

Complaining in Consumer Credit: Evidence from the Italian Financial System

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1 INTRODUCTION

Today, banks are fully aware that the global financial crisis has had a negative impact on consumer trust in financial intermediaries. In the present scenario, successful companies gain a competitive advantage through increased efficiency, high quality of service, and improved customer relations.

Several arguments are currently encouraging banks to increasingly adopt strategies of customer retention and customer loyalty. These arguments are based on a very simple fact: the costs incurred in avoiding the loss of old customers are clearly much lower than those required to acquire new customers. Moreover, keeping customers satisfied is currently both

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really critical and important, since losing customers in one business may also mean losing them in other business areas.

As regards service quality in particular, bank stakeholders are paying greater attention to the real value of financial products and services and their delivery processes as a parameter for the sustainability of trust-based relationships between banks and their customers.

The issues of the transparency and fairness standards of financial intermediaries and trust-based relationships with customers are of great significance. Banking initiatives must deal with the correct progress of the dynamics of contractual balances, in which any conduct based on the abuse of a dominant position by strong counterparts must be avoided. Within banking contracts, there is a natural imbalance between the two parties. The weaker counterpart, the customer, is in a position of net disadvantage compared to the bank.

Furthermore, the existence of a quick and direct procedure for communicating and managing any dissatisfaction or disservice is a way of protecting consumers. In fact, customers may not be able to apply to the civil courts due to reasons of cost and complex procedures. This point may, on the one hand, lead to difficulties in ensuring consumer rights and, on the other, result in unfair conduct on the part of lenders.

As a consequence, in many developed countries, banks have adopted complaint management systems in order to provide instruments to protect the weaker counterpart, namely, the customer.

For this reason, Alternative Dispute Resolution (ADR) systems have become a topical issue in the attempt to facilitate access to justice for consumers. These systems have developed extensively in the financial services sector and are viewed as an inexpensive way to manage dispute resolution in consumer matters.

The presence of an effective dispute resolution mechanism gives financial intermediaries an incentive to act in accordance with principles of transparency and fairness in customer relations, in addition to enhancing the public's trust in such intermediaries. Moreover, it helps the monitoring of operational, legal, and reputational risks.

Numerous studies (the marketing and management stream of literature) focus on complaint management as a useful mechanism in customer retention and to improve the quality of the provided services.

Many academic studies (the regulatory and banking stream of literature) investigate the consequences of ADR decisions on customer behaviour or the interactions between regulation and individual behaviour.

The number of customer complaints has been gradually increasing, having doubled in the last two years. This does not seem to be related

solely to the quality of financial services or the lack of compliance of banking output. Another reason can be found in the characteristics of the procedures involved, these being very simple and free of charge (without any sanctions, costs, or penalties for incorrect use or behaviour). Moreover, the ADR mechanism produces a relevant effect for the bank because all procedures are monitored by the Banking Authorities.

The aim of our study is to analyse the effects of ADR on the behaviour of consumers and financial intermediaries.

Our study analyses the complaints submitted directly to financial intermediaries by consumers regarding credit services. Subsequently, the analysis is extended to the characteristics of complaints received by Italy's Banking Financial Arbitrator (BFA) related to consumer credit. The analysis covers the period 2010–2016 and uses confidential data collected by the Italian Association of Consumer and Real Estate Credit (Assofin) as well as public data collected by the BFA.

The aims of the study are to analyse how the behaviour of consumers submitting a complaint to a bank or an appeal to the BFA has changed over the years and to highlight the main changes on the supply side of the consumer credit market. The chapter thus aims to highlight the role of the current ADR approach and its main critical issues, with specific concerns related to consumer protection.

The chapter is structured as follows.

Section 1, the Introduction, briefly introduces the topic and explains the structure of the study. In Sect. 2, we review the main strands of the research literature on the topic. Section 3 describes the process of managing complaints by banks via the different existing steps and the main features of the Italian ADR system (BFA). Section 4 provides statistical information on the appeals submitted to the BFA and on complaints received by financial institutions regarding consumer credit. This is followed by some concluding remarks and managerial implications in Sect. 5.

2 LITERATURE REVIEW

2.1 *Complaining in the Managerial and Marketing Stream*

Increasing interest in consumer complaint behaviour (CCB) arose during the 1960s. At that time, consumer satisfaction, consumer dissatisfaction, and CCB were three different—yet at the same time highly correlated—themes investigated by marketing and consumer studies.

Real and concrete marketing problems may be considered to be at the origin of these studies. For example, the importance given to quality, performance, and satisfaction and the emphasis afforded to customers are all factors that lead researchers to inquire into the complex mechanisms determining customer satisfaction or dissatisfaction, and into what constitutes consequent behaviour.

At the same time, the findings of studies are aimed at identifying and suggesting managerial and practical solutions which can be applied to markets or services.

CCB is an area of research dealing with the identification and analysis of all the aspects involved in the consumer reaction to a product or a service failure and the ensuing perceived dissatisfaction.

In fact, CCB consists of all the potential responses that customers use to express their dissatisfaction.

More specifically, CCB is the behaviour that people show and includes expressing negative opinions about the product and services to the producing company, to the supplier of products and services, or to third-party organizations. Thus, the study of CCB seems essential to explain and predict the customer's intention to continue doing business with and to remain loyal to the firm in question.

