NAIC 2023 FALL NATIONAL MEETING ORLANDO

Draft: 11/14/2023

2023 Fall National Meeting
Orlando, Florida

Life Insurance and Annuities (A) Committee
Sunday, December 3, 2023
9:30 – 10:30 a.m.
Hilton Orlando Bonnet Creek—Floridian Ballroom A–I—Level 1

ROLL CALL

Judith L. French, Chair	Ohio	Eric Dunning	Nebraska
Carter Lawrence, Vice Chair	Tennessee	Scott Kipper	Nevada
Mark Fowler	Alabama	Justin Zimmerman	New Jersey
Barbara D. Richardson	Arizona	Adrienne A. Harris	New York
Karima M. Woods	District of Columbia	Glen Mulready	Oklahoma
Doug Ommen	Iowa	Scott A. White	Virginia
Vicki Schmidt	Kansas	Nathan Houdek	Wisconsin
James J. Donelon	Louisiana		

NAIC Support Staff: Jennifer R. Cook/Jolie H. Matthews

AGENDA

1. Consider Adoption of its Nov. 21 Minutes —*Director Judith L. French (OH)* — Attachment One

2. Consider Adoption of the Report of the Life Actuarial (A) Task Force

3. Hear a Federal Update on the Proposed Retirement Security Rule: Definition of an Investment Advice Fiduciary—Taylor Walker (NAIC)
   A. Hear Brief Comments from Interested Parties

4. Hear a Presentation on Consumer Financial Literacy vs. Life Insurance and Annuities Illustrations —*Birny Birnbaum (Center for Economic Justice—CEJ) and Brenda J. Cude (University of Georgia)* — Attachment Two

5. Discuss Any Other Matters Brought Before the Committee —*Director Judith L. French (OH)*

©2023 National Association of Insurance Commissioners

Agenda Item #1

Consider Adoption of its Nov 21 Meeting Minutes

Draft: 11/28/23

Life Insurance and Annuities (A) Committee
Virtual Meeting
November 21, 2023

The Life Insurance and Annuities (A) Committee met Nov. 21, 2023. The following Committee members participated: Carter Lawrence, Chair (TN); Barbara D. Richardson (AZ); Mark Fowler (AL); Karima M. Woods represented by Philip Barlow (DC); Doug Ommen (IA); Vicki Schmidt represented by Julie Holmes and Craig VanAalst (KS); James J. Donelon represented by Tom Travis (LA); Eric Dunning represented by Adam Clayton (NE); Justin Zimmerman (NJ); Scott Kipper (NV); Adrienne A. Harris represented by Bill Carmello and Mark McLeod (NY); Judith L. French represented by Daniel Bradford (OH); Scott A. White represented by Craig Chupp (VA); and Nathan Houdek represented by Lauren Van Buren (WI). Also participating was: Rachel Hemphill (TX).

1. Adopted its Summer National Meeting Minutes

Commissioner White made a motion, seconded by Commissioner Kipper, to adopt the Committee's Aug. 15 (*see NAIC Proceedings – Summer 2023, Life Insurance and Annuities (A) Committee*) minutes. The motion passed unanimously.

2. Adopted the 2024 GRET

Hemphill explained that the Society of Actuaries (SOA) provided the Life Actuarial (A) Task Force with the annual update to the Generally Recognized Expense Table (GRET). She said no concerns were raised with the SOA updates, and the Task Force unanimously adopted the updated 2024 GRET on Sept. 8.

Travis made a motion, seconded by Commissioner Zimmerman, to adopt the 2024 GRET (*see NAIC Proceedings – Fall 2023, Executive (EX) Committee and Plenary, Attachment _*). The motion passed unanimously.

3. Adopted the Life Actuarial (A) Task Force's 2024 Proposed Charges

Hemphill explained that the Task Force made one minor revision to its 2023 charges for 2024, removing a charge that had been completed: *Evaluate and provide recommendations regarding the VM-21, Requirements for Principle-Based Reserves for Variable Annuities/Actuarial Guideline XLIII—CARVM for Variable Annuities (AG 43) standard projection amount (SPA), which may include continuing as a required floor or providing as disclosure. This evaluation is to be completed prior to year-end 2023.* She said that ongoing maintenance and considerations regarding VM-21's SPA will continue to be part of the Task Force's Charge A: *Work to keep reserve, reporting, and other actuarial-related requirements current. This includes principle-based reserving (PBR) and other requirements in the Valuation Manual, actuarial guidelines, and recommendations for appropriate actuarial reporting in blanks. Respond to charges from the Life Insurance and Annuities (A) Committee and referrals from other groups or committees, as appropriate.* Hemphill said no concerns were raised with the update, and the Task Force adopted its 2024 proposed charges on Oct. 10.

Travis made a motion, seconded by Commissioner White, to adopt the Life Actuarial (A) Task Force's 2024 Proposed Charges (*see NAIC Proceedings – Fall 2023, Executive (EX) Committee and Plenary, Attachment _*). The motion passed unanimously.

4. Adopted its 2024 Proposed Charges

Commissioner Lawrence explained that the Committee's 2024 proposed charges are the same as last year.

Commissioner Ommen made a motion, seconded by Van Buren, to adopt the Committee's 2024 proposed charges (*see NAIC Proceedings – Fall 2023, Executive (EX) Committee and Plenary, Attachment _*). The motion passed unanimously.

5. Gave an Update on Fall National Meeting Agenda

Commissioner Lawrence said that a federal update on the U.S. Department of Labor's (DOL's) proposed "Retirement Security Rule: Definition of an Investment Advice Fiduciary" is on the agenda for the Committee's upcoming meeting on Dec. 3 at the Fall National Meeting. He asked interested parties who would like to make brief comments after the update to please email Jennifer Cook (NAIC). Commissioner Lawrence said that also on the agenda is a presentation by Birny Birnbaum (Center for Economic Justice—CEJ) and Brenda J. Cude (University of Georgia) to talk about financial literacy from the consumer perspective, and he wants to ensure there is enough time on the agenda.

Having no further business, the Life Insurance and Annuities (A) Committee adjourned.

SharePoint/NAIC Support Staff Hub/Member Meetings/A Cmte/2023 Fall National Meeting/11-21-22 ACmte min

© 2023 National Association of Insurance Commissioners

Agenda Item #2

Consider Adoption of the Report of the Life Actuarial (A) Task Force
--Rachel Hemphill (TX)

2023 Fall National Meeting
Orlando, Florida

LIFE ACTUARIAL (A) TASK FORCE
Wednesday, November 29, 2023
8:00 a.m. – 4:30 p.m.

Thursday, November 30, 2023
8:00 a.m. – 11:00 a.m.

Meeting Summary Report

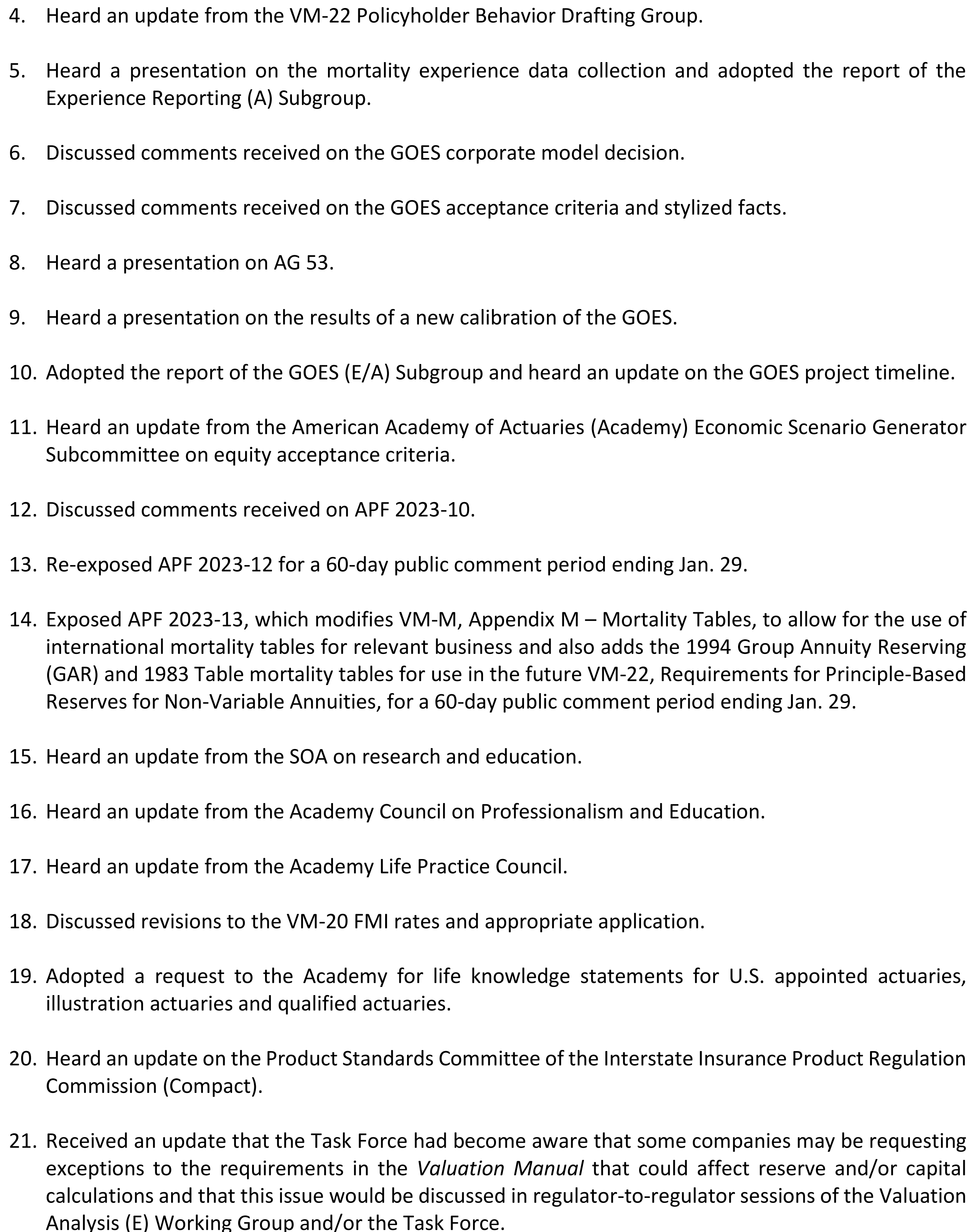
The Life Actuarial (A) Task Force met Nov. 29–30, 2023. During this meeting, the Task Force:

1. Adopted its Nov. 2, Oct.11, Oct. 5, Sept. 28, Sept. 14, and Aug. 31 minutes, which included the following action:
   A. Adopted its Summer National Meeting Minutes.
   B. Exposed amendment proposal form (APF) 2023-11, which removes references to risk-based capital (RBC) from the *Valuation Manual* that are inconsistent with the purpose, scope, and intended use of RBC.
   C. Exposed APF 2023-12, which clarifies expectations for the reflection of equity return volatility in asset adequacy testing (AAT).
   D. Adopted the 2024 Generally Recognized Expense Tables (GRET).
   E. Exposed APF 2023-10, which would change the discount rate for the stochastic reserve in Valuation Manual (VM)-20, Requirements for Principle-Based Reserves for Life Products, to be the net asset earned rate (NAER).
   F. Adopted the Task Force's 2024 proposed charges.
   G. Adopted APF 2023-09, which requires the use of historical mortality improvement (HMI) for company mortality experience in VM-20.
   H. Exposed acceptance criteria and stylized facts for the generator of economic scenarios (GOES).
   I. Adopted a memorandum directed to the Society of Actuaries (SOA) regarding the changes to the SOA's educational pathway.
   J. Adopted APF 2023-08, which clarified the treatment of interest maintenance reserves (IMR) in the *Valuation Manual* along with an IMR template and temporary guidance.
   K. Adopted the *Actuarial Guideline LIII—Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves* (AG 53) templates for year-end 2023.
   L. Adopted the 2023 VM-20 HMI and future mortality improvement (FMI) rates.

2. Adopted the reports of the Longevity Risk (E/A) Subgroup, the Variable Annuities Capital and Reserve (E/A) Subgroup, and the Indexed Universal Life (IUL) Illustration (A) Subgroup.

3. Adopted the report of the VM-22 (A) Subgroup, including its Nov. 15 and Nov. 8 minutes. During these meetings, the Subgroup took the following action:
   A. Exposed the draft VM-31, PBR Actuarial Report Requirements for Business Subject to a Principle-Based Valuation.

© 2023 National Association of Insurance Commissioners



4. Heard an update from the VM-22 Policyholder Behavior Drafting Group.

5. Heard a presentation on the mortality experience data collection and adopted the report of the Experience Reporting (A) Subgroup.

6. Discussed comments received on the GOES corporate model decision.

7. Discussed comments received on the GOES acceptance criteria and stylized facts.

8. Heard a presentation on AG 53.

9. Heard a presentation on the results of a new calibration of the GOES.

10. Adopted the report of the GOES (E/A) Subgroup and heard an update on the GOES project timeline.

11. Heard an update from the American Academy of Actuaries (Academy) Economic Scenario Generator Subcommittee on equity acceptance criteria.

12. Discussed comments received on APF 2023-10.

13. Re-exposed APF 2023-12 for a 60-day public comment period ending Jan. 29.

14. Exposed APF 2023-13, which modifies VM-M, Appendix M – Mortality Tables, to allow for the use of international mortality tables for relevant business and also adds the 1994 Group Annuity Reserving (GAR) and 1983 Table mortality tables for use in the future VM-22, Requirements for Principle-Based Reserves for Non-Variable Annuities, for a 60-day public comment period ending Jan. 29.

15. Heard an update from the SOA on research and education.

16. Heard an update from the Academy Council on Professionalism and Education.

17. Heard an update from the Academy Life Practice Council.

18. Discussed revisions to the VM-20 FMI rates and appropriate application.

19. Adopted a request to the Academy for life knowledge statements for U.S. appointed actuaries, illustration actuaries and qualified actuaries.

20. Heard an update on the Product Standards Committee of the Interstate Insurance Product Regulation Commission (Compact).

21. Received an update that the Task Force had become aware that some companies may be requesting exceptions to the requirements in the *Valuation Manual* that could affect reserve and/or capital calculations and that this issue would be discussed in regulator-to-regulator sessions of the Valuation Analysis (E) Working Group and/or the Task Force.

