistic Test Model 3

Model Summary (Willingness)

R	R Square	Adjusted R Square	Std. Error of the Estimate
.44	.19	.14	.46

ANOVA (Willingness)

	Sum of Squares	df	Mean Square	F	Sig.
Regression	1.69	2	.85	3.99	.028
Residual	7.22	34	.21		
Total	8.92	36			

Source: author, 2017

For non-investor measurement, adjusted R-square is 0.14. It shows that only 14% of willingness to invest under new compensation limit of investor protection fund in capital market can be explained by expenditure and level of education. However, about 86% of dependent variable is explained by other variables outside the model.

ANOVA table in table above shows that F-value is 3.99 at the significant level of 0.028. The significant level is lower than 0.05, which means that expenditure and level of education variable is simultaneously affect willingness to invest variable.

Table 7. Regression Result Model 3

Coefficients (Willingness)

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	1.46	.42	.00	3.44	.002
Edu	-.10	.06	-.30	-1.80	.081
Exp	.13	.10	.22	1.35	.186

Source: author, 2017

Based on table above, the regression shows that the level of education variable has the significant level below 0.10 and coefficient regression negative 0.10. It means that level of education has significantly negative relationship with the willingness to invest in the capital market and reject H_1. While, expenditure variable has significant level 0.186. This value is higher than 0.05. Coefficient regression for expenditure variable is positive 0.13, means that expenditure has positive relationship with the willingness to invest in capital market, but this relationship is not significant. Expenditure variable is a proxy to measure respondents' income. Respondents may have high income if they have high expenditure.

Same as with result from investor, non-investor also shows that level of education has negative relationship with the willingness to invest, which means that investor with lower level of education will be more eager to invest in capital market. The result shows different result from Kontogoergos et.al (2014), which state that education is expected to have a positive effect on willingness to invest. Depth analysis about characteristic of respondent show that the respondents in lower level of education is mostly students with the age between 19 and 23 years old. Their knowledge about investment gives significant contribution to their willingness to invest in capital market. But, the interest finding shows in regression result of non-investor side for expenditure variable. The regression shows positive relationship between expenditure variable and the willingness to invest, even though its relationship is insignificant. The positive relationship means that the more expenditure of respondents, the more they will invest in capital market. This result is supported by study from Shum and Faig (2005) who stated that the willingness to invest in capital market is increasing when respondents have higher income. It is because the sensitivity of income to risk in capital market is decreasing. The higher income individual will tend to invest more in risky investment (Benzoni and Chyruk, 2005).

Ⅴ. Summary

The objective of this study was to see the willingness of people, both existing investor and non-investor, to invest their money in capital market after the new regulation about new compensation limit of investor protection fund. This was the question in this survey addressed to 110 respondents in Jabodetabek (Jakarta, Bogor, Depok, Tangerang and Bekasi). Moderated Regression Analysis (MRA) has been applied to identify the willingness to invest under new maximum compensation limit. The expenditure and education level of existing investor is negatively and significantly associated with the willingness to invest, contrary to our initial hypothesis. As well as existing investor side, the expenditure variable of non-investor has statistically significant negative effect on the non-investor willingness to invest. Confirming this study initial hypothesis, education level of non-investor has positive effect on the non-investor willingness to invest but the effect is not statistically significant.

References

Baumol, J.W. (1960), The Stock Market and Economic Efficiency. New York: Furham University Press

Benzoni, L., Olena Chyruk. 2009. Investing over the life cycle with long-run labor income risk. Federal Reserve Bank of Chicago. *Economic Perspectives Journal*, 29-43.

Burke, John JA. (2009), Re-examining investor protection in Europe and the US. eLaw Journal: *Murdoch*

University Electronic Journal of Law, 16 (2).

