
Resolution on G20 Action on Financial Consumer Protection

Background

Financial services, their governance and their development, are particularly important to consumers in the EU and US, who rely on financial products and services to facilitate purchases, for savings and investments and to insure against risk. Over the years, however, financial products, such as mortgages, investments, credit cards, small loans and other payment products, have become more complex and potentially risky for consumers. The rapid pace of innovation in the market and the long term nature of many transactions mean that consumers need protection at every level in order to avoid the considerable risks that these services pose.

The financial system also needs those protections to insure its own stability. The financial crisis of the last several years dramatically illustrates that weak consumer protections pose a significant risk to the wider economy. In the words of Sheila Bair, the Chair of the US Federal Deposit Insurance Corporation, *"There can no longer be any doubt about the link between protecting consumers from abusive products and practices and the safety and soundness of the financial system."* Similarly, the January 27, 2011 final report released by the Congressionally mandated Financial Crisis Inquiry Commission (FCIC) concluded that the financial crisis was an "avoidable" disaster caused by widespread failures in government regulation, excessive risk taking by Wall Street and corporate mismanagement.²

TACD has previously expressed its concern at the slow effort of both governments and the financial industry to correct the continuing market failures and recognized the urgent need for them to take action on financial consumer protection, notably in its resolution of June 2009³ and through the subsequent 2010 Ljubljana declaration on consumers and financial services,⁴ to which it is a signatory.

¹ Statement of Sheila C. Bair, Chairman of the Federal Deposit Insurance Corporation, on Modernizing Bank Supervision and Regulation before the US Senate Committee on Banking, Housing and Urban Affairs, March 19, 2009

² FIN. CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES xvii-xxv (2011), *available at* http://c0182732.cdn1.cloudfiles.rackspacecloud.com/fcic_final_report_full.pdf.

³ TACD resolution on financial services regulation June 2009
http://tacd.org/index2.php?option=com_docman&task=doc_view&gid=214&Itemid=40

⁴ Ljubljana declaration on consumers and financial services, May 2010
http://tacd.org/index2.php?option=com_docman&task=doc_view&gid=291&Itemid=40

TACD is continuing its engagement in the field of consumer protection in financial services and will be holding a one-day conference for consumer organizations, government and regulator representatives, as well as other stakeholders, in June 2011 in Brussels. The aim of the conference is to evaluate the new initiatives in the field of financial sector reform and address the unresolved issues and urgent needs for further action.

Building on these initiatives, Consumers International, the global federation of consumer organizations, and its members launched a campaign in late 2010 calling on the Group of 20 to take action to improve consumer protection in financial services. In November 2010, G 20 leaders meeting in South Korea made the following commitment in the Seoul Action Plan⁶:

Enhancing consumer protection: We asked the Financial Stability Board to work in collaboration with the OECD and other international organizations to explore, and report back by the next summit, on options to advance consumer finance protection through informed choice that includes disclosure, transparency and education; protection from fraud, abuse and errors; and recourse and advocacy.

The FSB and OECD are due to present their report to G20 leaders at the summit in France in November 2011.

Additionally the G20 finance ministers at their meeting in February 2011 requested that the FSB and OECD develop common principles on consumer protection in financial services. The French presidency of the G20 has also announced that a high level conference on consumer protection in financial services will be held in October 2011, the results of which would be expected to contribute to the final report.

Recommendations

In the context of the discussions described above, TACD calls on the governments of the US and EU to work with the FSB and OECD to implement the commitment made in the G20 Seoul Action Plan to “report on options to enhance consumer protection” in financial services.

Specifically, the TACD urges the US and EU governments to collaborate with the FSB and OECD to develop a strong set of recommendations drawing on those listed below⁷; support their adoption at national and where appropriate international levels, and establish suitable processes to review their implementation.

1. Information design and disclosure

Consumers should receive clear, sufficient, reliable, comparable and timely information about financial service products. Severe failure to meet these criteria should cause a contract to be voidable. Contracts must include clear up front pricing so that consumers

⁶G-20 Seoul Summit document, Action Plan para 41, G 20 Seoul. 2010

⁷ These recommendations draw on those developed by Consumers International, which are outlined in their publication “Safe, fair and competitive markets in financial services: recommendations for the G20 on the enhancement of consumer protection in financial services”, March 2011.

<http://www.consumersinternational.org/media/669348/cifinancialreport2011.pdf>

can appreciate the cost of the product before becoming obligated to pay. Financial service providers should be responsible for testing the quality and comprehensibility of the information provided, with additional audits conducted by national regulators.