© 2023 National Association of Insurance Commissioners

Agenda Item #3

Hear a Federal Update on the Proposed Retirement Security Rule: Definition of an Investment Advice Fiduciary —Taylor Walker (NAIC)

A. Hear Brief Comments from Interested Parties

NAIFA link - https://lifehappens.org/videos/paradise-found/

Agenda Item #4

Hear a Presentation on Consumer Financial Literacy vs. Life Insurance and Annuities Illustrations

—Birny Birnbaum (Center for Economic Justice—CEJ) and Brenda J. Cude (University of Georgia)

Consumer Financial Literacy vs. Illustrations for Life Insurance and Annuities

NAIC (A) Life Insurance and Annuities Committee

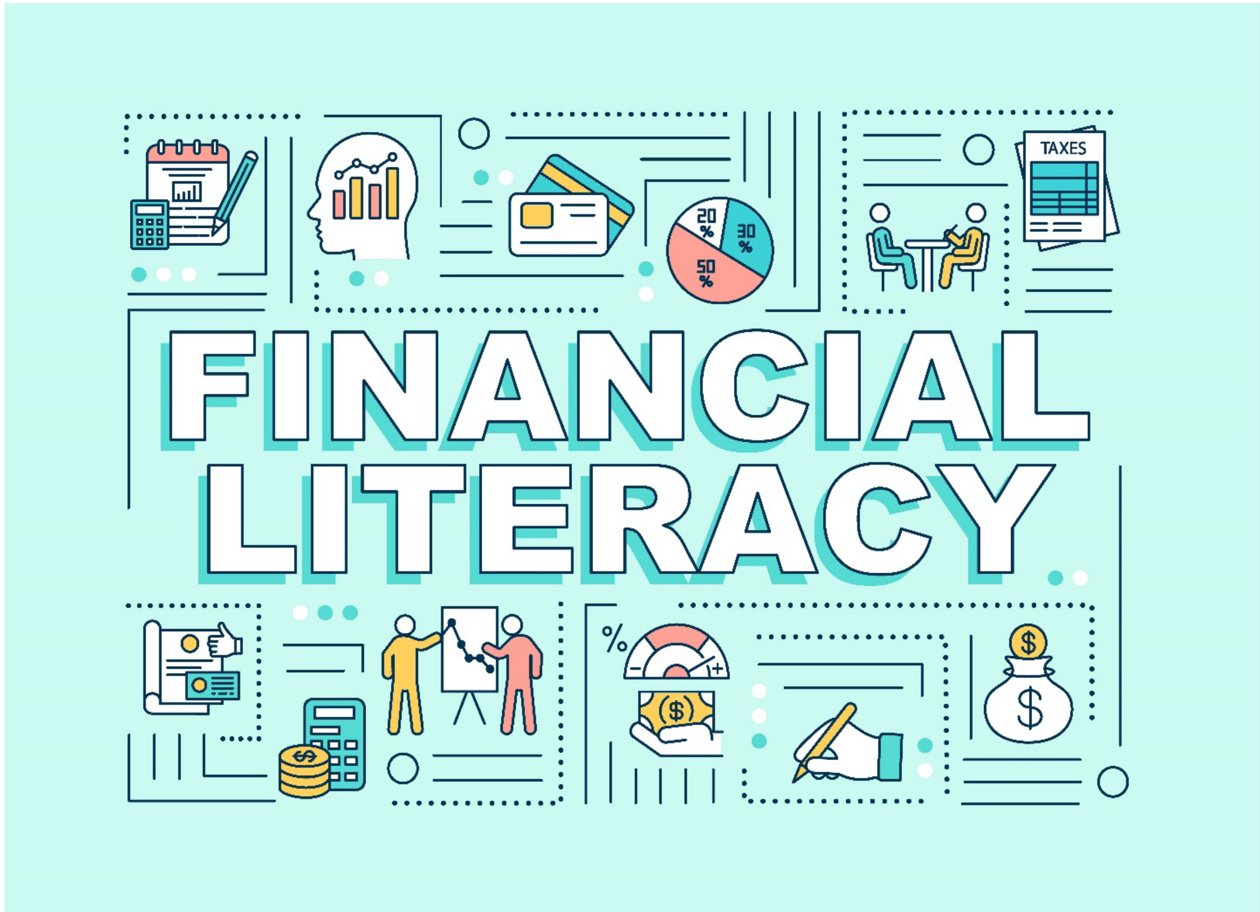
Birny Birnbaum
NAIC Consumer Representative
Center for Economic Justice

Brenda J. Cude, PhD
NAIC Consumer Representative
University of Georgia

December 2023

Resources for Regulators

- Examples of illustrations for indexed life insurance and annuity products;
- A study, referenced in the presentation, from Australian Securities and Insurance Commission and the Dutch Authority for Financial Markets regarding consumer protection and complex financial products.
- *Life Products Review 375: Engineered Indices and Fixed Indexed Annuities*
- Concepts for Consumer Testing of Re-engineered Illustrations from the Center for Economic Justice



Financial Literacy

- Financial literacy is what people
  - Think,
  - Know, and
  - Do about money
- Supports financial life goals
- Makes people less vulnerable to fraud and deception

Consumers are NOT financially knowledgeable

- Worldwide, just one in three consumers are financially literate
- In the U.S, just 55% are financially literate

Suppose you had $100 in a savings account and the interest rate was 2% per year. After 5 years, how much do you think you would have in the account if you left the money to grow?

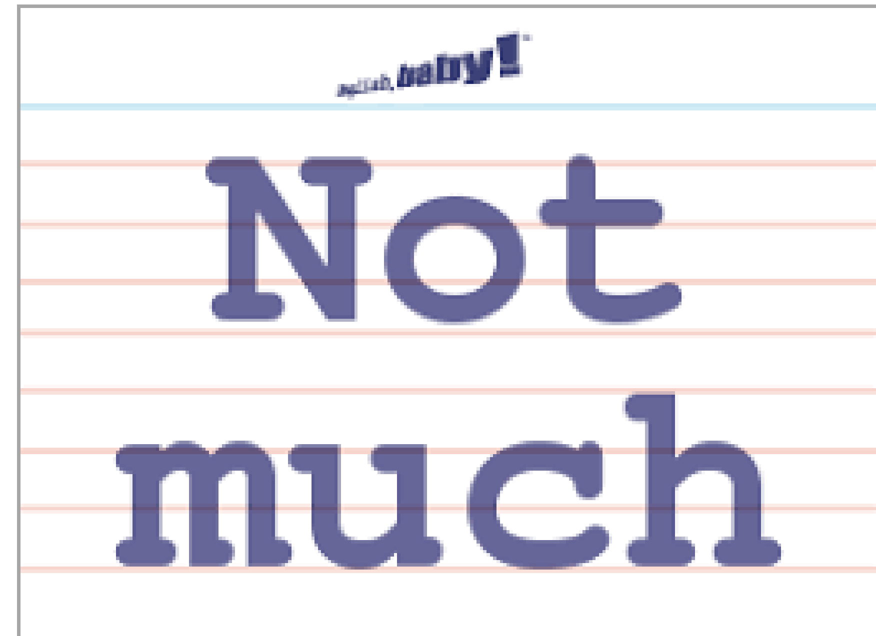
- A) More than $102
- B) Exactly $102
- C) Less than $102
- D) Don’t know
- E) Prefer not to say

How is financial knowledge assessed?

- Usually multiple choice or true/false questions about basic concepts
  - Inflation
  - Compound interest
  - Risk diversification

What do consumers know about investing, insurance, assessing risk?

	Gen Z	Baby Boomers	Silent Generation
Borrowing	47%	64%	61%
Saving	47%	59%	58%
Investing	33%	49%	50%
Insuring	26%	50%	55%
Comprehending risk	32%	36%	36%



Why aren’t people more financially literate?

- It isn’t taught or isn’t taught effectively or taught when the content is relevant
- Products are complex and making decisions about them is complex
- It’s hard to sort through misleading, deceptive, and irrelevant information
- Cognitive biases lead people, even those who are financially literate, to make poor choices

Disclosures Cannot Replace Other Market Regulation

- Disclosures are appropriate only when the problem is information asymmetry
- Disclosures may not improve consumer decision-making and can even backfire
- Disclosures can place an unfair burden on consumers
- Real-world testing and monitoring are necessary to ensure success

Limitations of Disclosures to Empower Consumers

"Disclosure: Why It Shouldn't Be the Default" – a report by ASIC and AFN – the Australian and Dutch Financial Service Regulators:

"Financial services disclosure has traditionally been assumed to inform us (as consumers), help us make 'good' financial decisions, and drive competition.

"This report focuses on the real-world context in which disclosure operates. It shows that, and explains why, disclosure and warnings can be less effective than expected, or even ineffective, in influencing consumer behaviour. In some instances it shows that disclosure and warnings can backfire, contributing to consumer harm."

The Challenge of Retirement Security

- Balancing current and future needs
- Assessing unknown future needs
- Assessing risk tolerance and unknown future risks
- Identifying ways to meet goals and trusted professionals who can help
- Sorting through information vs. marketing
- And often without the security of an employer pension

NAIC Illustration Model Regulations

- "The purpose of [the Life Insurance Illustrations Model Regulation] is to provide rules for life insurance policy illustrations that will **protect consumers and foster consumer education**. . . . The goals of this regulation are to ensure that illustrations **do not mislead** purchasers of life insurance and to **make illustrations more understandable**. Insurers will, as far as possible, eliminate the use of footnotes and caveats and define terms used in the illustration **in language that would be understood by a typical person** within the segment of the public to which the illustration is directed."
- "The purpose of [the Annuity Disclosure Model Regulation] is to provide standards for the disclosure of certain minimum information about annuity contracts to **protect consumers and foster consumer education**. . . . The goal of this regulation is to ensure that purchasers of annuity **contracts understand certain basic features** of annuity contracts."

To use a complicated product like an illustration

Think	Know	Do
Important to plan for the future	What is annuity What is indexed annuity How to get income When to get income What an index is How indices are different How much I need to buy one	Find a trusted advisor
Indexed annuity is good choice	What are the fees What is guaranteed What are the risks What is the surrender period	Determine how annuity fits plan
Worth it to give up time & money now	Potential for return Accumulation period Other options? How choices affect fees, returns, etc. What is prospectus What is illustration	Commit to future

- Consumers need
  - Literacy
  - Financial knowledge
  - Numeracy
  - Document literacy

Examples of Illustrations

Attached are examples of four illustrations for fixed indexed annuities – how well do they meet the purposes and goals of the illustrations models?

Cognitive Biases and Risk Assessment

Introduced by Twersky and Kahneman in 1972, cognitive biases describe systematic errors in thinking that affect decisions and judgments. Bias examples include Anchoring, Attentional, Availabiity, Confirmation and Overconfidence Biases.

Howard Kunreuther studied behavioral biases in risk assessment, including Myopia, Amnesia, Optimism, Inertia, Simplification and Herding.

Some cognitive biases make consumer particularly susceptible to unrealistic or deceptive illustrations.

Deceptive and Misleading Presentation

“FIA illustrations operate under the same basic illustration framework as Indexed UL. Both use a hypothetical historical lookback methodology that applies currently declared “interest crediting adjustments” to historical index return data.

“The fundamental problem with this hypothetical lookback methodology is that it can be easily gamed because the data is already known. All you have to do is optimize an index or a crediting strategy to back-fit the data if you want to increase illustrated performance.

Deceptive and Misleading Presentation

“Life insurers have become exceedingly adept at maximizing illustrated performance in their FIA products using engineered indices. There are now 165+ engineered indices in market that permeate virtually every FIA product. . . . the chief attraction for engineered indices is that they deliver the holy grail of indexed crediting - cheap options and high backtested performance. Put those two things together and you get 100%+ participation rates and colossal illustrated performance. It’s the stuff sales people dream of.

Deceptive and Misleading Presentation

The combination of engineered indices, multi-year crediting strategies and fee-for-rate designs have pushed illustrated returns on FIAs into the stratosphere. There are around 550 accounts available in FIA products that illustrate more than 10%."

See the chart on page 3 of "Engineered Indexes and FIAs" showing illustration annual crediting rates of 14% to 33% for the majority of top FIA writers.

See page 7 of ACL Accumulation Protector Plus illustration example – a $100,000 premium grows to $877,000 index account value in ten years – compounded average annual returns of 24.2%

Deceptive and Misleading Presentation

- As high as those average returns are, the more insidious problem with the best/worst/most recent 10 year illustration construct is what happens on the worst-10 side of the ledger. Engineered indices are optimized to deliver not just lights-out illustrated performance from the most recent 10 year period but also to maintain high returns in the worst-10 scenario. . . . Carriers, agents and distributors play this up as a “can’t lose” sort of situation where the “worst case” scenario is still double-digit returns. That is a fundamentally misleading characterization that, in my experience, seems to sometimes be a key part of the sales process.

The Path Forward

Re-engineer illustrations regulations for a consistent approach for indexed annuities and life insurance:

Stop the incentives for illustration / unrealistic accumulation competition: Eliminate hypothetical historical results and projections of non-guaranteed outcomes – these two actions will also eliminate insurance producers acting as financial planners without the training or qualifications to do so.

Improve the content and presentation: Use consumer testing to provide simplified information about product fees and performance, such as how frequently and by how much the insurer changes product features

How can illustrations be useful?

- Use a consumer decision-making design focus
- Use iterative consumer testing

Questions? Reach out

Birny Birnbaum
NAIC Consumer Representative
Center for Economic Justice

Brenda J. Cude, PhD
NAIC Consumer Representative
University of Georgia

Re-Engineering Life and Annuity Illustrations and Disclosures for Consumer Protection and Fair Competition

December 3, 2023

Birny Birnbaum
Center for Economic Justice

NAIC Models Related to Life and Annuity Illustrations and Marketing

The NAIC has several model regulations and actuarial guidelines regarding life and annuity illustrations, disclosures and advertising.

NAIC Life Insurance Illustrations Model Regulation

Purpose: The purpose of this regulation is to provide rules for life insurance policy illustrations that will protect consumers and foster consumer education.

The goals of this regulation are to ensure that illustrations do not mislead purchasers of life insurance and to make illustrations more understandable. Insurers will, as far as possible, eliminate the use of footnotes and caveats and define terms used in the illustration in language that would be understood by a typical person within the segment of the public to which the illustration is directed.

NAIC Life Insurance Disclosure Model Regulation

Purpose: The purpose of this regulation is to require insurers to deliver to purchasers of life insurance information that will improve the buyer's ability to select the most appropriate plan of life insurance for the buyer's needs and improve the buyer's understanding of the basic features of the policy that has been purchased or is under consideration.

NAIC Annuity Disclosure Model Regulation

Purpose: The purpose of this regulation is to provide standards for the disclosure of certain minimum information about annuity contracts to protect consumers and foster consumer education.

The goal of this regulation is to ensure that purchasers of annuity contracts understand certain basic features of annuity contracts.

Advertisements of Life Insurance and Annuities Model Regulation

Purpose: The purpose of this regulation is to set forth minimum standards and guidelines to assure a full and truthful disclosure to the public of all material and relevant information in the advertising of life insurance policies and annuity contracts.

Actuarial Guidelines 49, 49A and 49B for Indexed Universal Life illustrations.

Provides guidance in determining the maximum crediting rate for the illustrated scale and the earned interest rate for the disciplined current scale.

Limits the policy loan leverage shown in an illustration.

Requires additional consumer information (side-by-side illustration and additional disclosures) that will aid in consumer understanding.

Current Insurer Marketing and Illustration of Indexed Life and Annuities Fails to Meet the Purposes of These Models

Illustrations obscure, instead of explain, the operation of the policy or contract.

Illustrations and advertisements present misleading information about risk and return.