Recognizing the causes and consequences of customer complaint behaviour is of great importance within the environment of competition between products and services, as well as among financial intermediaries.

Especially for banks, this area is critical for identifying and managing operational, legal, and reputational risks: great attention paid to customer complaints may reduce these kinds of risks. The recent financial crises have shown to what extent reputational risk can influence the performance of banks and financial institutions.

Within the managerial and marketing stream of literature, many empirical and theoretical studies have analysed complaints and the importance of different variables within customer experience dissatisfaction.

The truly seminal work on the alternatives available to dissatisfied people is the paper by Hirschman (1970), which is based on three possible options: exit, voice, and loyalty.

Researchers suggest various taxonomies to understand the numerous CCB responses in which consumers can engage (Singh 1988; Maute and Forrester 1993; Broadbridge and Marshall 1995).

Customers can complain in various ways: seeking redress, boycotting suppliers, telling family and friends about the experience, or doing nothing

at all (Blodgett et al. 1995). Consumer complaints can be used not only to obtain redress but also to increase the firm's efficiency. Sellers receive important feedback on their products/services, leading to improved and increased consumer satisfaction. Complaints in fact disclose problems that, in many cases, are significant (Landon 1980).

Complaints can inform firms about the existing needs of consumers and provide the opportunity for discussion about future needs. Sanes (1993) stated that 'understanding complaints is equivalent to mining gold'.

From this perspective, complaining may help in discovering and correcting product issues, increasing consumer satisfaction, retaining the consumer as an active purchaser, rather than simply as a comfort consumer, or providing an excuse and/or fair redress (Hogarth and English 2002).

In many studies, a specific aspect is underlined: the existence of relevant differences if the customer uses a service or, instead, buys a product. More specifically, consumers seem to experience greater dissatisfaction with services compared to products (Best and Andreasen 1977); the reasons most frequently mentioned seem to be careless and unprofessional conducts. The same authors find that complaints are more frequent when the problem is perceived as obvious rather than subjective.

Hirschman (1970) and Tronvoll (2007) reported different consumer behaviour according to the market situation. Consumer reaction towards a product's or a service's decline can vary enormously if alternatives are really and easily available. In a competitive market, the 'exit' solution is easy to adopt because competitors are known and available. In a monopolistic situation, however, the most likely reaction to product or service failure is to remain silently loyal or to engage in negative word of mouth.

Different studies have sought to profile customers according to various aspects: age, sex, education, income, nationality, and personality. However, the findings of many studies on this aspect of CCB have shown very limited consistency and low significance.

As can be seen in the main managerial- and marketing-related stream of literature, many studies highlight the value of customer complaints and underline the fact that these should be welcomed.

A great deal of this research assumes that customers do not knowingly complain without a good reason. In fact, the focus within the service failure literature on service recovery is primarily rooted on the assumption that services have genuinely failed and the reasons which drive customers' complaints are essentially legitimate.

In contrast, as far as research is concerned, little attention has been paid to the behaviour (and hidden reasons) of those consumers who knowingly voice 'fake complaints', which represent the dishonest and unjustified aspect of CCB.

In fact, counter to the aforementioned main body of the managerial and marketing stream of literature (where customers' complaints originate from true dissatisfaction), this minor strand of literature argues that complaint episodes may occur without customers experiencing real service failure or dissatisfaction.

Jacoby and Jaccard (1981) acknowledge the existence of complaints from *satisfied users* who may *deliberately fabricate* problems.

Reynolds and Harris (2005) explore the reasons for and forms of deliberately illegitimate complaints, professed while reporting not sincere service failures. Using the critical incident technique, they analysed 104 interviews with customers who had knowingly made an illegitimate complaint six months prior to the interview. Interesting insights and four distinct forms of customer complainants emerged from their study. They labelled these as follows: one-off complainants, opportunistic complainants, conditioned complainants, and professional complainants.

Ro and Wong (2012) investigate how service employees in hotels and restaurants handle opportunistic customer complaints.

Huang and Miao (2016) explore frontline employees' perceptions and responses given to illegitimate customer complaint behaviour in the hospitality industry. In their study, the analysis of data revealed different types of illegitimate complainants: opportunistic plotters, repetitive grumblers, and occasional tyrants.

Customers with legitimate complaints could also become opportunistic complainants by taking advantage of the service failure in order to obtain extra financial benefits when complaining (Wirtz and McColl-Kennedy 2010).

These are only some of the research studies related to this specific, yet at the same time, important approach. All these studies contradict the mantra that 'the customer is always right'. This mantra in fact gives certain types of customers an unfair advantage.

For our analysis, this stream highlights a key issue within the literature.

2.2 *Complaining in the Financial Sector*

Services and products in the financial sector are very similar; even when there are innovations, they are quite easy to copy. Hence, when it comes to supplying services and products, banks can differentiate themselves

only in terms of price and quality. In this industry, satisfaction becomes a key variable, allowing differentiation from competitors.

Complaint management is a relatively recent research field, integrated within the larger perspective of customer relationship management.