Standard formats (such as Key Information Documents) should be used for the presentation of information about financial service products so that consumers can easily compare products.

2. Contracts, charges and practices

Many financial service products are now so complex that consumers, regulators and even the financial service providers themselves cannot understand them. This complexity needs to be managed and, if necessary, overly complex products should be kept off the market. Regulators should introduce a requirement of comprehensibility and prohibit products that are not comprehensible. They should require the availability of simple standard financial service products, and key financial service products should be required to meet minimum standards of consumer protection.

Conflict of interest in the provision of advice and sale of financial services needs to be addressed. Commissions and related charges must be fair in amount and be made transparent at an early stage. Financial advice to consumers should be subject to a fiduciary duty to act in the customer's best interests. . Advisers should seek to minimize, appropriately manage, and fully disclose any conflicts of interest. Disclosure of conflicts should occur at a time that enables the consumer to make an informed choice among advisers.

Additionally, there should be protection against inappropriate marketing methods. The following practices should be cause for appropriate sanctions, including in the most egregious cases, for a contract to be voidable:

- failure to gain the informed consent of the consumer
- unfair or unreasonable fees and costs charged to consumers and included in consumer contracts for financial services products
- clauses in financial service contracts that result in consumers' waiving core consumer protections, and
- the sale of financial services that are unsuitable for the consumer.

3. The structure and functions of national financial consumer protection bodies

Under the UN guidelines for consumer protection, all governments have a responsibility to protect and promote consumer rights.⁸ Governments should each establish a national body that has consumer protection as an explicit regulatory objective with full authority to investigate, halt and remedy violations of consumer protection law, including where necessary the right to define specific practices or products as unfair, deceptive or otherwise illegal.

The body should have effective regulatory power over every financial institution, product and provider and, in response to a serious failure to abide by consumer protection rules, it should have the power to remove an institution's license or, in response to lesser

⁸ *UN Guidelines for Consumer Protection* Adopted 1985, expanded 1999, re-adopted in General Assembly decision 54/449 ; UN 2003

abuses, impose penalties sufficient to discourage repetition. The body should have sufficient funding and resources to conduct the tasks assigned to it.

The body should be independent of the industry, free from conflicts of interest and include a balance of members with industry and consumer expertise and include staff with broad knowledge and expertise. It should be transparent and should clearly publicize occasions where it has taken action against specific practices and products or misleading financial promotions either industry wide or against specific firms. Reputational regulation should be initiated to allow consumers to choose providers based on firms' record of treating customers fairly. There should be strong links with other consumer protection bodies (including representatives of consumers) to ensure that experience and expertise in consumer protection is shared. Representatives of the consumer interest should be integrated into the governance of the sector at national level. Consumer organizations should have a right to initiate a formal procedure at the consumer protection agency if they have arguments and cases for a serious consumer detriment / provider misconduct aimed at a multitude of consumers.

4. International Trade Agreements Should not Undermine Financial Regulation

Financial services strictures under the World Trade Organization (WTO) and other international trade agreements could undermine financial regulation. Financial Transaction Taxes (FTT), capital controls, bans on risky financial services and size limits on banks are some of the policies at risk as provisions of the WTO General Agreement on Trade in Services (GATS) prohibits whole categories of regulation in committed services sectors.

Unless WTO limits on non-discriminatory financial regulations are removed and/or a meaningful safeguard for prudential measures is inserted, U.S. and EU governments should lead the G20 in halting further demands for more WTO financial services liberalization in the Doha Round.

5. Redress and dispute resolution systems

Access to dispute resolution and redress is one of the eight consumer rights. Still, there is a serious risk that such systems are absent, not acting independently and neutrally, or being overwhelmed by the sheer number of complaints relating to financial services. This underlines the importance of preventing complaints arising through the introduction of effective upstream consumer protection.

Governments should ensure that consumers have access to adequate redress mechanisms, which are "expeditious, fair, inexpensive and accessible."⁹ Ideally, there should be one clearly identifiable scheme for redress per sector. Consumers should be proactively informed about the availability of such a system. Governments should also provide collective redress mechanisms in order to reduce the demand for individual proceedings.

Findings from these redress mechanisms should be synthesized and reported to regulators in order to inform future regulation and enforcement.

