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Financial Information for Consumers: A Future Strategy for Consumer Organisations

EDITORS' NOTE

The provision of information and advice about financial services will be an important task for consumer organizations and agencies in the years ahead. The present paper by Jeremy Mitchell gives a good overview over the issues and problems involved. Most of his examples come from the U.K. In future issues, JCP hopes to bring reports about the provision of financial information also from other countries.

ABSTRACT. The consumer is faced with increasingly complex decision-making in relation to financial services. His or her information needs are growing more sophisticated and comprehensive. At the same time, the supply of many financial services to consumers is becoming increasingly internationalised. It is suggested that national consumer organisations should work in collaboration to identify consumers' financial information needs, to develop a shared testing programme for internationally available financial services and to share experience in developing information and communications technology-based personal financial advice.

A British consumer who wants to borrow money to buy a house is faced with a complex set of interlocking decisions. First, what type of financial institution should be approached for a loan? Possible sources of finance include:

- Building societies;
- Banks;
- Insurance companies;
- Finance houses;
- Local authorities.

Second, what is the most suitable type of loan? The choice lies between:

- Repayment loan;
- Endowment life assurance-linked loan, further sub-divided into five different kinds of endowment life assurance policy;
- Pension-linked loan, for some consumers.

These two decisions are not even independent: Not all types of loan are available from all types of financial institution.

Third, which combination of institution and loan is cheapest, in terms of the cost of borrowing? What weight should be given to cost against other factors involved? In the case of some endowment life

assurance-linked loans, this will also involve making an assessment of the likely future profits performance of different life assurance companies.

Internationalisation of Financial Services

Even this simplified example shows the complexity of financial decision-making that confronts the consumer and the consumer's need for access to comprehensive and sophisticated information. It also illustrates two fundamental revolutions that are taking place in the supply of personal financial services. The first of these is the internationalisation of financial services. Taking the example of the British consumer wanting a loan to buy a house, the list of foreign banks and other lenders willing to offer loans includes Bank of America, Citibank Savings, Chemical Bank, First National Bank of Boston, Security Pacific Trust, Royal Trust Company of Canada, Canada Permanent Trust, Allied Arab Bank and United Bank of Kuwait (Consumers' Association, 1986a). A less visible form of internationalisation is that some British building societies are now raising wholesale funds in European financial markets, through Eurobonds and Eurodollar Certificates of Deposit, to lend to British consumers,

The internationalisation of the market for housing finance in Britain has already started to happen. The same process of change is happening with other forms of credit and with savings and investment. It is on the brink of happening with payment systems and insurance. The driving force is the search for new markets, which is transforming many financial institutions into financial multinationals. It is a process about which many governments are ambivalent. They see the economic advantages to be gained from favourable balance of trade in financial services, while adopting a protectionist stance — often in the guise of strict prudential controls — to safeguard their domestic institutions. Nevertheless, the direction of change is moving inexorably towards the abolition of national boundaries in relation to the provision of financial services. On a global scale, there is the inter-governmental agreement reached at Punta del Este, Uruguay, in September 1986 to consider ways in which barriers to international trade in services, including financial services, can be reduced. Within the European Community, the White Paper on completing the internal market (Commission of the European Communities,

1985) sets out clear targets for the establishment of a single, barrier-free market for financial services.

Barriers Between Different Financial Institutions Break Down

The second of these revolutions is the breaking down of barriers between different types of financial institution. Increasingly, different types of financial institution are in competition with each other over a wide range of financial services. There is pressure for change in national prudential control systems to take account of the realities of the market place. For example, in Britain the Building Societies Act 1986 has added a wide range of new powers to the building societies' traditional function of lending money to consumers to buy houses. They now have the freedom to make unsecured loans, lend on overdraft, engage in money transmission and foreign exchange services, establish and administer pension schemes, arrange the provision of insurance and, through a subsidiary, provide estate agency services and establish and manage both personal equity plans and unit trust schemes for the provision of pensions. Building societies are therefore now in full or partial competition not just with banks, but also with pension funds, insurance brokers and other financial intermediaries, estate agents, and unit trusts.

Other Developments

Accompanying and sustaining these two revolutions is the rapidly growing use of new information and communications technology. At present, this is most evident to consumers in the form of cash dispensers and automated teller machines but in fact it increasingly supports the whole nexus of financial services.