Illustrations create unrealistic expectations for consumers about policy accumulation values.

Products and related illustrations are relying more and more on the use of custom indexes produced by data mining historical results resulting in:

- Backtesting, not permitted for any other type of investment product, based on hypothetical results before the index was created; and
- Conflicts of interest created when the provider of the index is also providing the hedging program to support the insurers' products.

Current Insurer Marketing and Illustration of Investment-Type Life and Annuities Fails to Meet the Purposes of These Models

Competition among insurers is focused on product design to game illustration rules, instead of competition to provide consumer value and understanding

Projections, not permitted for any other type of investment product, for 20, 30, 40 and 50 years showing constant annual returns

Misleading premium financed product illustrations showing riskless arbitrage

Annual rates of return untethered to actual market conditions

Producers acting as de facto financial planners.

Bottom Line: Setting unrealistic expectations, ensuring future consumer complaints and lawsuits and creating retirement insecurity.

Illustration Re-engineering Concepts

<u>The Illustration</u>

Simpler Explanation about How the Product Operates

Apples to Apples Comparison of Product Accumulation with Alternative Investments

Show Insurer Performance for Key Product Features like Changes in Caps/Floors and Expense Features

Show the Cost and Value of Insurance

Show Meaningful Measures of Risk and Return

Set Realistic Expectations for Policyholders

Illustration Re-engineering Concepts

Consumer Protections and Fair Competition

Prohibit Hypothetical Index History / Results for Illustrations

Prohibit Hypothetical Future Accumulation

Discourage Illustration Competition / Product Design to Juice Illustrations

Prohibit Index Providers from Providing the Hedging Program to Support the Product Using That Index.

Prohibit Indexes That Are Not Transparent and Allow the Consumer to Independently Verify the Stated Results.

Create Consistent Illustration Requirements for Indexed Annuities and Life Insurance

Provide Buyer's Guide and Policy Overview Prior to Purchase

Illustration Re-engineering Concepts – Consumer-Testing Needed!

Simpler Explanation of How the Product Operates

[Product Name]: How Your Account Value Changes for One Period

Show in Account Value	Index Increases by 3%	Index Increases by 15%	Index Stays the Same – 0% Change	Index Decreases by 3%	Index Decreases by 15%
Product Value at Start of Period					
Change in Value from Changes in Index Inclusive of All Policy Features					
Change in Value from Policy Fees or Any Charges					
Product Value at End of Period					

How is the Change in Account Value Calculated?

Show steps in similar table showing participation rates, multipliers, caps and every other product feature affecting account value calculation.

[Product Name]: How Your Account Value Changes – Part 2

Show in Cumulative Percentage Change	Index Increases by 3%	Index Increases by 15%	Index Stays the Same – 0% Change	Index Decreases by 3%	Index Decreases by 15%
Change in Value from Changes in Index					
Policy Feature 1 (Cap/Floor)					
Policy Feature 2 (Participation Rate)					
Policy Feature 3 (Multiplier/Bonus)					
Policy Feature 4					
Policy Feature 5					
Change in Value from Policy Fees or Any Charges					
Total Change in Product Value at End of Period					

Show Meaningful Measures of Risk and Return

The changes in your product's account value are tied to changes in [name of index].

[Name of index] has been in existence for [X] years.

Over the past [X] years, here are some best and worst performance information about your index and a comparison to the S&P 500 (with and without dividends). The S&P 500 is provided for comparison because it is the most common measure of the returns of a diversified stock market investment and has been in existence for a long time.

The comparison to the S&P 500 results shows you the value of the insurance you are purchasing. An investment in the S&P 500 is risky because you are exposed to all the gains or losses of the "market." Your insurance product may provide protection against some or all of the losses if the "market" declines, as well as other benefits.

No comparison is perfect. Insurance products may have tax advantages that are significant for you.

Past performance is not a guaranty of future outcomes.

Historical Performance of [Name of Product Index/Investment/Dividend] and Product] and [Name of Index]

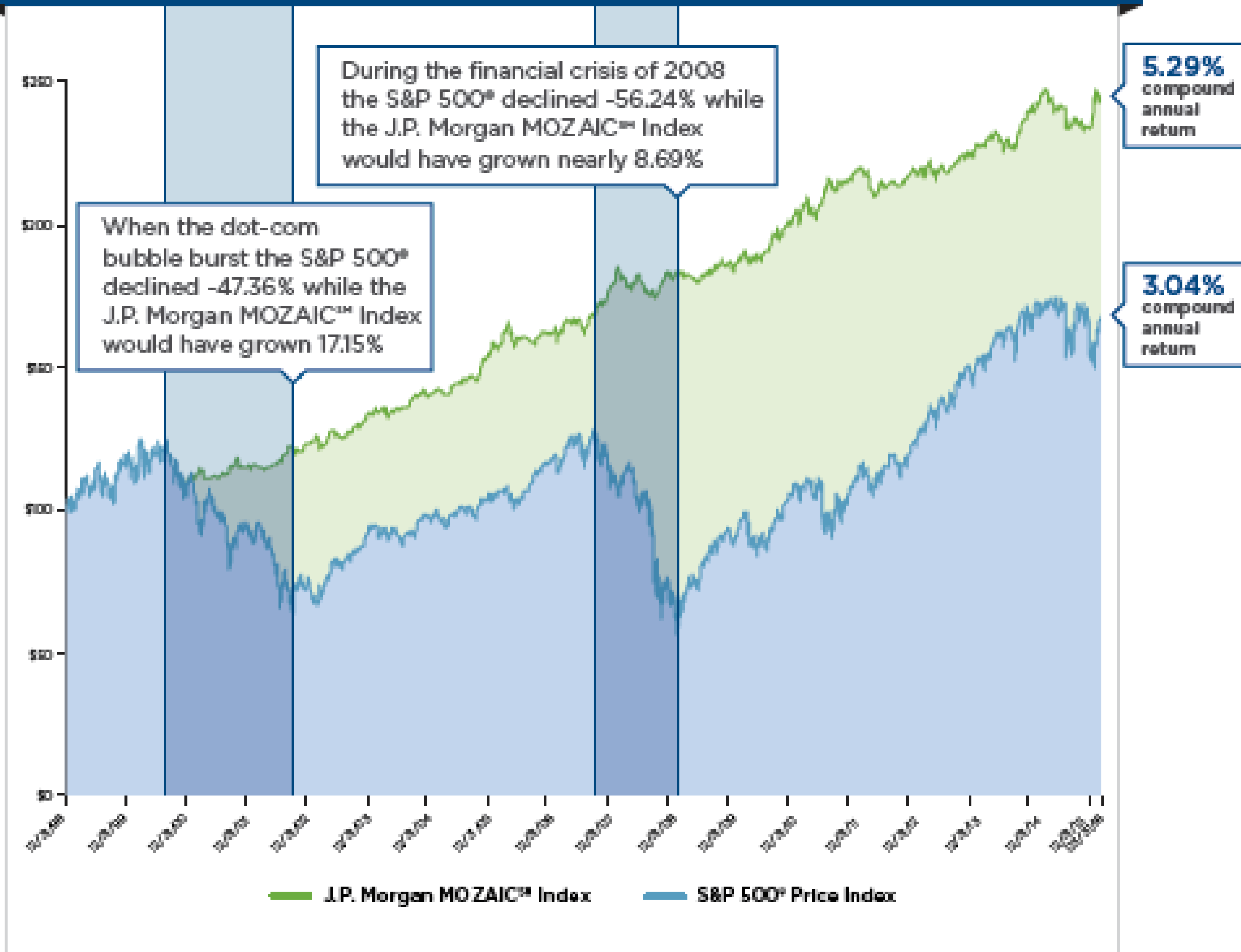
	[Name of Index / Investment]	[Name of Product] including policy features, fees and charges	S&P 500 excluding dividends (1970-2019)	S&P500 including dividends (1970 – 2019)
Worst 1 year			-38.5%	-37.0%
Best 1 year			34.1%	37.6%
Worst 5 Year			-5.73%	-2.35%
Best 5 Year			26.18%	28.56%
Worst 10 Year			-3.04%	-1.38%
Best 10 Year			16.04%	19.21%

Apples to Apples Comparisons

Show the Cost and Value of Insurance

Why is this chart, taken from an insurer's marketing materials, misleading and deceptive?

It compares the performance of an index to only one part of an investment in the S&P 500 – it omits the dividends (a significant part of investment return) obtained by investing in an actual index fund.


J.P. Morgan MOZAIC℠ Index vs S&P 500® Price Index
During the financial crisis of 2008 the S&P 500® declined -56.24% while the J.P. Morgan MOZAIC℠ Index would have grown nearly 8.69%
When the dot-com bubble burst the S&P 500® declined -47.36% while the J.P. Morgan MOZAIC℠ Index would have grown 17.15%
5.29% compound annual return
3.04% compound annual return
J.P. Morgan MOZAIC℠ Index
S&P 500® Price Index

Cost and Value of Insurance

Compared to investing directly in the S&P 500 or the securities that comprise the [Name of Index / Investment], your insurance product offers the following benefits:

[List benefits – Protection against loss when the market or investments go down, tax advantages, death benefit, etc.]

The cost of these insurance benefits is:

[X% of the return from directly investing in the securities that comprise the [Name of Index / Investment]

[$Y and/or Z% in annual charges]

[Charges for withdrawing more than A% annually for B years]

[Other costs/charges]

Provide Key Insurer Performance Information

With most indexed insurance products, the insurer retains the right to modify the cap on returns and expense provisions. In some cases, the insurer retains the right to modify the floor.

Illustration requirements should include a history of changes in key product features for all indexed products offered by the insurer over the past 20 years:

- Number of indexed products offered with changeable caps, floors or expense provisions
- Number of reductions in caps
- Number of increases in caps
- Number of increases in expense provisions or cost of insurance
- Add measures of size (e.g., median amount) time frames of changes

The Annuity Edge

Subscribe

Engineered Indices & FIA

Bobby Samuelson
September 18, 2023

Engineered Indices & FIA

A longer-form version of this post was originally published to The Life Product Review.

If you've been even casually watching the Indexed UL landscape over the past 5 years or so, then you're probably well aware of the fact that engineered indices have come to play an increasingly pivotal role how Indexed UL products are illustrated and sold. The story of the index is becoming *almost* as important as the story of the product itself. The illustrated performance of these indices is driving larger allocations to them and life insurers are incredibly reliant on those allocations for overall profitability. It feels as though Indexed UL has entered a new phase that is distinctly different from what came before and not entirely good for the industry. And if that's concerning to you and you feel like things are getting a little bit out of hand in Indexed UL, then buckle up. You ain't seen nothing yet.

FIA illustrations operate under the same basic illustration framework as Indexed UL. Both use a hypothetical historical lookback methodology that applies currently declared "interest crediting adjustments" to historical index return data. The difference is that in AG 49 for Indexed UL, the illustrated rate is level and based on the average of 25-year returns for the past 66 years. But for the Disclosure Reg and FIAs, the illustrated rate is variable and based on the best, worst and most recent 10-year periods over the past 20 years. The 10-year variable returns are then repeated out for the remainder of the illustration.

The fundamental problem with this hypothetical lookback methodology is that it can be easily gamed because the data is already known. All you have to do is optimize an index or a crediting strategy to back-fit the data if you want to increase illustrated

performance. Life insurers were doing it with bespoke crediting strategies in the 2010s and now they're doing it with engineered indices. Both of those are simply means to maximize illustrated performance without necessarily delivering more value to the customer - if you define "value" as the fair-market cost of the options used to support the crediting strategy.

Engineered Index Illustrated Performance in FIA

Life insurers have become exceedingly adept at maximizing illustrated performance in their FIA products using engineered indices. There are now 165+ engineered indices in market that permeate virtually every FIA product. There is nothing inherently wrong with engineered indices. They can offer valuable diversification benefits and, in some situations, outperform benchmark indices. But the chief attraction for engineered indices is that they deliver the holy grail of indexed crediting - cheap options and high backtested performance. Put those two things together and you get 100%+ participation rates and colossal illustrated performance. It's the stuff sales people dream of.

As a result, FIA writers have plunged headfirst into engineered indices. There are, by my count, no less than 13 FIA writers who have a 1-year indexed crediting strategy using an engineered index with illustrated rates *greater than 10%*. There are a whole slew of companies in the 8-10% range. At the absolute top of the heap is Athene, with a whopping 24.67% illustrated rate on the new HSBC AI Powered Global Opportunities index, followed by Nationwide at 17.51%. And, for the sake of clarity, I feel like I need to emphasize the fact that these are annualized returns that are calculated based on the actual cash value growth in the illustration. If a client deposits $100,000 into a policy illustrating 25%, the illustration is showing over $900,000 in account value by the end of the 10th year.

As high as those average returns are, the more insidious problem with the best/worst/most recent 10 year illustration construct is the what happens on the worst-10 side of the ledger. Engineered indices are optimized to deliver not just lights-out illustrated performance from the most recent 10 year period but also to maintain high returns in the worst-10 scenario. For example, one index that I happened to pull has a 12.14% illustrated rate for the most recent 10 years, 14.21% for the best 10 years and 11.28% for the lowest 10 years. Carriers, agents and distributors play this up as a "can't lose" sort of situation where the "worst case" scenario is still double-digit returns. That is a fundamentally misleading characterization that, in my experience, seems to sometimes be a key part of the sales process.

These sorts of double-digit returns on best/worst/most recent illustrations that I've

quoted so far are only for vanilla account structures. When you combine multi-year strategies with fee-for-rate ("performance fee") structures, some of which have annualized fees as high as 3%, you can get some pretty massive illustrated returns without even pushing the limits in terms of the index itself. Nassau Re, for example, sports an 11.07% on its 2-year Nasdaq 100 account with a 2% performance fee.

The combination of engineered indices, multi-year crediting strategies and fee-for-rate designs have pushed illustrated returns on FIAs into the stratosphere. There are around 550 accounts available in FIA products that illustrate more than 10%. Below is a table of the top 20 FIA writers by IMO sales in Q2 of 2023 and their maximum illustrated annualized rate. Sales data is courtesy of Wink's Sales & Market Report.

