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Special Focus On Privacy

Privacy In Banking: Maintaining Customer Trust

By Roy W. Urrico

"Perhaps the greatest privacy concern for consumers is that, after they have ordered enough products, companies will have accumulated enough personal information to harm or take advantage of them." — Tim Berners-Lee in "Weaving the Web"

The information age, propelled by the light-speed development of data-gathering technology and Internet commerce, has kicked up quite a privacy storm with financial institutions thrust right in the midst of it. While banks need to be aware of the potential ramifications of the privacy issue, you should not shy away from it either. You need to be proactive and continue to take the lead as fiduciary institutions that consumers entrust with their financial data.

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"I am sure bankers will say 'we understand customer trust, we've always protected confidential information,'" says Anne Wallace, manager at KPMG Consulting's Financial Services Business, which works with banks on privacy and security. However there was a tendency to underestimate the scope of the privacy issue.

"Privacy took the industry by surprise for that very reason…they [banks] were caught by surprise as to what threat new technology poses in that [customer] relationship," explains Anne.

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It's Okay To Share, But Be Careful

Data warehouses, data mining and other customer-relationship management tools allow banks to better profile customers. This has permitted financial institutions — through intensive data collection and analysis — to economically generate more business opportunities and allow bank customers to see new product and services offerings, quicker help, and lower costs.

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"By allowing banks to share customer information with affiliates or third-party vendors, consumers can receive consolidated account statements of their financial activity; call a single customer service hotline to inquire about their mortgage, credit card, and investment accounts; and receive loan approvals in minutes rather than days," said Donna Tanoue, FDIC chairman at a public forum in March. "By allowing consumer information to be used for cross-marketing purposes, institutions offer consumers the benefit of customized products and services and access to discounts."

The Downside

However it is the downside that is generating headlines. "You can't do CRM without thinking through the privacy issues," stated Jo Ann Barefoot, managing director, KPMG Consulting's Financial Services Business, at Retail Delivery.

No organization wants to be part of a news story involving fraud. Such was the case of an institution that sold millions of credit card numbers to a convicted felon, who then used the information to go on a $46 million buying spree.

"The tension between the consumer's desire to keep personal information private and the desire of the financial industry to use the information in a variety of ways is at the center of an ongoing discussion on privacy," says Donna.

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New Rules On The Way

Of immediate concern to financial institutions is Title V of the Gramm Leah Bliley Act of 1999 — also known as the financial services modernization act — that places new limits on the sharing of customer data with nonaffiliates. The Act applies to all financial institutions, which essentially involves: depository institutions; broker-dealers; investment advisors and companies; insurance underwriters agencies and brokerages; nonbank credit card issuers; mortgage companies; and consumer finance organizations. Title V ordered regulators to publish implementing rules by May 12th, six months after the act was signed into law.

"...it can be an important incentive for banks and other businesses to adopt good privacy practices..."

A provision of the Gramm-Leach-Bliley Act allows consumers to opt out of certain information sharing. "This brings market discipline into play. And it can be an important incentive for banks and other businesses to adopt good privacy practices," states the FDIC chairman.

The FDIC's proposed regulation, due to be finalized next month, would require a financial institution to:

- Provide notice to customers about its privacy policies and practices.
- Describe the conditions under which a financial institution may disclose nonpublic personal information about consumers to nonaffiliated third parties.
- Provide a method for consumers to prevent the financial institution from disclosing that information to nonaffiliated third parties by "opting out" of that disclosure.

Although the new law spells out an opt-out opportunity, some privacy advocates argue that the law would be more effective with an "opt-in" provision, where consumers grant permission before personal data is used.

The proposed regulation, which is scheduled to take effect in November, was developed jointly by the FDIC, the Office of the Comptroller of the Currency, the Federal Reserve System, the Office of Thrift Supervision, the Department of the Treasury, the Securities and Exchange Commission, the National Credit Union Administration and the Federal Trade Commission. Similar regulations are being proposed by those agencies.

"It is going to be tough to implement that deadline," states Anne. "The systems and the processes that have to be changed are substantial."

You should not be waiting for the regulators to arrive. "Banks need to be thinking about the privacy policy, they need to adopt any operational changes...and to train their staff...there is a lot to do," says Charlotte Bahin, regulatory counsel for America's Community Bankers Association.

As a guideline you can use the Privacy Principles approved by the ABA, FSTC, CBS, IBAA and other banking organizations.

Public Perceptions

Regardless of what the regulations provide, the key for banks is to recognize the importance of public perception and trust. Several public opinion polls within the last year place concerns over threats to privacy in the 80-90% range. (A SYNERGISTICS Research Corp. report is on page 1259). In addition state legislators, reacting to constituents' complaints, introduced more than 1,800 consumer privacy bills in 1998. "The American public has said that privacy is among the things that matter to them most — we must listen," says Donna.

"Despite the polls, advocates, politicians and regulators, consumers themselves have not always shown a great deal of initiative toward protecting themselves."

Reps. Asa Hutchinson (R-AR) and Jim Moran (D-VA) also introduced legislation to form a national privacy commission. "Regulators have underestimated the American peoples' interest in what bank's do with their information," says Lisa S. Dean, vp/technology policy at the Free Congress Foundation, a political watchdog group. "This privacy commission is not the answer to all our prayers but it is a good attempt by congress that they are trying to do something."