It is well known that the scenario in which financial institutions operate has altered in recent years. With increased competition, the global market, growing product portfolios, and diminishing margins, the behaviour of bank customers has also changed.

Customer dissatisfaction is often affected by the relationship established with front office human resources. The main motives for consumer complaint behaviour in banks are rude staff behaviour, delays in services, hidden costs, long queues, and misinformation. The psychological aspect that influences the relationship between bank employees on the one hand and customers on the other is analysed in Khartabiel and Saydam (2014). Many items are considered in the study: banking functions, training programmes, wages, communication related to bank organization, teamwork, job satisfaction, career opportunities, customer loyalty, and the provision of high-quality services to customers who meet their needs. The authors found that when bank acts to improve job satisfaction, customer satisfaction and loyalty are raised at the same time. In other words, job satisfaction has a significant influence on staff behaviour towards costumers, and this strengthens the important hypothesis that satisfied employees produce better results.

Moving on from the consequences of service quality to its underlying causes, there is consensus in the academic literature on banks and financial institutions regarding the importance of behavioural and process indicators such as attentiveness, responsiveness, care, and assurance as the main variables influencing banking service quality (Bloemer et al. 1998). These variables can be measured via customer satisfaction analysis, loyalty indicators, and complaint handling systems.

Other authors (Wang et al. 2003) show that, in the banking industry, the higher the quality of services perceived by customers, the lower the reputational risk exposure, whereas the lower the quality of services perceived by customers, the higher the reputational risk exposure.

The paradox of complaint management lies in the hypothesis according to which, following a negative event, dissatisfied customers may be more satisfied and more loyal than customers who did not experience such an event, provided that the firm proposes an adequate management of their complaints. Negative interactions are often more useful than positive interactions. Lok and Matthews (2007) found that the satisfactory

resolution of a complaint makes customers happier and less likely to leave the bank.

In the event of a complaint, the bank may reduce its losses and hence the risk of losing the customer by referring the customer to its own customer service department. If the department is able to provide a reasonable solution for the customer, the bank may reduce its losses, and the customer will be entitled to obtain a refund for the loss suffered (Uppal 2010).

Complaint management is a very crucial tool for enhancing customer loyalty, risk minimization, and CRM (Shalini and Munjal 2014). These authors found that complaints and risk have a significant relationship and that risk can be reduced through complaint management.

The possibility of gaining a competitive advantage from complaint management implies that the organizational structure is able to propose an efficient system of complaint management (Hakiri 2012). If the bank makes an effort to solve the problem promptly and tries to figure out the origin of the issue perceived by the customer, with this information being properly filed and stored, the bank can manage to improve the quality of the supplied service.

Unpleasant banking experiences have likewise been investigated (generally via surveys and questionnaires) in different national banking systems in order to ascertain the determinants of complaining. Poor and unsatisfactory employee behaviour determines unpleasant customer experiences, while misinformation from banking staff generally lead to an increase in unpleasant customer experiences (Jugenissova et al. 2014).

One of the crucial drivers of unpleasant experiences is the time spent during the carrying out of banking services (Srijumpa et al. 2007).

Ramachandran and Chidambaram (2012) compiled an almost complete review of the literature on these themes. These authors summarize the results of their literature review on customer satisfaction towards the services of a bank from five different perspectives: service encounters, customer waiting time to obtain the service, the role of intermediaries, the quality of the service provided, and customer complaints towards the bank. They state that the service process performance of an organization should be measured continuously in order to achieve a competitive advantage and that this is possible by providing excellent service.

Few studies have analysed the Italian banking industry in this respect, especially when we shift to analyses conducted using actual complaint databases.

One reason (but not the only one) for this is that, since 2010, the Bank of Italy has legally obliged banks to publish a report on their websites regarding their complaint management activities. This mandatory disclosure refers not only to the number of complaints but also to the type of services or products which generated them.

Malinconico et al. (2013) examined the content of these actual customer complaints within Italian retail banks using the complaint data available on all the bank websites mentioned above. Their study aims to discover the behaviour of different types of banks (by legal form, size, etc.). The underlying hypothesis of their paper is that the number of complaints received by a bank is a good proxy of customer dissatisfaction. The larger the bank and the number of services it offers, the higher the number of complaints it receives. In order to avoid problems of scale (i.e. comparing large and small banks), the total number of complaints is divided by appropriate scale variables. The study examined the year 2011 and a total of more than 66,500 complaints concerning 47 Italian banks, covering about 60% of transactions on the Italian banking market. From their initial results, conducted with three analysis of variance (ANOVA) tests, it emerges that small banks and local banks have a greater ability to prevent retail customer dissatisfaction.

D'Apolito and Labini (2014) analysed the level of disclosure in handling complaints in a sample of Italian banks. The study covered the period 2010–2012. These authors built a measure of disclosure based on the information that banks provide on their websites and in corporate documents, and estimated the relationship between disclosure levels and financial and organizational variables. The following results of their study may be highlighted:

- The level of disclosure increased both qualitatively and quantitatively during the three-year period, even with differences among banks.
- This level of disclosure was still low at that time.
- Size and efficiency variables were significant, as well as the internal organizational arrangements for handling complaints (internal management vs. outsourcing).

