

MARKETS IN MOTION

developments that matter in financial markets

Consumer Protection in Mature Financial Markets

"The challenge faced by regulators is to strike the right balance: to strive for the highest standards of consumer protection without eliminating the beneficial effects of responsible innovation on consumer choice and access to credit."

Ben S Bernanke, Chairman, Federal Reserve, US

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Introduction

A majority of consumers lack the required knowledge to evaluate and make decisions about products and services, particularly in financial markets. They are not equipped with adequate knowledge to assess complex products and their financial implications, which often lead to misguided decisions.

In the aftermath of the financial crisis, the financial market regulators have initiated steps on consumer protection to ensure that investors receive information ex ante that will allow them to make informed decisions and are not subject to hidden cost and risky surprises.

United States

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act was passed in the US, which paved the way for the establishment of the Consumer Financial Protection Agency (CFPA). The CFPA would serve as an independent regulator with broad authority over "any financial product or service" used by consumers. The principal objectives of the CFPA are to ensure that consumers of financial products and services have access to, and can utilize, the information that is necessary to make responsible financial decisions, while simultaneously protecting them from abusive, deceptive, and discriminatory practices. The goal of the new agency is to guarantee that markets for such products "operate fairly and efficiently with ample room for sustainable growth and innovation". The CFPA would have sole authority to promulgate and interpret existing and future consumer financial regulations. The CFPA would also assume all responsibilities regarding the supervision of banking institutions for consumer regulatory compliance.

United Kingdom

The UK government has proposed to set up Consumer Protection and Markets Authority (CPMA) that will take on the responsibility for consumer protection and conduct regulation. The CPMA will regulate the conduct of all firms, both retail and wholesale, and will take a proactive role as a strong consumer champion. The CPMA will oversee the newly created Consumer Financial Education Body (CFEB), which will play a key role in improving financial literacy.

Australia

Australia has enacted a new national law, the Australian Consumer Law (ACL), on March 17, 2010. Broadly, the ACL stipulates civil pecuniary penalties for contravention of certain consumer protection provisions, prohibits unfair contract terms in standardized form, and introduces

new enforcement powers for the Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC). The objective is to improve consumer well being through consumer empowerment and protection, foster effective competition, and enable the confident participation of consumers in markets in which both consumers and suppliers trade fairly.

Best Practices

- Consumers should receive a single-page Key Facts Statement about the financial product.
- Financial institutions should ensure that the product or service is appropriate to the consumer.
- Financial products with a long-term savings component should have a cooling-off period when the consumer may cancel the contract without penalty.
- Whenever a consumer is obliged to purchase any product as a pre-condition for receiving another product from the financial institution, he should be free to choose the product provider.

Canada

The Financial Consumer Agency of Canada (FCAC) has been set up to ensure compliance with the consumer protection laws and monitors compliance with the codes of conduct and public commitments that apply to banks, federally incorporated trusts, and loan and insurance companies. The FCAC also provides consumers with accurate and objective information about financial products and services and informs Canadians of their rights and responsibilities when dealing with federally regulated financial institutions.

Conclusion

The basic tenet of consumer financial services regulation is that the market is the best guarantor of consumer protection.

However, the recent financial crisis caused by some financial institutions has forced the regulators to tighten the disclosure practices of the institutions and make them provide specific information for a better market discipline.

If all material information is readily available to consumers in a form that can be easily processed, then the consumers will be able to make intelligent, informed decisions, which will maximize consumer welfare and discipline product offerings.

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