These revolutions are far from complete. Indeed, they are only in their early stages. We are still some way away from an era when the provision of financial services to consumers is likely to be characterised by a mixture of high technology multinational financial conglomerates and smaller financial institutions which have retained or discovered a specialised niche in the market. It is not, though, too early for consumers and consumer organisations to think systematically about their needs for financial information and about how these can best be met in a period of rapid change. In embarking on this process, there are four questions that should be kept in mind:

- What financial services do consumers need information about?
- What kinds of information do consumers need?
- Who should undertake responsibility for providing the information?
- What means should be used to convey the information?

What Types of Services Are Relevant to Consumers?

The most significant financial services are savings and investments, credit, money transfer, insurance, pensions, and taxation. Are all of these fit and proper subjects for consumer organisations to give information and advice about? It is sometimes argued that if a consumer organisation gives information and advice about savings and investments, it commits itself to upholding a capitalist, free enterprise economic system. Is this a tenable argument? Whatever the ideological or campaigning stance of a consumer organisation, its job is to encourage consumers to take the decisions that are going to suit them best and to give them the information that will enable them to do so. Consumer organisations should not be inhibited about encouraging consumers to get the best possible value for money from their savings and investments.

What Kinds of Information Do Consumers Need?

Should a consumer organisation take ethical and social factors into account when giving information and advice on savings and investments? If a company has investments in South Africa, should it be “not recommended” as a home for consumers’ savings even though it might be a “best buy” on economic criteria? What about a company that manufactures cigarettes? Or refuses to recognise trade unions? The problem is that there is no limit to the list of ethical and social factors which might be taken into account in giving financial information and advice. Indeed, some of them might be mutually contradictory. Should consumer organisations also cater for the ideological stance of the consumer who wants to know which companies do *not* recognise trade unions? The only practical policy for a consumer organisation is to ignore these factors when dealing with financial services. There is nothing to prevent those consumers who have a strong ethical viewpoint from getting the information they want from other sources.

Should there be any ethical boundaries to the information and advice consumer organisations give about taxation? Perhaps it is better to think of the boundaries here in legal rather than ethical terms. There should be no encouragement to consumers to break the law by submitting incorrect or fraudulent tax returns. On the other hand, consumers should be given every help to ensure that they do not pay more taxes than they are legally obliged to.

Consumers need to know the terms and conditions on which a financial service is provided and how much it will cost them. Until recently, this has been a neglected area, certainly so far as some financial services and some countries are concerned. Banks in particular have been reluctant to set out clearly and explicitly the terms and conditions on which they do business with consumers. In France, the situation was so bad that in 1979 the Union Fédérale des Consommateurs (UFC) put forward proposals to the banks and the Government that there should be a "contrat de depot," setting out the rights and responsibilities of the bank and the consumer. This met with little response at the time, but in 1984 the Government introduced legislation requiring banks to set out their charges for their principal services in the form of a notice or leaflet available to the public. Even this was not enough to transform the situation. A check carried out by UFC between six and ten weeks after the new law came into force showed that 229 out of a sample of 278 bank branches visited (82.4%) were not complying with the law (Union Fédérale des Consommateurs, 1985).

In Australia, a report on new payments systems submitted to the Prime Minister by the Australian Science and Technology Council (ASTEC) commented on information about the terms and conditions of use of payments cards that:

Consumers who use the new forms of payment, including EFTPOS, need information to help them use the system correctly, to understand their rights and responsibilities as card-holders, to compare the conditions offered by various financial institutions and to have some indication of the costs of the system in contrast to those of other types of payment in many instances [the financial institutions] failed to meet these information needs (Australian Science and Technology Council, 1986).

The ASTEC report went on to point out that some Australian financial institutions apparently disclosed their terms and conditions *after* the consumer had signed up for a particular service. The Australian Federal Government subsequently (September 1986)

issued guidelines requiring financial institutions issuing payments cards to give the consumer advance written information about charges, conditions of use, procedures for reporting card loss or theft, and procedures for resolving disputes. While these guidelines are at present non-statutory, the Australian Government has warned that they may be given legislative force if financial institutions do not comply with them.

In Denmark, Forbrugerrådet played a vigorous part in lobbying for the passage by Parliament of the Payment Cards Act 1984. This includes significant consumer information provisions. Section 13 requires a financial institution issuing a payment card to give the consumer comprehensive advance information about the terms and conditions, charges, and use of the card.

In Britain, the National Consumer Council (NCC) considers that:

The law may be broadly acceptable, but it is important that customers should know and understand the nature of their relationship with their bank. There is less room for satisfaction here. Customers need to know the main rights and obligations of both parties, as well as other matters such as how charges are calculated, procedures for correcting errors and handling complaints, and so on (National Consumer Council, 1983b).