We could continue to analyse other studies, but frankly, the majority of the research within the financial sector covers and deals with the mainstream quite similarly to the ways described previously in this chapter.

Albeit with different depths, these studies—only a few of which are cited, for the sake of brevity—address the fact that the bank pursues a duality of interests: to preserve future benefits-related customers and to improve the quality of its services. Accordingly, this literature provides a common framework that is almost always related to the topic of dis/satisfaction. Briefly speaking, the main key messages are:

- Complaints are a manifested expression of dissatisfaction; for this reason, a careful analysis of complaints—which are very rich sources of information—allows banks to detect situations of customer dissatisfaction and their underlying motivations.
- Complaints are key indicators that are useful for measuring the actual level of performance of customer services.
- Complaint management is a suitable tool for enhancing the quality perceived by customers and the bank's relationship with them.
- Efficient complaint management systems should allow banks to limit legal and reputational risks via the reduction of conflict with customers and hence reduce litigation costs for banks.

2.3 *Complaining and ADR Schemes*

Most of the interest in ADR worldwide is based on the simple and true fact that the civil courts of justice are overwhelmed, and legal costs are very high.

The literature on ADR can be divided into three relevant clusters:

- Studies concerned with the regulatory analysis of the main features of different ADR systems. A large number of the research studies we examined are related to the Italian BFA (Bank of Italy 2014, 2015, 2016b, c, 2017; Caggiano 2015; Consolo and Stella 2011; De Carolis 2011; Frosini 2011; Maimeri 2012; Perassi 2011).
- Studies concerned with the comparative analysis of ADR schemes in various countries. The comparison of consumer ADR schemes shows a wide range of different approaches, including arbitration, ombudsmen, mediation, and conciliation schemes, as well as various determinants related to the choice of referring to the ADR procedure instead of to civil courts (Boccuzzi 2010; Valsecchi 2011; Gilad 2008a, b; Thomas and Frizon 2011).

- Studies concerned with the empirical analysis of the nature and trend of BFA appeals in terms of types and/or their correlation with other aspects such as the effects of the disclosure of verdicts on the frequency of new complaints (Malinconico et al. 2011; Malinconico and Fuccio 2016; Filotto et al. 2016).

For the present analysis, we are mainly interested in the third cluster of studies, which provides empirical analysis based on the statistics on bank disputes in the retail banking service, in order to assess to what extent ADR has been used by financial consumers and what the ensuing effects produced on banks' behaviour towards customers are.

Malinconico et al. (2011) focused specifically on the effect of ADR systems on customer protection. These authors provide an explorative analysis (covering the period 2009–2010) designed to understand the preliminary features of ADR in Italy.

The assumption that complaints are an expression of negative customer sentiment and that the way complaints are managed influences the perception the customer has regarding the quality of services has been studied by Malinconico and Fuccio (2016). In their study, the number of BFA appeals is treated as a reliable indicator of deep dissatisfaction that arises not only from the poor quality of the provided services but also from the speed with which the bank is able to manage customer complaints. The data used cover the period 2012–2014 and comprise appeals filed before the BFA related to a sample of 74 Italian banks. The results show that small banks and cooperative banks are presumably more inclined to closely monitor their customers, due to the fact that their organizational structures allow them to resolve customer problems.

An interesting study is that carried out by Filotto et al. (2016). These authors examined the behaviour of consumers appealing to the BFA, with the aim of understanding the effect of 'attracting' other complaints, obviously later in time. They started out from the observation that, if certain decisions are mostly in favour of the appellants, this encourages consumers to take actions, as the minimum cost of submitting a complaint does not represent a disincentive for non-valid claims. They studied the link between the number of new complaints submitted and the number of valid claims. Their main results show that a sort of 'attraction effect' exists for many banking products, and this effect is almost immediate, as it occurs within a two year span. Considering that the BFA's decisions are publicly disclosed, but still not widely known among unsophisticated customers, it is

difficult to understand how such a large number of consumers could become aware of these outcomes and decide to complain. One possible reasonable answer is that lawyers and professionals (the so-called facilitators) play today a significant role in seeking out potential complainants who are encouraged to submit a complaint to the BFA.

3 ITALIAN ADR

Complaint management systems are related to the process of receiving, investigating, and resolving controversies originating from customers who complain about a procedure or financial product.

The debate on ADRs as instruments that facilitate access to justice has recently become more widespread in the European Union, as these mechanisms have proved to be particularly useful for consumer-related disputes concerning small monetary claims. The low value of the majority of these disputes often makes courts of justice an unsuitable place to obtain individual redress. For this reason, courts are seen as the last resort, and, when available, consumers increasingly opt for more informal ADR schemes.

Furthermore, the financial crisis has given rise to a renewed focus on consumer protection, resulting in the adoption of new guidelines for complaint management in the finance industry.¹

In many developed economies, Banking Authorities have adopted an ADR procedure—in Italy, the so-called BFA—in order to manage complaints that customers and financial intermediaries cannot solve by themselves.

In Italy,² all customers can use this procedure after a first stage in which they submit their claims to financial intermediaries or banks through a specific system of complaint management.³ After 30 days, if they have not

¹ See Bank of Italy (2014, 2016b).