Q2 23 Sales Rank	Carrier by Rank	Share	Years	Fee	Top Illustrated rate	Index
1	Allianz	17%	2	0.95%	13.43%	Engineered
2	American Equity	11%	2	3.00%	19.53%	Engineered
3	Athene	11%	2	1.25%	32.97%	Engineered
4	Sammons	9%	2	0.00%	16.70%	Engineered
5	Security Benefit	9%	2	0.95%	19.44%	Engineered
6	F&G Life	7%	2	1.25%	23.96%	Engineered
7	Nationwide	5%	2	0.00%	17.51%	Engineered
8	Corebridge	4%	2	1.00%	19.74%	Engineered
9	SILAC	4%	1	0.00%	22.04%	Engineered
10	National Life	3%	2	1.00%	17.76%	Engineered
11	EquiTrust	2%	2	0.00%	11.18%	Engineered
12	Lincoln	2%	2	0.00%	11.36%	Engineered
13	Aspida	2%	2	0.00%	15.52%	Engineered
14	Nassau	2%	2	2.00%	11.07%	Nasdaq 100
15	Kuvare	1%	1	0.00%	10.86%	Engineered
16	MassMutual Ascend	1%	1	0.00%	7.87%	S&P 500
17	Investors Heritage	1%	1	0.00%	10.55%	Engineered
18	Atlantic Coast Life	1%	3	0.00%	18.92%	Engineered
19	Global Atlantic	1%	1	0.00%	12.82%	Engineered
20	American Life	1%	2	1.25%	14.26%	Engineered

Of the top 20 FIA writers in the IMO channel, just one, MassMutual Ascend, doesn't compete on maximum illustrated performance courtesy of multi-year strategies, fee-for-rate structures and engineered indices. But for literally every single other company on the list, illustrated rates appear to be a key element to their success in FIA, whether they want to admit it or not. If that wasn't the case, then why would they all be chasing double-digit illustrated returns

Illustrated Performance and Illustrated Income

Double-digit illustrated returns have a profound effect on illustrated cash value

performance, but the real leverage happens when these illustrated returns are applied to income. One of the most popular annuity designs in market today grows guaranteed income with indexed credits at the expense of lower indexed credits being applied to the actual policy account value. They are essentially single-use annuities designed for income – but they only really work if indexed performance is strong. Otherwise, the customer would have been better off in a traditional annuity with higher guaranteed income or a dual-use product that still offers strong Account Value growth.

As a result, the guaranteed income streams shown on the illustrations and fueled by illustrated returns on the indexed strategies can be colossal. Of the top 3 FIA products sold with these sorts of riders, all show illustrated IRRs of 13.5% or higher in their most aggressively illustrated accounts on an income stream from Age 65 to Age 85. Little wonder why they sell so well. But the entire pitch and competitive positioning is dependent on illustrated performance. Without that, there's no real reason to choose them.

Illustration Warfare Endgame

The fact that all major FIA writers, especially the ones at the top of the sales chart, heavily promote double-digit illustrated performance is, in my view, a structural weakness in the FIA ecosystem. These products don't need to be aggressively illustrated to be valuable. FIA products can deliver real benefits to consumers for both accumulation and income as an alternative to traditional fixed income. Why have FIA writers decided to embroil the entire industry in illustration warfare that has essentially reached a point of mutually assured destruction – and yet they're still at it?

The answer, in part, is because there is a lot of money to be made in engineered indices. Most of the biggest FIA success stories of the last decade in the IMO channel - Nationwide, Athene, F&G, Allianz - have, in some way, been predicated on the use of engineered indices. An entire cottage industry has cropped up to support engineered indices in FIAs including index analytics consultants, "product development" firms that make marriages between index providers, insurers and distributors, third-party index analytics firms and, obviously, the rapidly growing list of index providers themselves.

But I think that some of the illustration warfare is unintentional. The best/worst/recent 10 year illustration methodology in the Disclosure Reg is fundamentally flawed. It naturally produces aggressive illustrations without even life insurers trying to do it, especially for engineered indices. Consider a situation where a life insurer makes a decision about using a particular index based on the merits of the index structure alone without even looking at the backtested performance. Then, the insurer plugs it into illustration and

gets a 10% illustrated return - is the problem the insurer, the index or the regulation? What about if the index I'm talking about isn't engineered, but the Nasdaq 100 or some other benchmark index? I would argue that the chief blame, in this situation, lies with the flawed regulation that relies on backtested performance.

The question is what to do about it. Insurers have the choice of whether or not to feed into the hype-vortex on illustrated performance. Some are clearly choosing to play the game to maximize illustrated performance, but others are not, or at least are not doing it intentionally. Distributors have the choice of whether they want to craft their value proposition around the claims of insurers, index providers and "product development" companies about index performance or if they want to do their own due diligence. And agents, of course, have the choice about what story they ultimately want to tell to their clients about performance. Is FIA a fixed income alternative or a fantastical product that delivers 30% returns with no principal risk?

Decisions have consequences. And we, as an industry, need to start deciding before regulators, lawyers and potentially even the SEC decide for us.

Keep reading

Maximize Equity Exposure Within FIA Indices

8 months ago

THE ANNUITY EDGE
PRODUCT INTELLIGENCE DELIVERED WEEKLY

Week in Review - 9/22/23

AuguStar hits the market, Goldman Sachs releases a unique index with North American, Lincoln and GBU receive approval for new FIA products and engineered indices take a...

a month ago

Simple vs Compound Interest

a year ago

View more ›

The Annuity Edge

Everything you need to know about what's happening in annuity product, delivered weekly

Enter your email

Subscribe

Verify you are human

Privacy • Terms

© 2023 The Annuity Edge.

Privacy Policy | Terms of Use

Powered by beehiiv

ASIC
Australian Securities & Investments Commission

Disclosure: Why it shouldn't be the default

A joint report from the **Australian Securities and Investments Commission** (ASIC) and the **Dutch Authority for the Financial Markets** (AFM)

Contents

What we mean by 'disclosure' 3
Executive summary 4
Case studies in disclosure limitations 5
Disclosure does not solve the complexity in financial services markets 8
'People aren't dumb, the world is hard' 8
Financial decisions are complex 10
Some firms make their products and processes strategically complex, confusing consumers 12
Simplifying disclosure does not solve complexity 13
Disclosure must compete for consumer attention 20
Few consumers pay attention to disclosure 20
Firms' influence on consumers is timely and compelling 22
Firms with misaligned incentives may have the incentive, opportunity and means to work around and undermine disclosure 28
One size does not fit all – the effects of disclosure are different from person to person and situation to situation 34
People differ … so does the context 34
Context matters 39
No universal approach to disclosure can meet the needs of all 40
In the real world, disclosure can backfire in unexpected ways 42
A warning about warnings 45
Warnings do not always work as intended 45
Warnings can backfire 49
Conclusion 51
Appendix: Accessible versions of figures and notes 53
Accessible versions of figures 53
Notes for Figure 5 55
Key terms 56
Reference list 57

Disclaimer
This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the applicable laws apply to you, as it is your responsibility to determine your obligations.
Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.
The text of this document has been compiled with care and is informative in nature. No rights may be derived from it. ASIC and AFM are not responsible or liable for any consequences – such as losses incurred or lost profits – of any action taken in connection with this text.

What we mean by 'disclosure'

Disclosure is information the law mandates must be provided to consumers by firms.

Disclosure presents material information about the characteristics, fees and/or risks of financial products and services. Financial firms can provide disclosure in hard-copy document form or electronically (e.g. emails or on websites).

Some examples of disclosure documents are:

- detailed disclosure documents (e.g. prospectuses and Product Disclosure Statements)
- summary tools (e.g. Australian key facts sheets and dashboards, and Dutch financial information leaflets and Key Information Documents)
- warnings.

Firms may be required to provide the information to prospective customers at or close to the time of sale, as well as throughout the lifecycle of the product.

In this report disclosure does **not** include:

- contractual information
- other information conveyed by firms to consumers outside their mandatory disclosure obligations (for example, through advertising).

Executive summary

Financial services disclosure has traditionally been assumed to inform us (as consumers), help us make 'good' financial decisions, and drive competition.

This report focuses on the real-world context in which disclosure operates. It shows that, and explains why, disclosure and warnings can be less effective than expected, or even ineffective, in influencing consumer behaviour. In some instances it shows that disclosure and warnings can backfire, contributing to consumer harm.

The report is a joint publication by the Australian Securities and Investments Commission (ASIC) and the Dutch Authority for Financial Markets (AFM). Both of these regulators have, over a number of years, identified limitations to disclosure in their respective retail financial services markets.[1] Although the Australian and the Dutch financial markets and regulatory regimes differ, there is also much common ground.

As regulators, ASIC and the AFM agree that while disclosure is necessary, it alone is often not sufficient to drive good consumer outcomes.[2] Disclosure can and does contribute to better financial markets. For example, when media, competitors and intermediaries use it to gauge and thus enhance competition. Regulators can use it to contribute to market transparency, integrity and efficiency. And consumers can use disclosure as post-purchase reference documents in the event of disputes. However, we cannot assume that disclosure alone, including warnings, will be effective in protecting consumers, enabling good decision making and driving competition from the demand side.

Moreover, when disclosure is used to address problems it is ill-suited to solve, it can place an unrealistic and onerous burden on consumers – for example, expecting them to overcome complexity and sophisticated sales strategies.

ASIC and the AFM take the publication of this report as an opportunity to contribute to 'frontier' public policy discussions, by raising for consideration the need to rethink:

- the role of disclosure as the default option relied on to protect consumers
- assumptions about competitive market forces and what role disclosure actually plays in shaping 'effective' demand-side pressure

[1] ASIC, *Financial System Inquiry interim report: Submission by ASIC* (PDF 961 KB), August 2014, pp. 15–17; ASIC, *Financial System Inquiry: Submission by ASIC* (PDF 2 MB), April 2014, pp. 12, 80–81; ASIC, *Submissions of the Australian Securities and Investments Commission – Round 6: Insurance* (PDF 247 KB), Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, October 2018; P Kell, then ASIC Deputy Chairman, *ASIC and behavioural economics: Regulating for real people*, speech, Queensland University Behavioural Economics Group symposium, 18 October 2016; AFM, *Caution! Borrowing money costs money: A study of the effectiveness of a warning in credit advertisements* (PDF 1 MB), report, December 2016; AFM, *A closer look at consumer borrowing: An analysis of decision-making behaviour and potential interventions in the consumer credit market* (PDF 428 KB), report, May 2019; WB Hoekstra, Minister of Finance, 'Uitkomsten onderzoek consumptiefkredietmarkt' ('Results of consumer credit market research', Dutch only), letter to parliament, September 2018.

[2] A Fletcher, 'The role of demand-side remedies in driving effective competition', *Which?*, 7 November 2016, pp. 36–39; G North, 'Efficiency, fairness & irrationality: Incompatible or complementary?', *Banking & Finance Law Review*, vol. 24(2), February 2009, pp. 333–334.

- the appropriate balance between consumers and industry for effecting good consumer outcomes, and avoiding poor ones.

Real-world testing and monitoring is needed to assess the effectiveness of required information and disclosure in achieving good outcomes for consumers.

Case studies in disclosure limitations

The report explores the limits of disclosure, using case studies from ASIC, the AFM and other relevant sources as evidence. These case studies are drawn from the full range of financial products and services in different financial markets, and include all forms of disclosure.

As the case studies are specific to products and contexts, the findings from each are not generalisable. However, together they show how overloaded the expectations on disclosure and consumers can be; and why firms providing mandatory information does not necessarily result in 'informed consumers' and often does not correlate with good consumer outcomes. Disclosure is necessary, but not sufficient.

Why? Because:

> **Disclosure does not solve the complexity in financial services markets**
> Disclosure cannot solve complexity that is inherent in products and processes. Simplifying disclosure, for example, does not reduce the underlying complexity in financial products and services. Nor does it ease the contextual and emotional dimensions of financial decision making, both at the point of purchase and over time.

> **Disclosure must compete for consumer attention**
> We are constantly saturated with competing attempts to capture our attention and influence our decisions. Many firms have the commercial opportunity and means to effectively attract, distract and influence us; but regulators, and the disclosures they mandate, generally do not. Firms can also work around or undermine disclosure requirements that, once set, are generally slow to change.

> **One size does not fit all – the effects of disclosure are different from person to person and situation to situation**
> Like other forms of regulation, mandated disclosure requirements are often 'one size fits all' interventions – yet people and contexts differ and shift. It is hard to predict the individual and context-specific differences in how we will behave, make decisions, and engage with and process information.

> **In the real world, disclosure can backfire in unexpected ways**
> At worst, disclosure creates unintended detrimental outcomes for some consumers – in effect contributing to consumer harm (e.g. by increasing rather than decreasing trust in conflicted advisers, and decreasing rather than increasing credit card repayments). Ongoing monitoring of disclosure is needed because of these unexpected effects.

Finally, we also issue:

A warning about warnings

There is emerging evidence from financial services regulators about the limitations of the effectiveness of warnings that firms have to display about the risks and features of certain products and services. There is, for instance, some evidence of the effectiveness of warnings on our understanding of the risks associated with products, and in encouraging us to avoid unsuitable or harmful products.

Warnings are not a cure-all for problems in financial services markets. Further research to evaluate their effectiveness is warranted.

Disclosure does not solve the complexity in financial services markets

Disclosure does not solve the complexity in financial services markets

Disclosure cannot solve complexity that is inherent in products and processes. Simplifying disclosure, for example, does not reduce the underlying complexity in financial products and services. Nor does it ease the contextual and emotional dimensions of financial decision making, both at the point of purchase and over time.

'People aren't dumb, the world is hard'

One of the key assumptions on which disclosure has traditionally been premised is the idea that if information asymmetries are corrected, we will make optimal choices. However, this assumption disregards how difficult it can be to choose the best option (if, in fact, it is possible at all), given the computational complexities involved.[3] As the Nobel laureate Richard Thaler says, 'People aren't dumb, the world is hard'.[4]

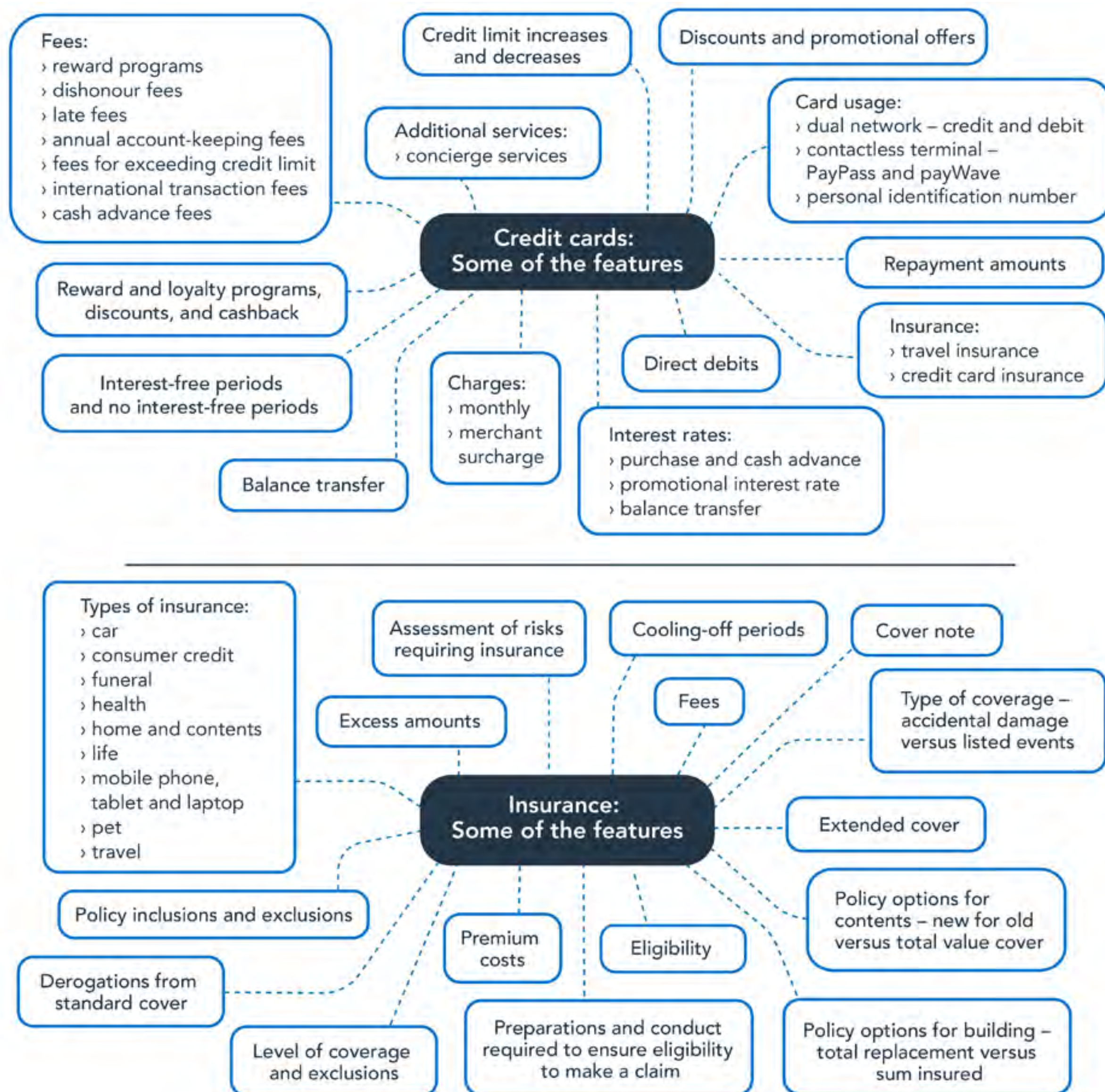
For instance, behavioural economist Pete Lunn and colleagues investigated consumer decision making about complex products. Their research indicates that once we have to take into account more than two or three different factors, our ability to identify good and bad deals becomes strikingly inaccurate.[5] This research also found that although people with high levels of numeracy and education performed slightly better than those without, the improvement was small. Everybody tested struggled to differentiate good from bad deals when they had to take into consideration more than two or three product attributes.