Cheng, S.-R., & Shiu, C.-Y. (2007). Investor protection and capital structure: International evidence. *Journal of Multinational Financial Management*, *17*(1), 30-44. https://doi.org/10.1016/j.mulfin.2006.03.002

El-Wassal, K. A. (2013). The Development of Stock Markets : In Search of a Theory. *International Journal of Economics and Financial Issues*, *3*(3), 606-624. https://doi.org/http://www.econjournals.com/index.php/ijefi/article/view/489

Guiso, L., Sapienza, P., & Zingales, L. (2008). Trusting the stock market. *Journal of Finance*, *63*(6), 2557-2600. https://doi.org/10.1111/j.1540-6261.2008.01408.x

Haw, I., Hu, B., Lee, J. and Wu, W. (2012), Investor protection and price informativeness about future earnings: international evidence. Rev Account Stud, 17(2), pp. 389-419.

Jirasakuldech, B., Dudney, D., Zorn, T. and Geppert, J. (2010), Financial disclosure, investor protection and stock market behavior: an international comparison. *Review of Quantitative Finance and Accounting*, 37(2), pp. 181-205.

Karami, Adiya Rizki. (2015). The Establishment of Indonesian Securities Investor Protection Fund Related To The Supreme Court Decision No. 535.K/Pid/2013 About The Case of PT Sarijaya Permana Securities. *Jurnal Problematika Hukum*, Vol 1, No, 1, Agustus 2015, 51-56

Kontogeorgos, Achilleas, Fotios Chatzitheodoridis, and George Theodossiou. (2014). Willingness to Invest in Agricultural Cooperatives: Evidence from Greece. Journal of Rural Cooperation, 42(2), pp. 122-138.

Rokhim, Rofikoh., Nur Dhani Hendrastiti and Nevya Wulandary. (2017). Investor Protection Fund and Trading Behavior: Evidence from Indonesia. *International Journal of Applied Business and Economic Research*, 15(5), pp. 47-58.

Shum, P., Faig M. 2005. What Explains Households Stock Holdings? *Journal of Banking and Finance*, 30. Available from: URL: http:/ www.Proquest.com

Suharjo, Farid Ghazi. (2011). Feasibility Study Lembaga Investor Protection Fund dan Implementasi di Indonesia. *Tesis MM FEB UI*. pp.1-2x

Received/ 2017. 05. 31
Revised/ 2017. 07. 02
Accepted/ 2017. 07. 05

Editorial Principles

1. Mission

The International Review of Financial Consumers (IRFC) aims to offer a communication platform for scholars, regulators, and practitioners to share their latest academic research on financial consumers and related public policy issues in both advanced economies and emerging market countries. All theoretical, empirical, and policy papers of relevancy are welcome, with the following as the topics to cover:

① protection for financial consumers
② business ethics of financial institutions
③ market discipline of financial industries
④ corporate social responsibility of financial institutions
⑤ renovation or innovation of law and regulations related to financial consumption
⑥ public policies for financial consumption
⑦ fair trading of financial products
⑧ dispute resolution for financial consumption
⑨ case studies of best practices for financial consumption
⑩ international comparison on any of the above topics

2. Publication schedule and contents

IRFC, the affiliated journal of the International Academy of Financial Consumers (IAFICO), will be published twice a year – April and October each year - and will pursue to be the first international academic journal focusing on the research related to financial consumers. As the contribution of financial consumption becomes increasingly important to the national economy for most countries, how to maintain an efficient and equitable financial market is an imminent issue for research. The trend of globalization and liberalization policies has reinforced the challenges in financial markets. Not only the financial instruments become more complicated and hard to understand by the public, but also the frequent changes in regulations and business practices cause confusions to the financial consumers. Consumption disputes regarding the financial products have drawn attention by the media in recent years. IRFC attempts to serve as a forum to publish and share original and innovative research, both academic and policy-oriented, on all the above issues.

3. On ethics for research

The range of research misconducts

① Misconducts related to academic research (“misconducts” hereafter) means that fabrication, falsification, plagiarism, unfair showing of papers' author, during research proposal, research performing, research report and research presentation, etc. It is as follows.