² We need to stress the fact that the main consumer ADR schemes adopted among different countries will not be analysed here. See, for instance, Boccuzzi (2010), Valsecchi (2011), and Bank of Italy (2017).

³ Specifically related to the organization and operation of complaint offices, a recent analysis conducted by the Bank of Italy examines good practices and criticalities in the handling of complaints. More precisely, the Bank of Italy has stated that complaint management guidelines—issued by the Joint European Banking Authority-European Securities and Markets Authority-European Insurance and Occupational Pensions Authority (EBA-ESMA-EIOPA) Committee in May 2014—require the competent authorities to ensure that companies (and banks, authors' note) adopt a complaint management policy and provide themselves with a business function and procedures that will enable them to manage complaints in a fair way.

received a reply or they are not satisfied with the bank's reply, they can apply for a ruling from the BFA or a civil court of justice.

In 2009, the Bank of Italy instituted the BFA, implementing Article 128 bis of the Consolidated Law on Banking, a provision introduced by Law 262/2005 (Investor Protection Law). The Investor Protection Law stipulates that the banking and finance industries must have systems in place for the out-of-court settlement of disputes, and the law itself states the principles to which these systems should conform: timeliness, cost-effectiveness, and effective legal protection; a deciding body that is impartial and representative; and protection of the legal right to seek remedy through the other means made available by the legal system.

The BFA's rulings are not legal judgments: they are not legally binding on the customer or the intermediary and they do not affect the possibility of submitting the dispute to the civil courts. The relevance of BFA's decisions lies in their authoritative quality and impartiality. If an intermediary refuses to comply with a decision, notice of its non-compliance is published on the BFA's website.⁴

It is important to stress the fact that the BFA cannot decide on issues related to investment products, services, or activities (securities trading or placement, investment advice, asset management, or matters relating to bonds issued or settled by banks). The Arbitrator of Financial Disputes (AFD), a new out-of-court dispute resolution body established by CONSOB, the Italian Companies and Stock Exchange Commission, was created in January 2017 to deal with these issues.

Procedures should include the identification of a manager and/or an office independent from business functions. The compliance function—or, in its absence, an Internal Audit—must report to the corporate bodies on the overall situation of the complaints received and the adequacy of the procedures and organizational solutions in place at least annually.

During 2015, inspections were carried out on the operations of these complaint offices. The audits identified a number of good organizational practices capable of providing quick, exhaustive, and satisfactory customer responses, as well as effective use of information obtained from complaints. In some cases, the controls highlighted the existence of areas of improvement. The Bank of Italy has therefore sent a communication to illustrate good practices throughout the banking and financial system, asking each operator to conduct an in-depth examination of its handling of complaints and to take initiatives aimed at raising the quality of the service. See Bank of Italy (2016a) for further details.

⁴ 'The BFA must not be confused with arbitration, a legal instrument whose purpose is to enable parties, under an agreement that may precede or follow the rise of the dispute, to have their case settled by one or more arbiters whose decisions are binding. Nor can the BFA be likened to mediation. The two procedures differ in legal basis, scope, prerequisites to access them and also the outcomes are very different'. See Bank of Italy (2014, 2016b).

Participation in the BFA system is mandatory for banks, being a condition for the exercise of banking and financial activities. Non-compliance is punishable with a fine.

All intermediaries are included in the registers kept by the Bank of Italy. Banks, finance companies, payment institutions, electronic money institutions, loan guarantee consortia, and BancoPosta must adhere to the system, as must foreign intermediaries operating in Italy which are not part of Fin-Net, the European out-of-court settlement system endorsed by the European Commission.⁵

The Bank of Italy 'checks banks' compliance with the rules on transparency and fairness with off-site prudential controls and on-site inspections at branches and headquarters. In the case of irregularities, anomalies or misconduct, the Bank intervenes and takes appropriate measures with respect to the system or individual banks, depending on the seriousness of the issues.⁶

The outcomes of the BFA's proceedings constitute a significant contribution to supervisory activity: the BFA's decisions 'become part of the broader pool of information at the Bank's disposal for its regulatory and control function.'⁷

Intermediaries are under no obligation in their customer relations to follow every interpretation made or endorsed by the BFA. Nevertheless, pursuant to its Directives, banks and other financial intermediaries

must ensure, through appropriate internal procedures, that their complaints departments are familiar with the BFA's guidelines, are updated to the most recent positions and assess customer complaints on this basis. In particular, the complaints departments are required to determine whether the point raised by the customer has a precedent in earlier cases decided by the panels.⁸

⁵ Fin-Net is a network promoted by the European Commission in order to assist the development and cooperation of ADR schemes in Europe. It enables consumers who have a dispute with an intermediary in another member state to turn to their own national ADR scheme, which, through Fin-Net, will put them in touch with the equivalent scheme in the intermediary's country. Fin-Net currently has 60 member ADR schemes from EU countries plus Iceland, Liechtenstein, and Norway. Italy's Banking and Financial Ombudsman has been a member since 2011. See Bank of Italy (2017).

⁶ See Bank of Italy (2014).

⁷ See Bank of Italy (2016c), Section 1.

⁸ See Bank of Italy (2014).