Applying this insight to financial services suggests that few (if any) financial products and services are *not* 'complex'. For instance, a savings account has several features to trade off: free withdrawal or not, compound interest (interest-on-interest) or not, and (in the EU context) which deposit guarantee scheme is applicable.[6] Ubiquitous products, such as credit cards and insurance products, also have multiple complex features: see Figure 1. While disclosure about complex products is still necessary, it alone is not sufficient to resolve complexity, nor to drive good consumer outcomes.

---

[3] P Bossaerts P & C Murawski, 'Computational complexity and human decision-making', *Trends in Cognitive Sciences*, vol. 21(12), December 2017, pp. 917–929.
[4] SJ Dubner, 'People aren't dumb. The world is hard (Episode 340)', *Freakonomics*, podcast, 11 July 2018.
[5] P Lunn, M Bohacek, J Somerville, AN Choisdealbha & F McGowan, *PRICE Lab: An investigation of consumers' capabilities with complex products*, report, Economic & Social Research Institute, May 2016.
[6] Some saving accounts offered in the Netherlands actually fall under the deposit guarantee scheme of another European country – for example, the deposits at the Landesbanki (Icesave) bank, which failed in 2008, were guaranteed by the Icelandic deposit guarantee scheme.

Figure 1: Complexity of ubiquitous financial services and products – Credit cards and insurance



Note: See Table 3 for the information shown in this figure (accessible version).

Further complicating our decision-making task is the choice we face between multiple options. In selecting a financial product, not only must we trade off the features within the product, we are also expected to compare and trade off those features across multiple types of products.

Case study: Consumers focus on price to the exclusion of other factors – Home insurance **AUS**

ASIC research into consumer decisions to purchase home insurance found that many consumers focused on price to the exclusion of other features. These price-motivated consumers chose the known over the unknown. They knew that a premium reduction was achievable; they did not know that choosing a policy based on a policy feature might be useful or even necessary to them in the future. In effect, this focus on price may have led consumers to take a short cut when choosing between complex products, discouraging them from discovering that the policies were not in fact comparable.[7]

Financial decisions are complex

Decisions about financial products and services are particularly complex because they:

- are often made **infrequently,** providing few opportunities for feedback and learning
- may have an **emotional dimension** – for example, when the impact they have on our lives and wellbeing is very large
- are **intangible**, with no physical cues by which quality can be judged
- may require **trade-offs over time** – for example, between present and future benefits, where the future benefits or harms may be only realisable long after we have made the decision to purchase
- may involve **uncertainty** – for example, about unknowable future states of the world and our own difficult-to-predict future behaviour, on which the features and prices of many financial products are contingent
- often involve **risk** – for example:
  - insurance products protect against risk
  - investment products require balancing the chance of positive returns against the risk of loss
  - credit products involve risk of over indebtedness and/or interest rate increases.

  Unsurprisingly, most of us judge risk intuitively and inaccurately. We have difficulty understanding probabilistic processes, and either overestimate or underestimate. Moreover, these (mis)judgments are made by both the general public and experts alike – particularly when experts rely on their intuition, rather than available data.[8]

[7] ASIC, Report 416 *Insuring your home: Consumers' experience buying home insurance* (REP 416), October 2014.
[8] P Slovic, 'Perception of risk', *Science*, vol. 236(4799), April 1987, pp. 280–285, p. 281.

Case study: Inaccurate perceptions of risk in stock markets and initial coin offerings (ICOs) **NL**

AFM research found that both investors and non-investors overestimated loss probabilities in the stock market.[9] This overestimation was stronger for non-investors, and it was particularly strong for longer investment periods.

The AFM also found that people who invested in ICOs underestimated the chances that they would lose money in their investment. The risk perception of ICO investors appears to be lower than justified. Three quarters of the ICO investors estimated that the probability of loss of their investment was less than 50%, whereas available data indicate that nearly half of the offerings in 2017 failed within the year.[10]

Case study: Onerous requirements to accurately assess risk in insurance **AUS**

In ASIC's experience, disclosure has proved particularly ineffective in enhancing consumer understanding of the level of risk involved in a product or service. For instance, in the context of insurance, research indicates that to accurately assess risks individuals must hold in their short-term memory:

- recollection of several previous insurable events
- an imagined situation involving their own home for all such events
- some kind of causal reasoning in which the consumer would judge, for example, that if the river flooded their house, it would be inundated to a certain level.[11]

More generally, we do not interact with disclosure in isolation, nor do we make decisions about or between specific financial products or services in isolation. Context matters. In the real world, we are routinely required to make multiple decisions on a broad range of day-to-day and major life issues, in an environment (over)crowded with information and choices. As Nobel laureate Daniel Kahneman has identified, nobody has the time or the resources to fully analyse all of the available information and fully maximise their utility with every choice.[12]

[9] S Zeisberger, C Borsboom, D-J Janssen, M Strucks, M & W Zijlstra, *Investor risk perception in the Netherlands* (PDF 807.3 KB), research paper, AFM, 2018.
[10] AFM, *Investing in cryptos in the Netherlands: Market survey under Dutch consumers* (PDF 371.98 KB), June 2018; K Sedgwick, 'Crowdfunding: 46% of last year's ICOs have failed already', *Bitcoin.com*, 23 February 2018.
[11] REP 416, p. 15.
[12] D Kahneman, *Why we contradict ourselves and confound each other*, interview transcript, October 2017.

Some firms make their products and processes strategically complex, confusing consumers

Some firms can compound and further take advantage of this already highly complicated environment by making products and processes strategically complex (e.g. bundled products and pricing, confusing and opaque 'discounts', unclear fee descriptors).[13]

Credit cards, for instance, are inherently complex products because they are at least three products in one – a non-cash payment facility, a credit facility and a means of withdrawing cash. Firms often add to this complexity by bundling and marketing credit cards with other financial products (such as insurance) and loyalty points, making it more difficult for us to separate the price and value of each feature – particularly as some of the costs and benefits are immediate and others are realised in the future: see Figure 1.

Firms can also make processes strategically 'sludgy' by including excessive, unnecessary frictions that make it difficult for us to do what we want.[14] For example, firms can make products easy to get into, but hard to get out of.

Strategies such as these can confuse us and/or take advantage of our confusion, and defeat our attempts to engage with or understand even simplified disclosure. The more products and processes are made complex, the harder they are to explain and understand.

Firms can also make the content and delivery of disclosure itself strategically complex. For example, by making the disclosure hard to find or hard to understand, or providing it when it is unlikely we will be able to factor the disclosed information into our future decisions and outcomes.

Case study: Consumer credit insurance – Devil in the detail **AUS**

Consumer credit insurance (CCI) is sold with home loans, personal loans and credit cards. It provides cover for consumers if they can't meet their minimum loan repayments because they become unemployed, sick or are injured, or to pay the outstanding loan balance if they die.

In Australia, 'sludge' is a feature in the design of CCI, as well as in sales and claims handing processes. This sludge can exacerbate the problems created by unfair sales practices and further reduce the ability of disclosure to drive good consumer outcomes.

Bundled products

In Australia the CCI sold with credit cards is particularly poor value in part, because of the **strategic and confusing complexity built into the products** – for example, they contain bundled cover for temporary disability, permanent disability, terminal illness, death, and involuntary unemployment.

[13] O Bar-Gill, *Seduction by contract: Law, economics, and psychology in consumer markets*, Oxford University Press, Oxford, 2012, pp. 18–20; X Gabaix & D Laibson, 'Shrouded attributes, consumer myopia, and information suppression in competitive markets' (PDF 147 KB), *The Quarterly Journal of Economics*, vol. 121(2), 2006, pp. 505–540.
[14] CR Sunstein, *Sludge audits*, Harvard Public Law Working Paper No. 19-21, April 2019.

Yet, despite disclosure, many consumers who have CCI have only a shallow knowledge of the policy, and others are not even aware they have it.

ASIC research conducted in 2013[15] found that most consumers interviewed described the decision to purchase as **easy and quick**. Some consumers were led to believe it was mandatory, and others recalled that it was provided to them automatically on what they described as an 'opt-out' basis.

Strategically complex and unfair sales tactics

Some consumers felt that the sales process worked against them being able to attempt to understand the policy features, with sales staff giving mixed messages and rushing decisions. Some consumers had no recollection of receiving any information, and others recalled not having time to read information, or only being given policy documents after they had purchased the policy.

More recently, ASIC has identified continued use of **strategically complex and unfair sales tactics**.[16] For instance, tactics used by telemarketers include:

- suggesting that consumers buy CCI and cancel it during the cooling-off period if they continued to see no value in it;
- failing to inform consumers about exclusions (which would make some consumers ineligible)
- using ambiguous language to obtain consent so that some consumers did not realise they were agreeing to buy CCI
- pressuring consumers and persisting with sales calls even when consumers stated they did not want or need CCI
- overcoming consumers' reasonable objections using practiced techniques that played to consumers' concerns.

High friction claims handling processes

ASIC's 2013 research found that some consumers who lodged claims, found the **process unexpectedly burdensome**, with onerous obligations to provide documentation and evidence. Generally, the consumers who were required to supply most information had suffered the most serious problems and were unlikely to ever return to work.

Simplifying disclosure does not solve complexity

Simplifying disclosure does not 'solve' complexity because, as Professors Omri Ben-Shahar and Carl E Schneider assert, the complex is not simple and cannot easily be made so.[17] They argue that much of the complexity in disclosure arises because so much affects a

---

[15] ASIC, Report 361 *Consumer credit insurance: Consumers' claims experience* (REP 361), July 2013.
[16] ASIC, Report 622 *Consumer credit insurance: Poor value producs and harmful sales practices* (REP 622), July 2019.
[17] O Ben-Shahar & CE Schneider, 'More than you wanted to know: The failure of mandated disclosure' (PDF 504 KB), *University of Pennsylvania Law Review*, vol. 159, 2011, pp 647- 749.

'well-considered' choice. The more factors that are eliminated (in the interests of simplification) the greater the risk that something that may improve a decision has been omitted. The fewer factors that are eliminated, the more we must struggle to understand, remember and take into account.

Moreover, 'simplification' often amounts to simplification of language, rather than concepts and issues. Even if simple words could efficiently describe concepts and issues, most of us lack the specialist experience and skills necessary to process and evaluate the information. Finally, it is clearly not feasible for disclosure to solve the many complex emotional and contextual dimensions of financial decisions (e.g. our mindset and circumstances at the time of the decision(s), or the inherently emotional nature of some decisions).

The following two case studies demonstrate the limited impact of both simplified and detailed disclosure on consumer choices about complex products. In both cases, participants in laboratory experiments were asked to pick the best available option, based solely on the information provided to them. The results showed that many participants were not able to select the best option, even in these idealised 'quiet' circumstances – isolated from the busy context of the real world, including the many distractions, demands and influences that affect our decisions and behaviour.

Case study: Limited impact of summary and detailed home insurance disclosure documents **AUS**

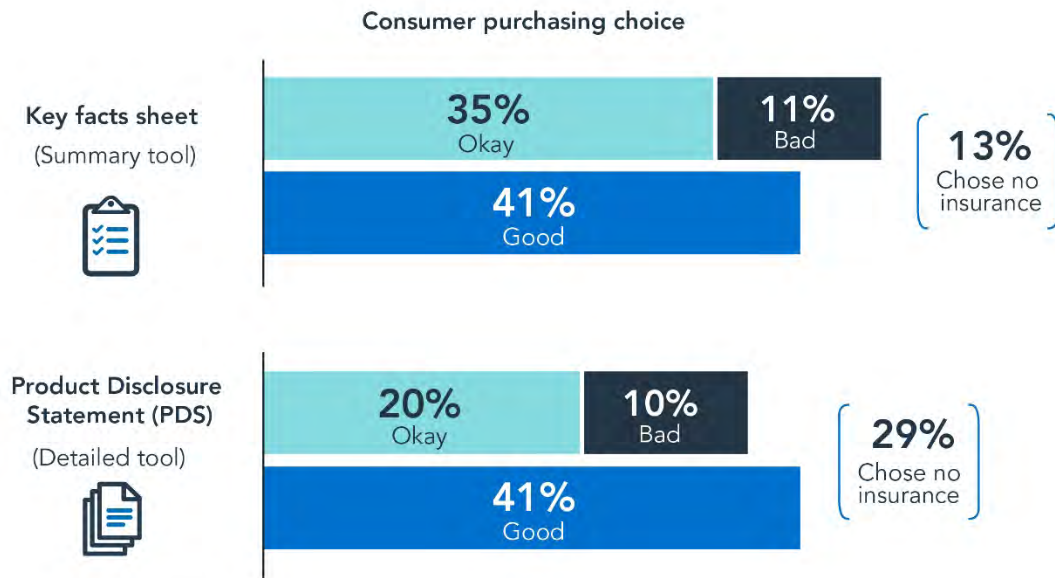
The effectiveness of different disclosure in helping consumers make 'optimal' purchasing choices about home insurance was tested in an experiment conducted by Monash University.[18] The experiment was conducted in a computer laboratory and the only information participants could base their decision on was a detailed Product Disclosure Statement (PDS) and/or a two-page key facts sheet.