1) "Fabrication" is the intentional misrepresentation of research results by making up data or research result.

2) "Falsification" is the distortion of research contents or results by manipulating research materials, equipment and processes, or changing or omitting data or results.

3) "Plagiarism" is the appropriation of another person's ideas, processes or results, without giving appropriate approval or quotation.

4) "Self-plagiarism" is the reusing a large portion of their own previously written research.

5) "Unfair showing of papers' author" is not qualifying people, who have been contributing to research contents or results scientifically, industrially and politically, as an author without just reason, or qualifying people, who have not been contributing the same, as an author with an expression of thanks or respectful treatment.

6) Obstructing investigation about misconducts of their own or others, or harming an informant.

7) Action which is out range of usually acceptable in the course of the research.

8) Action which is suggestion, pressure or threat to others to do the above things.

4. On plagiarism

Types of plagiarism

Following two forms are defined the representative action of research misconducts (Plagiarism).

① Using the original author's idea, logic, unique terms, data, system of analysis without indicate the source.

② Indicating the source but copying the original paper's words, idea, data and so on without quotation marks.

Bylaws of the International Academy of Financial Consumers (IAFICO)

March 31, 2015
April 19, 2016

Section 1 General Provisions

Article 1 (Official Name)

The official name of this academic society shall be the "International Academy of Financial Consumers (IAFICO hereafter)".

Article 2 (Registered office and Branch offices)

The registered office is to be in Seoul, South Korea. Branch offices may be established in provincial cities in South Korea or overseas should the need arise.

Section 2 Objectives and Undertakings

Article 3 (Objectives)

* *Pending*

The IAFICO is a non-profit association aiming at promoting and developing at an international level collaboration among its members for the study of various issues relating to financial consumers, including its education, legislation, creation of best practices, supervision and policy advancement to contribute to the development of the global economy and financial market, through investigation or research into financial consumers, and other academic activities.

Article 4 (Undertakings)

The following activities shall be carried out in order to achieve the objectives of the IAFICO.
1. Publication of journal and other literature
2. Hosting of academic conferences
3. Additional undertakings corresponding to the objectives of the academic society which are deemed necessary at the board of directors meeting or the general meeting

Section 3 Membership

Article 5 (Requirements and Categories)

The IAFICO shall have following categories of membership :

① Individual member
Individual members are categorized further into a regular member or and associate member.

1. Regular member shall be a specialist in the area such as finance, consumer studies, economics, management, law, or a specialist in the area such as finance, consumer studies, economics, management, law, or education etc, and must be a full-time instructor at a domestic or overseas university, an researcher at a research institute with equivalent experience, or should hole equal credentials to those mentioned previously, and shall become its member by the approval of the board of directors. Regular members attend general meetings and may participate in discussions, hold the right to vote, and are eligible to be elected a director or other status of the IAFICO.
2. Associate members shall be divided into either a student member, who is a current domestic or overseas graduate school student, or an ordinary member, who works for a financial institution or a related organization. Associate members do not hold the right to vote and not eligible to be elected to a director or other status of IAFICO.
3. Both regular member and associate member must pay the membership fee to the IAFICO every year.
4. In the case that a decision is made by the Board of Directors to expel a member due to a violation of the objective of the society, or demeaning the society, or in the case that a member fails to pay the membership fees for two years continuously without prior notice, their membership shall be revoked.

② Institutional member
1. Institutional member
Shall be organizations related to financial consumers who do not damage the impartiality of the IAFICO subject to approval of the Board of Directors Institutional members do not hold the right to vote and are not eligible for election.
2. Institutional member must pay its membership fee to the IAFICO every year.

Section 4 Organization

Article 6 (Designation of Board of Director)

The following Directors are designated to constitute the Board Directors to run the IAFICO.
1. Chairperson
2. Vice-Chairperson
3. President
4. Vice-President
5. Ordinary Directors
6. Auditor

Article 7 (Election of Board Members and Director)

① The Chairperson, Directors, and Auditors shall be elected or dismissed at the general meeting.
② Appointment of the Directors may be entrusted to the Chairperson pursuant to the resolution of the general meeting.
③ The Vice-Chairperson, President, and Vice-President shall be appointed and dismissed by the Board of Directors.