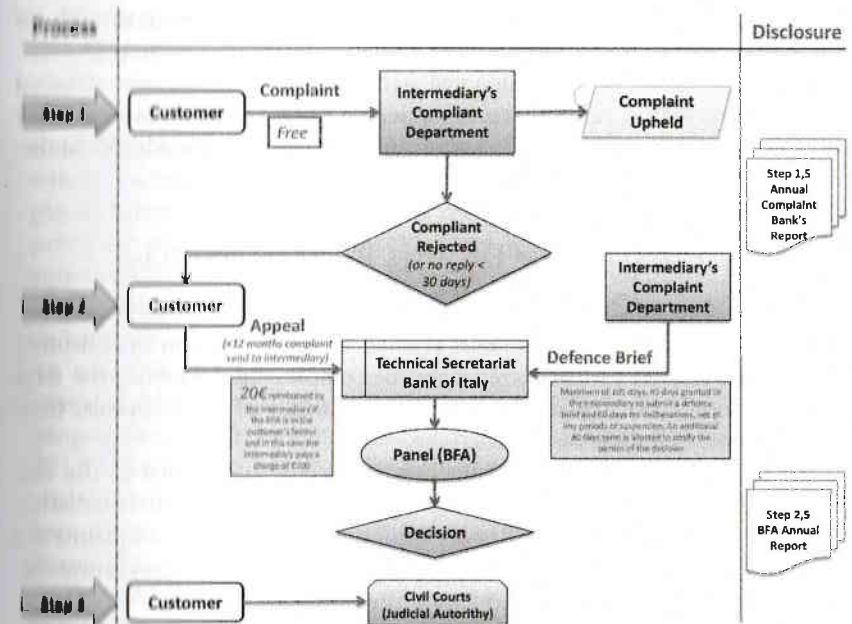


Fig. 6.1 The steps of the complaint handling process in Italy. (Source: Adapted from Bank of Italy 2014)

Figure 6.1 describes the steps of the process and the mandatory duties as regards the disclosures involved.

A complaint against a bank is first submitted by the complainant to the bank for its consideration ('Step 1').

A complainant who is dissatisfied with the bank's decision may then request its review by the BFA ('Step 2').

The BFA's decisions are legally binding upon firms, whereas consumers are free to pursue their case anew in the civil courts ('Step 3'). They are free to file a complaint before a civil court at any time (i.e. 'Step 3' does not necessarily come at the end). In Italy, it is well known that the standard expenses and duration of legal procedures are not competitive compared with ADR systems.

At the same time, banks disclose a report every year on their website containing a qualitative and quantitative analysis of all complaints received (aggregated data) during the year, and any changes with respect to the

previous year. We call this disclosure moment 'Step 1.5', even though we know that it does not happen exactly between 'Step 1' and 'Step 2'.

Moreover, the Banking Financial Arbitrator publishes a very detailed report every year including data on appeals and operations (matters under dispute, types of intermediary, outcomes, etc.). We call this additional disclosure moment 'Step 2.5' (with the same caveat as above).

4 ANALYSIS OF DISPUTES BETWEEN FINANCIAL INTERMEDIARIES AND CONSUMERS

Within the literature, most studies analyse the phenomenon of consumer complaints related to using credit services employing data from the BFA Annual Report. Such data describe the evolution of BFA appeals, their motivations, and their outcomes.

In the present study, consumer behaviour is also analysed in the first step of the ADR process, that is, complaints to financial intermediaries. Data from Assofin's Annual Report on Consumer Credit Complaints are used to this end. This source records a sample of intermediaries representing approximately 93% of the outstanding credit.

The joint analysis of complaints and appeals allows us to examine the whole ADR process and identify important features related to consumer use of ADR.

Complaints and BFA appeals have grown sharply in Italy. During 2016, the number of BFA appeals reached the figure of 21,652 (Table 6.1) with a Cumulative Average Growth Rate (CAGR)—in the period 2010–2016—of 32.3%. The total number of complaints registered in the Italian financial system during 2016 is over 250,000. Of these, 100,000 refer to consumer credit, the CAGR being equal to 17.1% in this case.

Table 6.1 BFA appeals and consumer credit complaints (annual data and % variation)

	2010	2011	2012	2013	2014	2015	2016
BFA appeals	3409	3578	5653	7862	11,229	13,578	21,652
Variation (%)		5.0	58.0	39.1	42.8	20.9	59.5
Consumer credit complaints		35,230	36,572	38,207	51,186	70,429	90,866
Variation (%)			3.8	4.5	34.0	37.6	29.0

Source: BFA, Banking and Financial Ombudsman Annual Report (various years), Assofin, Annual Report on Consumer Credit Complaints (various years)

The strong growth originates mainly from appeals related to loans secured by pledge of salary (LSPS), a typical kind of personal loan with wage assignment and where the payments are withdrawn directly from employees' pay. During 2016, these complaints accounted for 71% of the total. The same growth takes place on the complaints side, something which is a mandatory step in order to be admitted to BFA, where complaints related to LSPS represented 64% of the total in 2016. These disputes are mainly due to non-repayment to consumers of a part of the commissions not collected in the case of early repayment of LSPS.