Key findings from a number of different experimental groups showed that:

- only two fifths (41%) of participants provided with the 'simple' key facts sheet selected the objectively best insurance product. They did no better than those provided with the longer PDS: see Figure 2.
- almost three fifths (59%) of participants provided with either the 'simple' key facts sheet or longer PDS made suboptimal choices
- within some experimental groups, up to 42% of participants chose the worst product on offer.

[18] J Malbon & H Oppewal, *(In)effective disclosure: An experimental study of consumers purchasing home contents insurance*, research report of a study commissioned by the Financial Rights Legal Centre, Monash University: Australian Centre for Financial Studies, 2018.

Figure 2: Insurance purchase choices using key facts sheets and PDSs



Note: Online quantiative experiment with a sample size of 406 Australians aged 18 years and over, nationally distributed sample. Research conducted 2018. See Table 4 for the data shown in this figure (accessible version).

Case study: Limited impact of summary investment bond disclosure documents NL

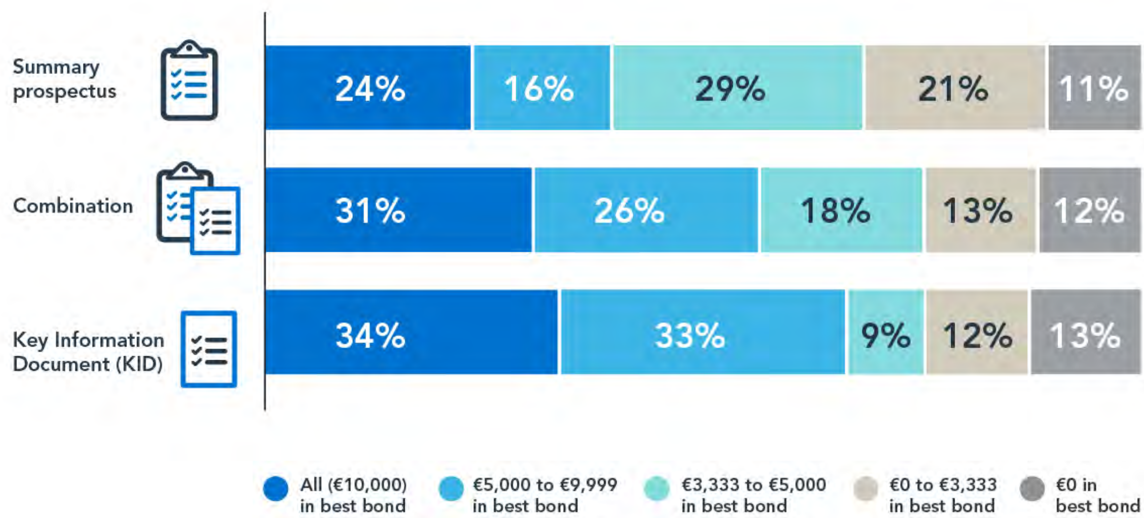
Similar research was conducted by the AFM.[19] Consumers were asked to decide which bond to invest their money in, based solely on one of two shorter documents (a four-page summary prospectus or a three-page Key Information Document (KID)), or a combination of both documents. It was possible to objectively assess the best choice bond, because in the controlled setting there was one offering that dominated the other two bonds; costs and risks were lower or equal, and yields were equal or higher.

Key findings included that those participants who were given the KID made better investment decisions overall – over one-third (34%) of participants correctly invested everything in the dominating bond (for the summary prospectus this was 24%, and for the combined disclosure this was 31%). However, 66% of participants who were given the KID still invested some or all of their available assets in suboptimal options. So some forms of disclosure performed significantly better than other forms of disclosure. But no one type of disclosure helped all consumers.

For a summary of the results, see Figure 3.

[19] AFM, *A randomized controlled trial on the effectiveness of mandatory investment information*, article, 2019.

Figure 3: Investment decisions of consumers using a summary prospectus, KID and a combination of both



Note: Online quantitative experiment with a sample size of 384 Dutch retail investors. Research conducted in 2016. See Table 5 for the data shown in this figure (accessible version).

Reliance on expert advisers

One option open to consumers seeking to navigate the complexity in financial services markets is to seek expert advice. However, it can be difficult for consumers to know who to trust to give such advice and disclosure cannot solve this dilemma for consumers.

Case study: Difficulties in judging quality of advice — AUS

In Australia, financial product advisers must provide consumers with a Statement of Advice (SOA) that sets out the basis for advice, details about the providing entity, and any payments or benefits the adviser will receive. However, this information cannot provide consumers with the specialist skills, knowledge and experience required to accurately judge the quality of the advice provided.

Shadow shopping research ASIC conducted with real consumers who sought retirement advice identified a large gap between the technical quality of the advice (as assessed by ASIC) and the consumers' own assessment of that advice. While 86% of consumers considered the advice they received to be good, ASIC assessors rated only 3% of the advice reviewed as good, with the remainder rated as adequate, or poor: see Figure 4.[20]

[20] ASIC, Report 279 *Shadow shopping study of retirement advice* (REP 279), March 2012.

The research also identified a disconnect between the trust or level of comfort consumers felt with their advisers and the quality of advice received: 81% of consumers said that they trusted the advice they received from their adviser 'a lot', although 39% of the advice examples reviewed by ASIC staff were actually poor, and 58% were only adequate.[21]

Figure 4: Consumer versus ASIC staff rating of advice received

Sample: Qualitative shadow shop research with a sample of 64 Australian adults aged 50–69 years. Each advice example was reviewed by at least two ASIC analysts. A 12-person expert reference group – composed of industry representatives, a representative of the Financial Ombudsman Service and a representative of ASIC's Consumer Advisory Panel – provided guidance and oversight of the advice assessment process. Research conducted in 2011.

Case study: Consumers rated the 'worst' mortgage advisers highly **NL**

Similar Dutch research found that some of the advice provided by mortgage advisers that consumers considered to be high quality was ranked among the worst by a bank, and vice versa. There was no relation between consumers' online ratings of mortgage adivsers and the ratings given by a bank that worked with the advisers.[22]

As with the underlying financial decision, judging advice quality involves unreasonable computational complexity and requires expertise and pre-existing knowledge. The absence of these can lead us to substitute other attributes – such as social affinity (grounded in shared religion, language or culture), strong social rapport and/or a trusted brand – to help us assess quality.[23]

[21] REP 279, paragraphs 18 and 22.
[22] M Mons & C Baelemans, *Value chain excellence in retail* (Dutch only), presentation slides, IG&H Consulting, July 2011.
[23] See, for example, ASIC, Report 15 *Hook, line and sinker: Who takes the bait in cold calling scams?* (REP 15), June 2002; ASIC, Report 126 *Understanding investors in the unlisted unrated debenture (UUD) market* (REP 126), April 2008; ASIC, Report 470 *Buying add-on insurance in car yards: Why it can be hard to say no* (REP 470), February 2016.

For instance, one investor involved in ASIC research based her decision to invest in an unlisted, unrated debenture on the trust she had in the salesperson, which was in turn grounded in the language and cultural background she shared with the salesperson.

"And of course we had a good hard yak in Polish, because I love the Polish language … and I felt that [this sales person] was very, very honest. "[24]

In practice, trust in advisers may be misplaced, particularly where advisers have misaligned incentives – for example, due to a remuneration scheme that creates perverse incentives. Disclosure has often been relied on to help consumers navigate the complexities associated with conflicts of interest. However, this disclosure-based approach can backfire, increasing consumers' trust in advisers and giving advisers 'moral license' (i.e. when people allow themselves to do something bad (e.g. immoral) after doing something good (e.g. moral))[25] to recommend biased choices to their customers.

The onus is on consumers to navigate this complex environment, in circumstances in which information alone is insufficient to correct the imbalance in experience, knowledge and power.

[24] REP 126, p. 22.
[25] On moral license, see A Merritt, D A Effron, & B Monin, 'Moral self-licensing: When being good frees us to be bad', *Social and Personality Psychology Compass*, vol. 4/5, 344–357, May 2010. On trust, see D de Meza, B Irlenbusch & D Reyniers, *Disclosure, trust and persuasion in insurance markets* (PDF 425 KB), IZA Discussion Paper No. 5060, July 2010.

Disclosure must
compete for
consumer
attention

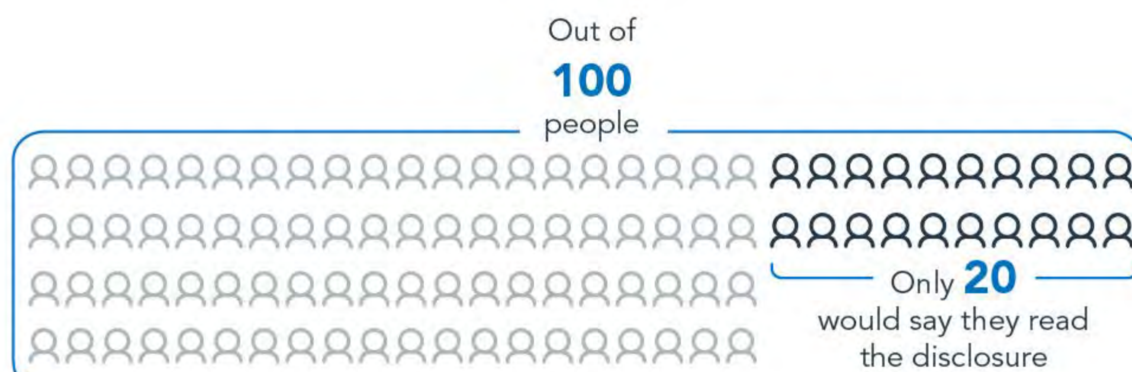
Disclosure must compete for consumer attention

> We are constantly saturated with competing attempts to capture our attention and influence our decisions. Many firms have the commercial opportunity and means to effectively attract, distract and influence us; but regulators, and the disclosures they mandate, generally do not. Firms can also work around or undermine disclosure requirements that, once set, are generally slow to change.

Few consumers pay attention to disclosure

A consistent finding in Australian research about consumer engagement with long disclosure documents about financial products – for example, investment,[26] insurance,[27] and superannuation products[28] – is that many of us do not access the documents at all, and those of us who do skip large parts: see Figure 5.

Figure 5: Proportion of consumers who read the disclosure



Note: The diagram is based on six separate quantitative research studies of consumers who read or used mandated disclosure and/or information. Research findings included products and services across channels and sectors (e.g. financial services and online privacy). See 'Notes for Figure 5' for details on data and methodology.

Similarly, in the Netherlands, nearly half of consumers interviewed in one study reported not reading their service agreement documents ('dienstverleningsdocument') or its precursor.

---

[26] ASIC, Report 540 *Investors in initial public offering* (REP 540), August 2017; WhereTo Research, *Factors that influence retail investors in IPOs* (Attachment to REP 540), August 2017, p. 6; ASIC, Report 341 *Retail investor research into structured capital protected and capital guaranteed investments* (REP 341), May 2013; ASIC, Report 588 *Consumers' experiences with the sale of direct life insurance* (REP 588), August 2018.
[27] REP 416; Effective Disclosure Taskforce, *Too long; didn't read – Enhancing general insurance disclosure* (*Too long; didn't read*), report, Insurance Council of Australia (ICA), October 2015; ASIC, Report 292 *Paying for funerals: How consumers decide to meet the costs* (REP 292), July 2012; REP 588.
[28] ASIC, Report 576 *Member experiences with self-managed superannuation funds* (REP 576), June 2018.

Only about 1 in 10 consumers thoroughly read these documents,[29] and a minority of consumers use them to compare financial advisers. [30]

Two common barriers that we self-identify in explaining the limited attention paid to disclosure are that the documents are impenetrable and not relevant: see Table 1.

Table 1: Common barriers self-identified by consumers

Barrier	Examples
Disclosure was impenetrable	Consumers found that the disclosure was too long, was too complex, and/or used difficult and technical language and concepts.[31]
Disclosure was not relevant	Consumers found that the disclosure lacked 'candid information' and/or did not provide information that was actionable in light of the consumers' personal circumstances and context.[32] Consumers who skipped large parts of the disclosure documents reported that they focused on the sections they considered to be important.[33]

However, these reasons do not provide a complete explanation of the limited attention we pay to disclosure. They must be considered in conjunction with other limitations of disclosure, such as those discussed in this report, and the broader context within which we make decisions.

In particular, disclosure is often provided at a time and in a manner that renders it unlikely to influence us. For example, it may be provided:

- after we have already committed to the purchase[34]
- when there is insufficient time for us to read and consider the document,[35] or
- as one of multiple documents provided at the confirmation or appointment of a financial adviser.[36]

Those of us who do access disclosure documents often remain confused and/or fail to act on them as intended by policy makers. This is true for both detailed disclosure documents and shorter, simplified summary tools. For instance, in the Netherlands, there is high name recognition of shorter financial information leaflets ('Financiële bijsluiter') – that is, people know it exists, so they could access this summary document. But only two in five people actually used it in their decision to purchase a complex financial product, such as a mortgage or life insurance.[37]

---

[29] P Risseeuw, M Kerste, B Baarsma, & R Dosker, *Evaluatie provisieregels complexe producten* ('Evaluation of provisions for complex products', Dutch only), report no. 2010-44, SEO Economisch Onderzoek, September 2010.
[30] M Elsen, R van Giesen, M Elshout, & J Leenheer, *Consumenten en financieel advise. Consumentenonderzoek in het kader van de evaluatie van het provisieverbod* ('Consumers and financial advice. Consumer research for the evaluation of the ban on commissions', Dutch only), CentER Data, November 2017.
[31] See, for example, REP 341; REP 416; REP 540; REP 576; *Too long; didn't read*.
[32] See, for example, REP 540; REP 576.
[33] See, for example, *Too long; didn't read*; REP 416; REP 576; REP 540.
[34] See, for example, REP 416 and REP 470.
[35] See, for example, REP 416 and REP 470.
[36] R van Steen, J Visser & A Eecen, *De effectiviteit van de Financiële Bijsluiter: resultaten van onderzoek onder consumenten* (PDF 382 KB) ('The effectiveness of the Financial Leaflet: results of consumer research', Dutch only), report, TNS Nipo, 13 March 2009.
[37] R van Steen, J Visser & A Eecen, *De effectiviteit van de Financiële Bijsluiter: resultaten van onderzoek onder consumenten* (PDF 382 KB) ('The effectiveness of the Financial Leaflet: results of consumer research', Dutch only), report, TNS Nipo, 13 March 2009.

Firms' influence on consumers is timely and compelling

Firms frequently try to capture our attention and influence our behaviour. Regulators seeking to influence us rely chiefly on disclosure. Firms, on the other hand, can directly influence us through a broad range of increasingly sophisticated marketing and sales techniques.