6. Promoting competition in financial services

⁹ UN Guidelines *op cit.* Art 32

The financial crisis led to a significant reduction in competition in the financial services sector, which was already suffering from a high level of market concentration. Competition is an important consumer issue, and TACD strongly recommends that the G20 take action to promote competition on terms that enhance consumer protection in financial services.

The G20 should recognize that it is counterproductive to allow competition law to be overridden in the interests of financial stability, as it results in the creation of even larger institutions and increases the probability of taxpayers' needing to provide support in the future. In addition, steps to support financial institutions which are "too big to fail" can distort competition.

The G20 should therefore encourage member countries to instigate independent competition inquiries into the increases in concentration and reduction of competition caused by the financial crisis and recommend that national governments apply 'public interest tests' to the disposal of their stakes in the banking sector. This should include specific objectives to make competition stronger after disposal of the stakes so that some of the increase in concentration is reversed.

Additionally, to encourage new entrants, governments and regulators should take steps, such as those pertaining to comparability of products, portability of account numbers and others, to ease switching of accounts for consumers. Finally, regulators should encourage '*reputational regulation*' by publishing details of complaint numbers, compensation and enforcement action so consumers can choose a provider of retail financial products based on their track record.

7. Measures to promote stability and safety of consumers' deposits and investments

The financial crisis dramatically highlighted how new banking practices are exposing consumers to enormous risk. Rather than manage risk, the structure and practices of the financial services sector magnified risks to a level that threatened the collapse of the sector itself.

TACD urges the US and EU to support a G20 leader agreement to use leverage control to reduce risky activity rather than starve consumers and businesses of access to credit. These measures should be complemented with the use of non-operating holding company (NOHC) structures to address contagion and counterparty risk directly, including maintaining demarcation between investment banking and retail banking reducing risk of cross-contamination through legal separation of operations. Living wills for financial entities should be introduced and should contain provisions for the treatment of customers so that financial institutions can fail without causing catastrophic damage to consumers or the economy.

Credit ratings agencies should be liable for the validity of their analyses and should be answerable to prudential supervisors. In particular it is necessary to purge the conflicts of interest between the carrying out of analyses by these agencies and the subsequent public reports on the one hand, and, on the other, payment by financial services providers for an evaluation which will have an impact on the value of those same businesses. The agencies need to move more to a role of independent auditing as is customary for businesses in many jurisdictions, so that the auditors themselves have a public responsibility for the validity of their reports.

Greater transparency and accountability in financial transactions will also help to reduce risk. Actions should include developing systems to assess consumers' capacity to take on financial commitments, giving consumers access to risk data regarding individual financial service providers and ensuring that loan assignees should be liable for the practice of the original credit granter.

Deposit protection schemes should provide cover for each separate brand and create a seamless transition of essential banking services with consumers maintaining access to deposits used for transactional banking. Any payment from the protection scheme regarding deposits held in savings accounts should be made within seven days. Measures should also be introduced to provide flexible cover for temporary high balances.

And insolvency procedures should be reformed so that the rank of creditors is changed to put depositors at the top.

8. Access to basic financial services and the role of new forms of service

Universal access to free or affordable basic financial services should be a specific aim of government policy on financial services. New innovations and technologies are already making great strides in this area, increasing access but also raising new challenges for consumer protection. Governments should seek to encourage innovation in safe, effective, low cost methods for banking inclusion whilst supporting the development of consumer protection.

With regard to the important issue of remittances, the EU and US should support G20 development of the General Principle on Remittances (2007) with a view to introducing a stronger consumer orientation, with consumer protection as a primary objective.

9. Conclusion: ongoing international co-operation on financial consumer protection including reviews of implementation

There is now an urgent need for stronger international co-operation on financial consumer protection. The financial crisis showed that weak consumer protection in one country can pose a risk to other countries and the global dimension of financial services means that financial market conduct regulators around the world now face similar issues and challenges.

The G20 should therefore support the establishment of a permanent international organization to enable national financial consumer protection bodies to compare notes, share good practice and develop minimum international standards and guidelines based on the recommendations in this report, and review their implementation. The new organization should have consultative status with other international financial regulatory bodies and actively co-operate with these organizations and consumer organizations in the development of research, institutional capacity, guidelines and agreements, fraud monitoring and scrutiny of industry practices.

The new organization should have a network structure with representatives from national financial consumer protection bodies and the resources to establish a Secretariat. An independent consumer panel should also be established made up of representatives from independent consumer organizations with competence in financial consumer protection to monitor advise and challenge the work of the organization.