The geographical distribution shows a greater number of complaints and appeals in the southern areas of the country, where employee incomes are more widespread and, last but not least, where the average salary is lower (Table 6.2). In fact, a positive relationship is found between the geographical origin of the appeals and the risk of poverty (Bank of Italy 2017). Not surprisingly, households living in the South represent the most evident customer target of LSPS and, realistically, they are more likely to have repaid in advance and renegotiated the LSPS more than once. In all geographical areas, over 67% of appeals originate from male consumers.

The trend in appeals by type of financial intermediary reflects the role of individuals in the supply of LSPS (Table 6.3). During 2016, these appeals

Table 6.2 BFA appeals per million inhabitants (annual data)

	2011	2012	2013	2014	2015	2016
Northern Italy	40.3	72.8	107.5	135.0	147.0	241.6
Italy	47.4	80.2	114.6	165.2	206.5	341.1
Central Italy	66.7	98.2	124.7	176.9	239.4	353.4
Southern Italy and the Islands	42.2	76.9	117.3	202.2	271.2	485.4

Source: BFA, Banking and Financial Ombudsman Annual Report (various years)

Table 6.3 BFA appeals by type of financial intermediary (annual data and CAGR 2010–2016)

	2010	2011	2012	2013	2014	2015	2016	CAGR (%)
Domestic banks	2546	2213	2776	3541	4755	5742	10,002	23.3
Foreign banks	188	195	319	529	1083	1805	2894	55.0
Other financial intermediaries	654	1131	2479	3674	5238	5865	8228	35.8

Source: BFA, Banking and Financial Ombudsman Annual Report (various years)

amount to 87% of the total for foreign banks and 94% for financial intermediaries. Large banks are also affected by LSPS appeals, though to a lesser extent, whereas small banks and mutual banks more frequently receive claims related to topics like checking accounts, mortgages, and debit cards.

Banks however show a lower growth rate in terms of appeals. As we will see later, this reflects a different approach to complaint management that avoids exacerbating the conflict and preserves the relationship with customers, often characterized by a greater variety of products compared to other, more specialized intermediaries. Banks are more likely to be inclined to manage the situation at the time the complaint is made (Step 1) and to avoid unnecessarily pursuing a dispute with the customer.

The percentage of appeals resolved and concluded by the BFA (with an agreement between the customer and the financial intermediary) is increasing and represents 87% of the results of the appeals of 2016 (Table 6.4).

The analysis of resolved appeals shows a high share of favourable outcomes for the complainant: 91% for LSPS; while for other loans, the share is roughly 50% of the submitted appeals (Table 6.5).

Table 6.4 Outcomes of submitted appeals (%)

	2012	2013	2014	2015	2016
Resolved	48	37	33	43	51
Settled	20	36	36	28	26
Dismissed	32	27	31	30	23
Total	100	100	100	100	100

Source: BFA, Banking and Financial Ombudsman Annual Report (various years)

Table 6.5 Outcomes of submitted appeals by product (%)

	<i>Resolved and settled</i>	<i>Dismissed</i>
Central credit register	37	63
Mortgage	39	61
Other loans	41	59
Consumer credit	42	58
Bank transfer	45	55
Deposit	49	51
Cheque	50	50
Debit card	60	40
Credit card	62	38
LSPS	91	9

Source: BFA, Banking and Financial Ombudsman Annual Report (various years)

From this point of view, the establishment of ADR is a really positive procedure for solving disputes between the customer and the financial intermediary. It decides the issues for many cases of unfair behaviour and strengthens the ability to protect the system. An increasing number of consumers are using ADR to resolve their disputes with financial intermediaries. During 2017, the BFA had to increase its staff in order to cope with the high number of appeals and reduce response times.

The BFA, whose due time for responding should be within 105 days, currently has an average response time of 314 days, and there are still a significant number of appeals in arrears.

An appeal to the BFA, just like a complaint to an intermediary, does not require any form of mandatory legal assistance. However, it is observed that consumers are supported by a legal advisor in over 60% of complaints, while this percentage rises to above 86% in the case of BFA appeals (Table 6.6).

It is interesting to investigate this phenomenon in order to understand whether there are specific reasons related to the ADR framework that prevent individual consumers from using this procedure independently.

The analysis of the appeals shows a positive relationship between the number of lawyers in a region and the number of appeals assisted by a lawyer (Bank of Italy 2017). At the same time, the sample analysis of complaints and appeals allows us to verify that the number of associations and legal advisors specializing in these disputes is not so high.

In fact, the presence of associations and legal advisors is not a negative phenomenon if it helps to improve the functioning of the ADR and allows the broadening of consumer protection. The final opinion becomes less

Table 6.6 Consumer credit complaints and BFA appeals by origin (%)

	2015	2016
Consumer credit complaints		
Lawyer/other professionals	55	59
Consumer association	5	7
Individual consumer	40	34
Appeals to the BFA		
Lawyer/other professionals	60	61
Consumer association	4	10
Other associations	14	15
Individual consumer	22	14

Source: BFA, Banking and Financial Ombudsman Annual Report (various years), Assofin, Annual Report on Consumer Credit Complaints (various years)

positive in the case of professionals who do not really improve the process, whose intervention is not regulated, and whose fees, paid by consumers, reduce, de facto, their protection and, above all, fair compensation for the damage incurred.