For some firms, these 'pathways' of influence are designed with the benefit of deep expertise, extensive resources and, increasingly, access to and use of personal consumer data. Many firms are adept at using behavioural approaches to encourage specific behaviours.

As the following case studies demonstrate, it is difficult, and often impossible, for disclosure to compete with and disrupt the myriad ways in which firms can capture our attention, strategically distract us and otherwise nudge our decisions. Firms can for instance:

› employ advertising and marketing
› develop sales pitches
› shape the choice architecture and context to their benefit.

Advertising and marketing

Firms may advertise or market a brand or product, and thereby influence our preferences and behaviour in ways we are often unaware of. They can use a broad range of sophisticated strategies to make their product offerings appear attractive and socially desirable.

These strategies extend beyond traditional written and broadcast advertising, and include social media and face-to-face marketing that leverage social rapport. The potential of marketing to influence us is ever increasing, as more firms use available data to profile consumers, micro-target communications and behaviourally target specific consumers in particular contexts at particular times.[38] Digitalisation makes collecting this data, often through online channels, easier and cheaper.

Relying on disclosure obligations that are generalised and static to keep pace with these evolving marketing techniques, is likely to become increasingly impracticable.[39]

[38] M Kaptein, *Persuasion profiling: How the internet knows what makes you tick*, English edn, Business Contact Publishers, Amsterdam/Antwerp, May 2015.
[39] LE Willis, M Hastak & J King, 'Customer confusion audits: Lessons from the use of consumer confusion audits in the United States', research report for ASIC (publication forthcoming).

Case study: Frequency and placement of advertisements for unlisted, unrated debentures a proxy for quality and safety AUS

Unlisted, unrated debentures can be high-risk products, in which companies borrow money from investors with a promise to repay with interest at a future fixed date. They are not listed on a secondary market, and so can be difficult to on-sell. They also do not have a credit rating.

ASIC research found that some investors in unlisted, unrated debentures were attracted to them by advertising or marketing and used the frequency and placement of advertisements as a proxy for quality. Some investors also specifically noted that they were influenced by spokespeople:

"I thought, there was some famous guy who was coming on the ad, I can't remember who it was … [I thought] if this company [is] not a good company then this man wouldn't be putting his name to it and standing there, and speaking for the company."[40]

The research also found that investors' understanding that they were investing in unlisted, unrated debentures was very low.

Case study: Financial funeral products advertising creates a new social 'norm' AUS

ASIC research into how people pay for funeral insurance found that many people who acquired the product had been exposed multiple times to funeral insurance advertising on television. All these people shared the idea that people not only can, but should formally prepare for the cost of their own funeral, suggesting the advertising had created a new 'social norm' around prepaying for funerals that did not exist previously in the community.[41] In Australia, the advertising created an 'invented need' for many consumers in a market where alternative options may be more fit for purpose.

Sales pitches

Firms can also draw on their expertise in the art of the sales pitch to influence us. This can include:

- the full range of tactics, from persuasive to pressure sales
- leveraging social factors, such as likeability, trust and reciprocity[42]
- harnessing known biases to bring their preferred messages front of mind for consumers.

---

[40] REP 126.
[41] REP 292.
[42] See, for example, RB Cialdini, *Influence: The psychology of persuasion, Revised edition*, Collins Business, New York, 2007.

For example, using statements such as 'while supplies last' and 'act quickly' can create an artificial scarcity and steer consumers and investors to act or invest quickly, motivated by a fear of missing out.[43]

A consistent theme from ASIC's consumer research is that many consumers pay more attention to, and are more influenced by, what they are told by sales staff than disclosure documents.[44]

Case study: Car yard sales strategies makes it hard to say no to 'add-on' insurance

AUS

ASIC research about how consumers are influenced to buy low-value 'add-on' insurance in car yards found that persuasive and pressure sales tactics leveraged social rapport, trust and conflict avoidance.[45]

For example, sales staff:

- established **trusting relationships** with customers in order to gain a competitive advantage in marketing a wide variety of products to them
- used small expenses like coffee to lend themselves a sense of **'likeability', professionalism and quality** (psychologists argue that people are much more likely to say 'yes' to requests made by people they like) and create a sense of **reciprocity** (which may nudge consumers to reward a kind action with another positive action)
- applied subtle pressure to consumers, leveraging our tendenacy to avoid conflict and/or the perception of being unreasonable. For example, sales staff might spend up to 40 minutes pre-filling application forms, even though they had not been asked to do so by consumers.

"They also gave me nine different options that I didn't want … This one seemed like if I had to take anything, this was the better option. I'll take the gunshot to the knee, thanks.**"**

[43] AFM, *AFM publiceert herziene beleidsregel Informatieverstrekking* ('AFM publishes Revised Policy Rule on the Provision of Information', Dutch only), media release, 31 December 2018. On artificial scarcity, see A Mathur, G Acar, M Friedman, E Lucherini, J Mayer, M Chetty & A Narayanan, *Dark patterns at scale: Findings from a crawl of 11K shopping websites*, paper, July 2019.
[44] See, for example, REP 470 and REP 126.
[45] REP 470.

Case study: Unbalanced communication distracts attention from the downside NL/UK

Firms can be unbalanced in their communication with consumers, disproportionately emphasising the advantages of a product or service. For example, fixating on using credit to buy a certain product may divert attention from the financial consequences of a decision. For example, research by the UK Financial Conduct Authority (FCA) found that consumers did not typically perceive overdrafts to be loans because firms often included overdrafts within the 'funds available', positioning the debt as part of the consumer's balance.[46]

Choice architecture

More generally, firms structure the choice architecture – that is, the features in an environment, noticed and unnoticed, that influence our decisions and actions. These design features are present at every stage of product design and distribution, and include how the product or service is framed, options are presented, processes are organised and products are 'sold'. Choices can never be framed completely neutrally – 'any way a choice is presented will influence how the decision-maker chooses'.[47]

For example, firms may:

- **make the decision to purchase easy** by simplifying and shortening messages and processes (among other things) to minimise the cognitive load, and eliminating frictions to reduce the 'hassle factor' and facilitate acting on impulse. For example, the streamlined approval and delivery processes in payday loans make it quick and easy for us to take out these high-interest loans
- **strategically time product offers** to either capture or distract our attention. For instance, offers made to increase credit when we are close to our limits will attract attention, while limiting the time we have to make decisions or review material will distract attention. Some firms are also adept at providing **product information just in time** to influence our decisions (e.g. texts sent to customers to influence their usage of credit cards, at the point in time the credit card is being used), or at a time when it is unlikely to attract our attention (e.g. drip pricing, where we are told an initial lower cost, and then told about additional costs after we have committed to the purchase).

---

[46] Jigsaw Research, *Consumer credit qualitative research: Credit cards and unauthorised overdrafts* (PDF 1.1 MB), report commissioned by the FCA (UK), April 2014; AFM, *Applying behavioural insights to promote better credit decisions: Impact of the choice architecture on decision-making* (PDF 368 KB), report, October 2016.
[47] E J Johnson, S B Shu, B G C Dellaert, C Fox, D G Goldstein, G Haubl, R P Larrick, J W Payne, E Peters, D Schkade, B Wansik & E U Weber, 'Beyond nudges: Tools of choice architecture' (PDF 211 KB), *Marketing Letters*, vol. 23(2), May 2012.

Case study: Defaults make it easy to go with the firm's preferred options **AUS/NL**

Defaults are options that are automatically selected when someone fails to actively decide otherwise. For example:

- ASIC identified that some Australian banks were defaulting loyal customers whose term deposits had expired into new term deposits. The 'new' term deposits had significantly lower interest rates than available alternatives – for example, at-call accounts.[48]
- The AFM has idenitifed the use of 'prefilled' amounts in credit-worthiness assessments influencing levels of reported income and expenditure. Prefilling amounts to assess credit-worthiness for phone credit led to a 20.5 percentage point increase in reported incomes within a 5% range either above or below the prefilled amount, and 15.8 percentage point increase in reported expenditure amounts close to the prefilled amount. [49]

Case study: Framing of cost influences preferences and judgment **NL**

Firms also influence consumer choices by how they frame the costs.[50] For example, by:

- **stressing the available balance** on revolving credit facilities (rather than repayment over the long term), which can play into consumers' tendency to underestimate future consequences and overestimate short-term gains
- **presenting cost as relatively small and ongoing**, which can lead people to underestimate the actual cost and impact of credit decisions. This can be done by highlighting ongoing costs, such as monthly instalments and/or interest, rather than total aggregate cost. For example, AFM research showed consumers prefered a shorter contract length (reducing the cost of the credit) when they were provided information about preferred duration instead of monthly instalments.

---

[48] ASIC, Report 185 *Review of term deposits* (REP 185), March 2010.

[49] AFM, *Prefilling income and expenditure has large and unwanted effects on telephone credit applications: a field experiment*, news article, March 2018.

[50] AFM, *Applying behavioural insights to promote better credit decisions: Impact of the choice architecture on decision-making* (PDF 368 KB), report, October 2016.

Case study: Add-on insurance sales processes fatigue consumers and rush decisions **AUS**

In ASIC research about the sale of low-value add-on insurance in car yards, consumers reported finding the structure of the sales process **fatiguing, overwhelming and rushed, minimising their attention and thinking time.**[51]

The insurance was offered at the end of a long day, when consumers had already been required to make multiple decisions – for example, about the car they wanted to purchase, what extras to include and how to finance the purchase. Many consumers explicitly mentioned that by the time they were offered insurance, they were expecting the experience to be over and wanted to leave.

“All our time and energy went into finding the right car, we didn’t even think of insurance.**”**

Consumers were subject to **overwhelming demands to make multiple decisions** at or around the same time. Some consumers felt they were **rushed through decisions** on insurance, as one or a small number in a string of decisions, and were confused about what each product actually was.

“… it’s like a maze. **”**

Context

The context (both physical and digital) in which firms interact with us also significantly affects how we are influenced. Each different context influences the time, attention and weight we give to the information and offers we receive – and firms can time and design their product information, offers and options accordingly.

For instance, we interpret and engage with digital information differently to how we do so with hard copy information, and we also process information differently on different digital devices. We take less time to process information on screens, and can be more likely to skim read and rush our thinking. This tendency can be even stronger with small devices, such as mobile phones – particularly when we use them while we are distracted, ‘on the go’, or in a hurry, increasing the chance that rushed or shallow thinking and visual biases will affect our decisions.[52]

In contrast, our engagement with hard copy information provided in face-to-face sales is influenced by other factors, including:

- the physical environment (e.g. a closed room with a sales person present,[53] or our own home)

---

[51] REP 470.
[52] See, for example, J Dunaway, *Mobile vs. computers: Implications for news audiences and outlets* (PDF 352 KB), Discussion Paper #D-103, Shorenstein Center on Media, Politics and Public Policy, August 2016; and S Benartzi, *The smarter screen: Surprising ways to influence and improve online behavior*, Portfolio, New York, 2015.
[53] REP 470.

- social factors (e.g. we place greater trust and pay more attention to sales staff than to the disclosure documents)[54]
- information being obscured by sales staff (e.g. physically covering up relevant information or distracting us with idle banter while we are trying to read).[55]

The net effect is that we are often nudged by firms in nuanced and context-specific ways towards decisions that may or may not be in our best interests, in ways we may or may not be aware of. Firms may, for example, intentionally, recklessly or inadvertently nudge us towards products and services that are not fit for purpose, or that prioritise commercial interests over consumer interests.

Equally, many firms have the means and resources at their disposal to improve consumer outcomes through nudging that is fair to consumers.

Firms with misaligned incentives may have the incentive, opportunity and means to work around and undermine disclosure

Firms can also work around, undermine and outpace disclosure requirements, particularly where the incentives of firms do not align with good consumer outcomes. This key issue has been identified and explored in particular by Professor Lauren Willis,[56] including in work conducted with ASIC.[57] Regulators should also consider how firms might react when preparing regulations, including disclosure.

Some firms can work around and undermine disclosure requirements

Some firms can work around and undermine disclosure requirements by strategically timing when the disclosure is provided (just in time to influence our preferences and decisions) and making small design adjustments (e.g. to size, order, consistency, placement and format) that significantly affect the extent to which and how we access, assess and act on the information presented.[58]

---

[54] REP 470.
[55] LE Willis, 'Performance-based remedies: Ordering firms to eradicate their own fraud', *Law and Contemporary Problems*, vol. 80(3), 2017, pp. 3, 13.
[56] LE Willis, 'When nudges fail: Slippery defaults' (PDF 656 KB), *The University of Chicago Law Review*, vol. 80, 2013, pp. 1154–1229.
[57] Professor Willis keynote speech at an ASIC forum, 'Regulating for results: Beyond disclosure' unpublished (2017); and LE Willis, M Hastak & J King, 'Customer confusion audits: Lessons from the use of consumer confusion audits in the United States', research report for ASIC (publication forthcoming).
[58] For example, LE Willis, M Hastak & J King, 'Customer confusion audits: Lessons from the use of consumer confusion audits in the United States', research report for ASIC (publication forthcoming).

Case study: High-cost small amount loan warning work arounds — AUS

Australia's Consumer Action Law Centre[59] found that providers of high-cost small amount loans (commonly known as 'payday loans') were presenting compulsory warnings on their websites in ways that were likely to reduce the warnings' impact – for instance, by:

- putting the warning at the bottom of the webpage, so the consumer would not need to scroll past it to apply for the loan
- partially obscuring the warning with an unrelated message
- timing the warning to pop up only after the consumer had put in their contact details (by which time they had likely made a mental commitment to the loan).

Case study: Detrimental messaging — NL

Firms can undermine the information they are legally required to provide in disclosure documents by providing inconsistent or contrary information through other channels.

One approach taken in the Netherlands to tackle this issue is to prescribe that information provided about a financial product or service, including advertisements, not be 'detrimental' to the information to be supplied or made available under the law.

In the Revised Policy Rule on the Provision of Information, the AFM provides an example: if the (mandated) risk indiciator shows that a risk associated with a product is very high, an advertisement about the same product that claims that the risk is 'relatively low' will be considered to be detrimental. The advertisements detracts from ('doet afbreuk aan') the mandated disclosure.[60]

Case study: Confusing product names — AUS/NL

Products can be named in ways that result in consumer confusion. More detailed descriptions about products contained in disclosure documents have been ineffective in resolving this confusion.

---

[59] Consumer Action Law Centre, *What warning? Observations about mandated warnings on payday lender websites* (PDF 1.98MB), report, August 2013. See also ASIC, Report 426 *Payday lenders and the new small amount lending provisions* (REP 426), March 2015.
[60] AFM, *AFM publiceert herziene beleidsregel Informatieverstrekking* ('AFM publishes Revised Policy Rule on the Provision of Information', Dutch only), media release, 31 December 2018.