Article 8 (General Meetings)

① General meeting shall decide following matters relating to the activities of the IAFICO.
1. Amendments to the Bylaws
2. Approval of the budget and settlement of accounts
3. Election or Dismissal of the Chairman
4. Election or dismissal of Auditors
5. Regulations concerning the duty and right of members
6. Resolutions regarding items submitted by the President or Board of Directors
7. Other important matters

② The Chairperson must call a regular general meeting at least once a year and report on the undertakings of the IAFICO. Provisional general meetings may also be held by the call of the Chairperson, or at the request of at least a quarter of current regular members, or according to the resolution of the Board of Directors.
③ At a general meeting, a quorum is formed by one third of regular members. However, regular members who are not able to participate in the general meeting in person may be represented by proxy, by entrusting a specific regular member attending the general meeting with their attendance or voting right. In this case the letter of proxy is included in the number of attendees.
④ Resolutions at the general meeting will be made according to the majority vote of the attending members who hold the right to vote.
⑤ In principle, the general meetings shall be held with face-to-face meeting, however, it may be held web-based meeting when needed.

Article 9 (Auditors)

① The auditors shall audit financial affairs, accounts and other transactions of IAFICO, shall participate in, and may speak at board meeting, and must present and auditor’s report at the regular general meeting.
② There shall be two appointed auditors.
③ Auditors are elected at the general meeting.
④ And auditor shall serve a term of two years and may be reappointed.

Article 10 (Board of Directors)

① The Board of directors shall be made up of chairperson and fewer than 80 directors.
② The Board of Directors shall decide a plan of operation and establish the budget, in addition to matters on the running of IAFICO.
③ Board meeting requires a quorum of at least one third of current board members. Resolutions at the Board meeting will be made according to the majority vote of the attending members. However, board members who are not able to participate in the board meeting in person may be represented by proxy, by entrusting another specific

board member attending the board meeting with their attendance or voting right.

④ A board member shall serve a term of two years, with a possibility of serving consecutive terms.

⑤ A number of sub-committees or branches in each country or region may be set up under the Board of Directors to support the running of the IAFICO.

Article 11 (Steering Committee)

① The Board of Directors may entrust some decisions relating to the conducting of business to the Steering Committee.

② The Steering Committee shall be comprised of the Chairperson, Vice-Chairperson, President, and the heads of each subcommittee.

③ Temporary task forces may be established by the Steering Committee when necessary to run the business of the Steering Committee.

Article 12 (Chairperson)

① The Chairperson shall represent the IAFICO and chair its general meeting and board meeting.

② There shall be one appointed Chairperson who serves a term of five years.

③ In the case of an accident involving the Chairperson, the Vice-Chairperson shall complete the remaining term of office of less than one year. If it lasts longer than one year, a new Chiarperson shall be elected at the general meeting.

④ A new Chairperson should be elected at the general meeting one year prior to the end of the current Chairperson's term of office.

⑤ Should it be judged that it is difficult for the Chairperson to carry out their duty any longer, he or she may be dismissed from their post by the decision of the Board of Directors and general meeting.

Article 13 (Vice-Chairperson)

① The Vice-Chairperson shall assist the Chairperson, and serve as a member of the Board of Directors.

② The Vice-Chairperson shall serve a term of two years, or the remaining term of office of the Chairperson, whichever is shortest.

③ The Vice-Chairperson shall be elected from one of the regular members at a meeting of the Board of Directors, according to the recommendation of the Chairperson.

④ The Vice-Chairperson shall may be reappointed.

Article 14 (President)

① During its term of office, the President shall become the head of the organizing committee supervising international conferences, and serves for a term of one year. The President shall attend the board meeting as a member of the Board of Directors.