Along with the absence of disincentives to present unacceptable complaints, this aspect could contribute to the increase in appeals submitted for purposes other than actual consumer protection.

The second part of the analysis deals with complaints towards financial intermediaries (Step 1), delving further into the dynamics of the relationship and consumer behaviour. Step 1 complaints presented by consumers during 2016 were around 250,000 at the system level, about 100,000 of which were related to consumer credit.

If we exclude complaints related to LSPS, there has been a reduction over the last two years (Table 6.7). This trend also originates from the behaviour of intermediaries due to the fact that they tried to remove reasons for dissatisfaction and complaint as far as possible in order to prevent future complaints.

These efforts have also arisen, to a certain extent, due to the establishment of ADR, which makes any opportunistic behaviour by financial intermediaries more expensive and produces incentives to change non-compliant operational and commercial practices.

This is evidenced by the decrease in complaints, in the three-year period from 2014 to 2016 compared to the previous three-year period, in all types of complaints made by customers (Table 6.8). This trend is generated by the learning effect of financial intermediaries, which enhances all the information acquired within the management of disputes with customers.

It is equally worth noting that the number of employees in complaint handling offices has increased by more than 50% since 2012. This has

Table 6.7 Consumer credit complaints without early repayment LSPS (annual data and % variation)

	2011	2012	2013	2014	2015	2016
Consumer credit complaints (without early repayment of loans secured by pledge of salary)	35,230	36,572	38,207	38,441	36,326	33,063
Variation (%)		3.8	4.5	0.6	-5.5	-9.0

Source: Assofin, Annual Report on Consumer Credit Complaints (various years)

Table 6.8 Consumer credit complaints by reason (% variation)

	Var. % 2011-2013	Var. % 2014-2016
Early repayment of loans secured by pledge of salary	n.a.	354
Insurance policies/accessory (financial services)	54	-13
Administrative/organizational aspects	39	-17
Disclosure	38	-19
Privacy/central credit register	-28	1
Credit standing	1	-2
Loan recovery	117	-33
Product and service anomalies	-44	-20
Disclaimers/fraud	-47	-3

Source: Assofin, Annual Report on Consumer Credit Complaints (various years)

Table 6.9 Consumer credit complaints' management

	2012	2016
No. of complaint office employees	100	156
Complaints per employee	366	582
Average no. of days for a response	17	17

Source: Assofin, Annual Report on Consumer Credit Complaints (various years)

occurred in order to ensure fast and due answers within 30 days (required by law) upon receipt of the complaint.

Specialization and acquired expertise have made it possible to improve employee productivity (from 366 to 582 practices), testifying to the efforts made by intermediaries in the management of consumer complaints (Table 6.9).

5 CONCLUSIONS

The parallel analysis of bank complaints and appeals to Italy's BFA underlines the positive value of the establishment of ADR in the market of credit and banking services to consumers.

ADR is an irreplaceable tool for direct consumer protection and contributes to improving the functioning of markets. As highlighted in this study, it represents a way to become aware of customer satisfaction and an instrument for improving the ability to respond to customer needs.

At the same time, it has likewise become a tool to improve the overall compliance of financial intermediaries and to pursue operational efficiency.

Undeniably, as suggested by law, ADR is also a monitoring tool for authorities and should contribute to improving the information framework available to credit authorities for their control and regulation activities.

The significant growth of complaints and BFA appeals confirms the need for the establishment of this dispute management system between consumers and financial intermediaries.

ADR intercepts a tiny dispute that would not have other results and that is of great importance both for the consumer's satisfaction and for financial intermediaries in terms of costs, risks, reputation, and so on.

Financial intermediaries and banks in particular have altered their behaviour and operating practices, valuing what they have learned from the management of complaints and the rulings of the BFA. This is confirmed by the decrease in disputes and consumer outcomes for many banking services, a sign that banks are trying to improve their ability to generate relational value.

However, there are areas for improvement both in terms of consumer protection and market efficiency. It is necessary to reflect on the distorting effects generated by the high incidence of professionals who support consumers, their cost, and the lack of disincentives (of an economic or other nature) with respect to the propensity to resort to ADR without the required positive assumptions.

We can currently see the main effects of this by considering certain key points: the increase in response times well beyond the number of days envisaged by the law; the unregulated distribution of compensation between the consumer and the legal advisor; and the growth of costs for financial intermediaries in the process of managing complaints and BFA appeals.

The increase in costs and operational risks for lenders is significant and could lead to an increase in average credit costs or, even worse, lower credit supply, especially for those products characterized by more regulatory uncertainty and greater litigation risk, which are, however, usually addressed to specific customer targets.

The managerial implications highlighted by the study include a need for the management of banks to analyse customer complaints better. Managers have to enforce mechanisms via which customer complaints are monitored and tracked in order to identify and challenge fraudulent complainants.

The policy implications are quite significant, as they suggest that the authorities should review these mechanisms, given that they can lead to opportunistic behaviour by consumers, consulting firms, law firms, and associations for business and profit reasons.

Credit authorities should consider and introduce appropriate mechanisms able to steer customers towards fair and honest behaviour, as well as penalties and disincentives able to make unfair and unjustified claim attempts very expensive.

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