The NCC opts for explanatory leaflets rather than written contracts or statements of terms and conditions.

Consumers have found it particularly difficult to find out the cost of credit, or to have the cost presented to them in a form which makes it easy for them to make a comparative assessment of the cost of credit from different sources. In Britain, this problem, which was previously acute, has been resolved by the Consumer Credit Act 1974 and the Regulations which have subsequently been made under the Act. One of the principles of the Act is that the cost of credit should always be made clear to prospective borrowers. This is done by setting out detailed definitions of the total cost of credit and of the annual percentage rate of charge (APR). All but the simplest advertisements for credit must include the APR and this enables consumers to make comparative assessments of the cost of credit. It cannot be denied that in the early years since the Act was passed, the results have been disappointing so far as consumers' understanding and use of the APR are concerned. A 1979 NCC survey of a sample of 915 consumers revealed that 61% said they did not understand interest rates. However, the use of APRs is a strategy which will bring benefits to consumers in the long term. In the USA,

lenders have had to disclose their APR since the Truth in Lending Act 1969. Survey research showed that just before the 1969 US Act was passed, only one in seven borrowers had an approximately accurate idea of the APR involved. By 1970, the ratio had risen to one in three and by 1977 to over a half (National Consumer Council, 1980).

On information about credit charges, at least, there is reason for consumer organisations to be cautiously optimistic about future international developments. The European Commission is committed to putting forward proposals for a standardised method of calculating the APR throughout the European Community. If the proposals are eventually adopted by the Council of Ministers, they will enable consumers and consumer organisations to make a comparative assessment of the cost of credit throughout the European Community. However, as it was twelve years before the first Consumer Credit Directive was finally adopted, and then only in an emasculated form, we cannot be too complacent. It may well require considerable pressure, both nationally and at the European level, to achieve success.

Who Should Supply the Information and by What Means?

The above examples illustrate improvements that have been made and that are under consideration in requiring financial institutions to provide consumers with information, particularly about terms and conditions and about charges. They show what can be done, but the requirements vary widely from country to country and from financial service to financial service. The involvement of consumer organisations has been spasmodic. What the examples do suggest, however, is that consumer organisations which are active in providing financial information should identify the specific financial information which the consumer needs and which the financial institution providing the service should be under an obligation to supply.

Every country has a system of company law, one of whose aims is to ensure that investors are given the information they need, information which only the company is able to provide. Why not take this as our model for financial services? Why not work out a set of minimum consumer information requirements for savings and investments, credit, money transfer, insurance, and privately provided pensions?

Given the rapid internationalisation of financial services which is taking place, it would not make sense for each consumer organisation to work separately on such a major initiative. For example, while the legal framework and prudential control system for insurance are very different in, say, Denmark, France, and the United States, consumers' information needs are surely much the same.

If it proved to be possible to develop a common international framework of consumers' minimum information needs about financial services, this could be used as a basis for campaigning either for financial institutions to undertake the provision of such information on a voluntary basis, or for them to be statutorily obliged to do so.

Developing a strategy of the kind outlined would not make the direct financial information role of consumer organisations redundant. On the contrary, it would enhance it. There is much information that it would be impossible or impracticable to ask financial institutions themselves to provide. As well as more general financial advice and information — for example, do you need life insurance? If so, how much? — the “brand comparison” aspect is clearly one which is ideally suited to consumer organisations and one which several have already developed to a sophisticated level. In particular, Verbruikersunie/Association des Consommateurs and Consumers' Association have shown what can be done in this direction. No one should doubt, however, what still remains to be done. Consumer information about the relative performance of different financial institutions is still massively imperfect. In fact, it is sometimes possible to quantify the degree of imperfection of consumer information. For example, a recent Consumers' Association report on life insurance compared the premiums for a 15 year life insurance policy for £30,000. The premiums payable by the consumer to a typical poorly performing company were between 60% and 90% higher than those payable to the best value companies, depending on the age and sex of the consumer (Consumers' Association, 1986b).