Like so many issues today it is difficult to separate hyperbole from reality. Despite the polls, advocates, politicians and regulators, consumers themselves have not always shown a great deal of initiative toward protecting themselves.

Many consumers seem to have accepted that less privacy is the trade-off for more convenience and information. In many cases consumers knowingly — or naively — share personal data. "Consumers are ultimately to be blamed because they gave away the information," says Lisa.

How many customers will respond to the to opt-out provision as prescribed by the modernization act? The Fair Credit Reporting Act, for example, already contains an opt-out provision that is gathering dust with only a 3% opt-out rate.

"It will be interesting to see how many people elect to not have their information shared," states Charlotte.

Don't Lose Your Advantage

A more important issue for banks, especially community banks, is preserving their close consumer ties. "Privacy is not about compliance, it is about information fundamental to the way you do business and fundamental to that [customer] relationship," says Anne of KPMG.

"In some ways senior [bank] management underestimated the seriousness of the issue," explains Anne. She lays the blame on a disconnect between those developing the software and the risk management people. "Banks have hired techies to build Internet banking; they are technically sophisticated but they don't have the deep roots in banking and are not sensitive to these [privacy] issues."

Those roots are at the core of traditional banks' advantage in the privacy issue. "One of the strengths for community banks is their customers already have a relationship with the bank," says Charlotte. This is where you need to be aggressive and put the privacy issue on the front burner and in front of your customers. You can take advantage of the new technology without impacting your relationship by stating your privacy policies clearly and ensuring customers that data, as always, is safe.

"For consumers, the banking relationship is personal, and a banker might be chosen, in part, because he or she is trusted to maintain confidences – to protect the details of financial relationships and information," states Donna. "For many consumers, banks are special because of the trust they have in bankers."

This seems to be true even amid all of the privacy controversy. "Most of our clients say they don't get a lot of concern from consumers yet the polls consistently show a concern about security and privacy," says Anne. "It may be that the abuses that the public gets most involved with are not [pertaining to] financial institutions."

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The current importance of customer information compels you to put greater emphasis in keeping that data secure and to use it properly. "The issue of privacy itself is a threat to the bank-customer relationship only in how a bank chooses to use the information entrusted to it by the customer," says Ron Gafron, svp/cto at Glenview (IL) State Bank. "We hold our customer's information very closely, and have no plans to use it for financial gain in and of itself by selling it to third parties. We just think it's bad business and weakens the trust our customers have in us."

Other Privacy Issues

The bank modernization act only addresses some of the privacy issues. Other issues gaining lots of attention from advocacy groups and lawmakers are profiling, telemarketing, identity-theft, third-party relationships, credit scoring and screen scraping.

Screen scraping presents an interesting paradox. On one hand consumer groups are advocating for more stringent financial privacy controls while some customers are providing third-party aggregators access to their accounts. "It is really, really confusing," says Anne. "Here you are concerned about posting a privacy policy and the consumer allows a third-party access to this information."

Ron sees the danger. "Being able to aggregate all of a customers' information for them in one place has a lot of value, but I am concerned about having my customers give their access information to a third party."

Take The High Road

Many have rightly questioned regulators' ability to keep pace with new technology in order to protect privacy and security. For banks, it comes back to your long-standing reputations as protectors of financial information. By staying involved and developing appropriate safeguards you can protect consumer privacy and allow customers to reap the many benefits that result from faster, more efficient information sharing.

"No amount of money that can be made selling our customer's information is worth the problems that can occur if this information is not used in an appropriate manner. We're a bank; to a large extent, our business is trust," says Ron.

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Privacy Issues Evolving Quickly For Financial Institutions

By Phillip J. Britt

One of the most compelling issues in the electronic age is that of customer privacy. Privacy deals with how banks use information, to whom banks disclose it and ensuring its accuracy. Equally important is information security. If people can get into information systems, all banks have a problem.

"I have never seen an issue like this one," says Jo Ann Barefoot, managing director at KPMG Consulting's Financial Services Group. "It is evolving faster than anything I have ever seen. It's unique because it's an issue that everyone cares about. It hits a nerve near the bone for everybody."

Eyes On Banking

Part of what banks have to do is not wait for the regulations to be final, John Byrne, senior counsel and compliance manager, American Bankers Association, said at the Bank Administration Institute's retail delivery conference.

"All eyes will be on the banking industry on how we handle this new law," John said. "We're going to have to prove we can handle what's in the law today and what will be in the regulation shortly. If we can't prove that, we're going to face more and more restrictions on what we can do with information."

Financial institutions will have to post and disclose their privacy policies. This is something you should have been doing all along.

"We think most of the large institutions are already there," John added. "All institutions must disclose at the time of establishing the customer relationship and every year after that to every customer, the policies and procedures for 'Protecting customers non-public personal information, including the policies and practices of how you disclose information to affiliated and nonaffiliated entities.'"

State laws could be even more stringent than the federal regulations, John cautioned.

Already Working

One of the largest financial services companies, Citigroup, has worked on privacy for quite some time

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