② The succeeding President shall be elected by the Board of Directors after considering their ability to organize and host the following year's conferences. The succeeding President shall also attend board meeting as a member of the Board of Directors.

③ The Board of Directors may elect the next succeeding President should the need arise. The next succeeding President shall also attend board meeting as a member of the Board of Directors.

④ The President, succeeding President, and the following President may appoint a vice-President respectively by obtaining approval of the Board of Directors.

⑤ The appointment and dismissal of the President is decided at the board meeting.

Article 15 (Vice-President)

① A Vice-President is a member of the Board Directors and shall assist the President, supervise applicable international conferences.

② A Vice-President is recommended by the President and shall be approved by the Board of Directors.

③ Multiple Vice-Presidents may be appointed.

④ A Vice-President shall serve a term of one year, the same as the term of President.

⑤ In the event of an accident involving the President, a Vice-President shall fulfill the President's duties during the remaining term of office.

Article 16 (Editorial Board)

① The Editorial Board shall be responsible for editing of journals and other materials to be published by the IAFICO.

② The head of the Editorial Board shall be appointed by the Board of Directors, and shall serve a term of office decided by the Board of Directors.

③ The head of the Editorial Board shall be a member of the Board of Directors.

④ Additional matters concerning the running of the editorial board shall be decided separately by the Board of Directors.

Article 17 (Advisory Board and Consultants)

① The Chairperson may select individuals who could make a large contribution to the development of IAFICO, and appoint them as advisors subject to the approval of the Board of Directors.

② The Chairperson may appoint consultants subject to the approval of the Board of Directors in order to receive advice relating to all business matters of the IAFICO, such as development strategies, conferences, research plans, and research projects etc.

③ Advisors and consultants shall serve terms of one year and may be reappointed.

Section 5 Financial Affairs

Article 18 (Accounting and Revenue)

① The fiscal year of the IAFICO shall run from the 1st of January to the 31st of December each year.

② The finance required to operate the IAFICO shall be sourced from membership fees, member contributions, society participation fees, and other incomes. Related matters shall be decided by the Board of Directors or the Steering Committee.

③ Should the need arise, the IAFICO may accept sponsored research, donations or financial support from external parties in order to support the business performance of the IAFICO. The Chairperson shall report the details of these at the board meeting.
④ Chairperson should report all the donation from outside and their usage of the year at the IAFICO homepage by the end of March of the next accounting year.

Section 6 Supplementary Rules

Article 19 (Revision of the Bylaws)

① Any other matters not stipulated by this Bylaws shall be resolved by the Board of Directors.
② Revision of the Bylaws shall be carried out, by the proposition of the Board of Directors, or at least one-tenth of regular members, at a general meeting where at least one-third of the total regular members are in attendance, or at a provisional general meeting, with the agreement of at least two-thirds of current members.

Article 20 (Dissolution)

Should the IAFICO intend to be dissolved, it must be decided upon at a general meeting with the agreement of at least two-thirds of current members, and permission must also be received from the Fair Trade Commission. Except for bankruptcy, the dissolution must be registered and reported to the Ministry of Strategy and Finance within three weeks, accompanied by a certified copy of register.

Article 21 (Residual Property upon Dissolution)

Should the IAFICO be dissolved, according to article 77 of the Korean civil law, all remaining assets of IAFICO shall belong to the state, local government, or other non-profit corporations carrying similar objectives.

Additional Clause

These Bylaws shall become effective from the 1st April 2016.

The International Review of Financial Consumers

Vol.2 No.2

Printed	2017. 10. 30
Published	2017. 10. 30
Publisher	Jung, Hong Joo
Editors	Cho, Man and Tsai-Jyh Chen
Publishing Institute	The International Academy of Financial Consumers
	32516 Dasan Hall of Economics, SKKU, 25-2, Sungkyunkwan-ro, Jongno-gu, Seoul, Korea
	Tel : +82 2 760 1283
	Fax : +82 2 766 0527
	E-mail : iafico@skku.edu