The Future Role of Consumer Organisations

Looking to the future role of consumer organisations, the internationalisation of financial services is again crucial. Within the European Community there is now a clear commitment to creating a free internal market in financial services. The obstacles to achieving this have been identified and there is a timetable to remove them by

1992. Even if this proves to be ambitious, there can be little doubt about the direction in which the Community will move and the eventual goal. The long list of planned proposals for directives covers banking, insurance, transactions in securities, and money transfer. In principle, any bank, insurance company, or other financial institution will be free to offer financial services anywhere within the Community providing it complies with the legal and prudential control requirements of its parent country. There is of course some way to go before the stipulated "minimum harmonisation of surveillance standards" is reached which will enable this transformation to come about, but the target is clear (Commission of the European Communities, 1985).

What are the implications of this for consumers in European Community countries? National markets for financial services will partly disappear, and a Community-wide market will emerge. Of course, many financial institutions will continue to operate nationally, regionally or locally, but some will choose to work internationally, either by setting up subsidiaries or branches in other Community countries or by offering services across national frontiers. The consumer will have a wider range of choice and many financial services may well become more competitive.

What are the implications for consumer organisations? Increasingly, they will have to think on a Community-wide basis about the financial services on offer, or even globally. There will be a tendency for identical "brands" of financial services to be on offer throughout the Community, and even elsewhere, though there will always be national variations.

Because of the shortage of resources in the consumer movement, it would again make sense for consumer organisations to pool their expertise in testing and reporting on financial services. The Bureau Europeen des Unions de Consommateurs and the European Testing Group have shown what can be done in relation to product tests and are extending this approach to the assessment of public services — for example, the telephone service. Financial services, however, present a different problem. Despite what has been said about the drive for a free internal market in financial services, the European Community is not necessarily the most appropriate framework for collaborative consumer work in this field. Many innovations in financial services stem from the USA and it is there that the consumer movement has gained considerable experience about

consumers' financial information needs. For the future, we can also look to Japan and the South-East Asian countries that rim the Pacific. Future financial services collaboration between consumer organisations may need to be world-wide and self-selecting, rather than being based on the European Community.

Personalized Financial Advice

Even if initiatives for collaboration between consumer organisations are successful, there will still be an enormous gap in the consumer's need for financial information and advice. What is missing is personally tailored advice designed to fit the individual consumer's own distinctive financial situation. The consumer might want advice of this kind about savings and investments, credit, insurance, pensions, or taxation.

Personal financial advice is available on a commercial basis from financial intermediaries. This kind of advice is a growth industry in many countries and obviously meets a consumer need. However, it is often less than satisfactory. For example, a test of 142 insurance advisers in Britain concluded that their performance was disappointing (Consumers' Association, 1984). The European Consumer Law Group has expressed doubts about the part played by intermediaries in selling credit to consumers, on the grounds that the intermediary has a strong interest in earning commission irrespective of whether the consumer is in a position to meet his or her repayment obligations (European Consumer Law Group, 1986).

Genuinely independent and objective financial advice is hard to find — and expensive to provide. In Britain, rising unemployment and increasing marital breakdown have been the main reasons for a significant rise in the proportion of consumers unable to repay loans (National Consumer Council, 1983). To meet consumers' needs for financial advice in critical circumstances, a number of specialist money advice centres have been set up. Also, trained money advisers are available in some general information and advice centres. However, funding is uncertain and the demand for advice far outweighs the supply.

Both Association des Consommateurs and Consumers' Association have experimented with the use of new information technologies for personal financial advice, in the form of videotex and computer programs. The cost threshold for this mode of conveying advice is at

present high, but the potential is enormous. Looking again to the future, and to the likely spread of interactive cable and other home-based information technologies, the need for consumer organisations to harness new information technologies in order to give personal financial advice is surely self-evident.

Conclusion

A possible future programme for an international collaborative network on financial information and advice would be:

- continuing study of and campaigning for the information obligations that should be accepted by or imposed on financial institutions;
- shared testing programme for internationally available financial services;
- shared experience in developing information technology-based personal financial advice.

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ZUSAMMENFASSUNG

Verbraucherinformation über Finanzdienstleistungen: Eine zukünftige Strategie für Verbraucherorganisationen. Verbraucherentscheidungen in finanziellen Fragen sind

schwieriger, der Informationsbedarf der Konsumenten ist umfassender und komplexer geworden. Da gleichzeitig viele finanzielle Dienstleistungen in internationalem Rahmen angeboten werden, schlägt der Beitrag vor, daß die nationalen Verbraucherorganisationen in internationaler Kooperation den Informationsbedarf der Konsumenten zu finanziellen Fragen erfassen. Außerdem sollte ein Programm zur Prüfung und Bewertung von international angebotenen finanziellen Dienstleistungen entwickelt werden.

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