For example:

- In Australia, ASIC found that the labelling and description of some investments as being **'capital protected'** or **'capital guaranteed'** led some investors to (mis)understand that their entire capital was protected and that they would get 100% of the money they invested back when their product matured. This 'capital protection' was a key reason why investors in capital protected products chose their investments. In fact, 'protected' may really mean 'protection if certain conditions are met', and if those are not met, then the capital is at risk of loss.[61]
- In the Netherlands, about three in ten consumers holding **interest-only mortgages** (known in the Netherlands as 'free of down payment mortgages'[62]) are not completely aware of the fact that the total amount of the debt is still due at the end.[63] More than half of the total Dutch mortgage debt (which is nearly €700 billion) is interest only.

Some firms can outpace and outmanoeuvre government attempts to improve disclosure and regulate choice architecture

Governments have responded to some of the issues raised in this section of the report by attempting to make improvements to disclosure or regulating choice architecture. However, as government regulations are generally static and slow to change, it is difficult to pre-empt or respond to firm strategies to work around or undermine the new regulation's intended purposes.

Case study: Improved disclosure – Superannuation dashboard vulnerable to manipulation **AUS**

Product dashboards for superannuation products are intended to provide a 'simple' snapshot summary of a superannuation product that appears on a fund website. Dashboards were designed to be radically shorter than PDSs, to encourage member engagement and help people compare superannuation products by providing prescribed key information about risks, returns, return targets, investment options and asset allocation.

ASIC undertook standard user testing with consumers to refine the design of the dashboards and found, among other things, that people were sensitive to small design details (e.g. size, order, consistency, placement, format and terminology). At the same time, consumer preferences for information presentation varied considerably.[64]

[61] REP 341.
[62] 'Aflossingsvrije hypotheken' in Dutch.
[63] Novio Research, *Onderzoek: Aflossingsvrije hypotheken* (PDF 1 MB) ('Research: Free of down-payment mortgages', Dutch only), report commissioned by the Dutch Banking Association (Nederlandse Vereniging van Banken), November 2018.
[64] ASIC, Report 378 *Consumer testing of the MySuper product dashboard* (REP 378), December, 2013; ASIC, Report 455 *Consumer testing of the Choice product dashboard* (REP 455), December, 2015.

Professor Hazel Bateman and colleagues later tested the disclosure in a series of laboratory experiments, to try to assess actual impact on consumer choices (this work was not commissioned by ASIC). They found that:

- the choices of more than 35% of participants were not significantly impacted by any of the prescribed information items
- even simplified risk information was irrelevant to the decisions of approximately three quarters of participants
- only 5% of participants used all or almost all of the prescribed information and, at times, these participants used the information in unexpected ways.

The research of Hazel Bateman and colleagues also identified that despite the intention behind the dashboard to focus consumers on matching risk-adjusted returns to their own risk profile, the most influential factor on consumer choice was the asset allocation pie chart.[65] Having focused on the pie chart, consumers appeared to use a relatively simple '1/n heuristic' approach to allocation (preferring to spread resources evenly across funds or categories). When applied to already highly diversified investment options, this type of diversification can result in outcomes that are not informed by appropriate risk–return trade-offs.

A key implication of this research is the ease with which consumer choice could be manipulated through the 'dashboard' form – for example, by relabelling or reweighting asset allocation information used in the pie chart.

This case study highlights a significant limit of standard user testing, even when it is conducted with real consumers from an appropriate target group. It cannot assess actual impact on consumer and firm behaviour; nor on consumer outcomes, or prevent unexplored backfires.

Case study: Choice architecture regulation – Slippery overdraft coverage default	US

In an attempt to protect consumers from high overdraft fees, US regulators introduced a no overdraft fee default, where customers had to opt in to overdraft coverage (in effect a high cost loan for fees paid when an account is in overdraft).

However, the banks were opposed to this change. As a result, banks leveraged their direct access to consumers and used a range of behavioural techniques to counter the default.

Banks **minimised transaction barriers** to almost eliminate the cost of opting in. They introduced quick 'push buttons' on automatic teller machines (ATMs), stationed bank employees at ATMs to sell opting in and assist customers to do so, and telephoned likely overdraft targets directly.

[65] H Bateman, LI Dobrescu, BR Newell, A Ortmann & S Thorp, 'As easy as pie: How retirement savers use prescribed investment disclosures' (PDF 1.28 MB), *Journal of Economic Behavior & Organization*, vol. 121, 2015, pp. 60–76.

Banks **created conditions that triggered decision and judgement biases** that encouraged opting in (and neutralised those that would strengthen the effect of the default). Banks used:

- messages and labels that encouraged people to preserve the overdraft status quo and positioned the default in a way that triggered loss aversion. For instance, banks called overdraft products 'account protector', 'courtesy pay' and 'bounce protection' and used messages like 'Don't lose your ATM and debit card overdraft protection'
- multiple marketing channels to focus on the immediate benefits presented by overdraft coverage (immediate access to funds) and positioned the coverage as a free 'perk' they were offering their customers.

Banks also **acted to shape people's preferences** by relying on social norms that encouraged opting in, with messages such as 'most of our customers have taken up coverage'.[66]

[66] LE Willis, 'When nudges fail: Slippery defaults' (PDF 656 KB), *The University of Chicago Law Review*, vol. 80, 2013, pp. 1154–1229.

One size
disclosures
do not fit all

One size does not fit all – the effects of disclosure are different from person to person and situation to situation

> Like other forms of regulation, mandated disclosure requirements are often 'one size fits all' interventions – yet people and contexts differ and shift. It is hard to predict the individual and context-specific differences in how we will behave, make decisions, and engage with and process information.

People differ … so does the context

As people, we all differ both from person to person and from situation to situation in how we make financial decisions. There are multiple nuanced dimensions to these differences including:

› different decision-making processes

› different decision-making styles

› people seeking out and responding to different sources for information and advice

› different ways of engaging with information.

The following case studies illustrate each of these dimensions in the context of a number of different financial products and services.

Decision-making processes

Case study: Different decision-making processes – Insurance **AUS**

As an example of how decision-making processes vary between individuals, Figure 6 sets out the wide variety of approaches consumers take when seeking to purchase insurance. This data comes from research undertaken by the Insurance Council of Australia (ICA).[67]

Consumers take each step to varying degrees, but the process is not always sequential. The only two stages in the processes shared by most consumers were 'starting to look' and 'deciding'. All other stages were undertaken variously by only 'some' or 'few' consumers.

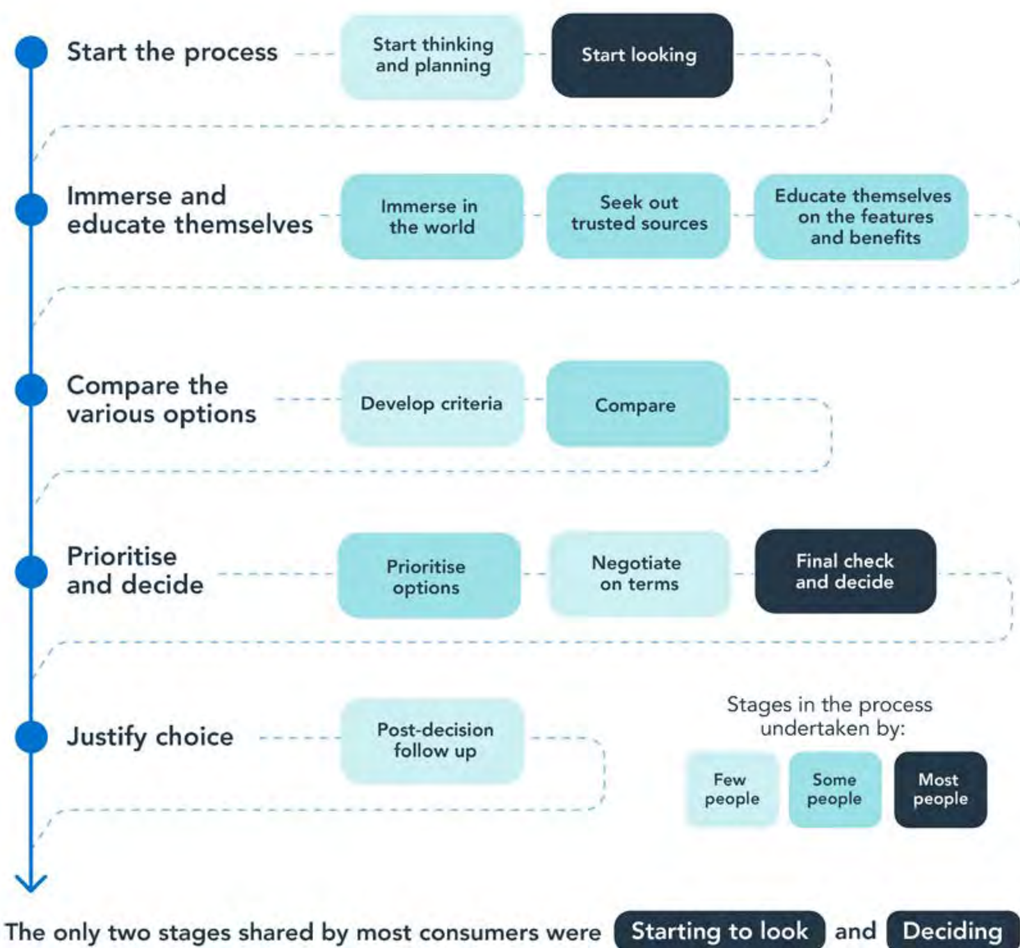
---

[67] ICA, *Consumer research on general insurance product disclosures*, report, February 2017. See also REP 416, p. 12, which found that some consumers making enquiries about home insurance policies spent a lot of time and effort comparing policies according to multiple criteria, while others compared only two policies, based on price only.

Another component of the ICA research found that the extent to which consumers read the detailed PDS and/or summary KFS varied significantly (where they were aware of the these documents):

- **PDS:** 16% did not read; 35% read some but not all; 47% detailed or quick read of all; 2% couldn't recall
- **KFS**: 8% did not read; 22% read some but not all; 69% detailed or quick read of all; 1% couldn't recall.

Figure 6: Decision-making process for purchasing home insurance



Note: Qualitative research, including 30 face-to-face ethnographies with Australians in three capital cities and two regional centres. In addition, 120 digital longitudinal ethnographic case studies, nationally distributed sample. Research was conducted in 2016. See Table 6 for the information shown in this figure (accessible version).

Decision-making styles

Decision-making styles are diverse and context specific. For example, we may have different feelings of confidence, be more or less self-directed, be able to search and research more or less.

While there is no perfect way to reflect this diversity, one way to examine decision processes is to identify and characterise common features or styles.

Case study: Different decision-making styles **NL**

The AFM has segmented financial consumers into four different 'financial decision types', based on extensive qualitative and quantitative research: see Table 2.[68]

The main point of this segmentation was not to put consumers into rigid 'boxes', but rather to illustrate that the simplistic, singular concept of 'the consumer' does not exist. Instead, deep and complex diversity exists. These segments do not neatly correlate with demographic segments (e.g. socio-economic background, age, gender, race).

Under this segmentation, consumers might be classified under different segments in different contexts, and it is also possible to shift from one segment to another over time. An individual consumer's decision-making style is not constant, and can shift from situation to situation. For example, consumers seeking to purchase a car may be 'in control' regarding the decision to purchase the car, but 'convenience-oriented' regarding subsequent decisions to purchase add-on insurance.

Table 2: AFM segmentation of financial consumers into financial decision types

Decision type	Description
In control	Consumers read information and want to be well informed. Statements that are especially indicative of 'in control' consumers are: › 'I search for a lot of information.' › 'I take a lot of time.' › 'I consider many options.' › 'I search until I have found the best product.'
Ambitious	Consumers are quite similar to the 'in control' group, but are much more risk seeking (or less risk averse). Statements that resonate with them are: › 'I'm willing to run some risk.' › 'I like to try new products.'
Convenience-oriented	Consumers don't want any hassle or to invest much effort themselves. They often prefer these statements: › 'I try to limit the amount of information.' › 'I consider a limited amount of alternatives.' › 'I talk little about it with friends and family.' › 'I stop searching as soon as I have found a product that suits me.' › 'I prefer certainty.' › 'I prefer products that I know.'

[68] AFM, *Rapport: Kennismaking met de financiële consument* ('Report: Meet the financial consumer', Dutch only), report, April 2005.

Decision type	Description
Advice-oriented	Consumers rely heavily on others, be it professional financial advisers or friends and family. They often employ a financial adviser and have a relatively high tendency towards statements such as: › 'I let others figure out as much as possible.' › 'I trust advisers easily.' › 'I talk a lot about it with friends and family.'

Sources of information and advice

Just as decision-making processes and styles vary, so do the sources of information and advice we draw on.

Case study: Different information and advice gathering processes – Initial public offerings (IPOs) **AUS**

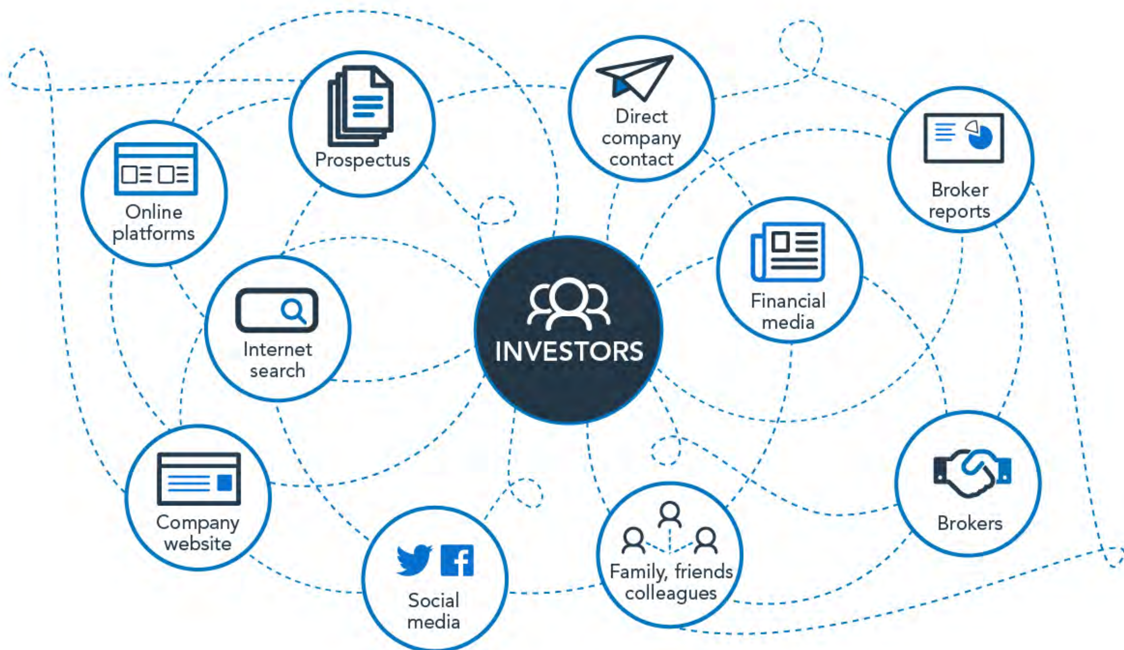
ASIC research into IPO investors found that consumers used different processes to gather information and advice, depending on the specific IPO they were considering.

Most investors did not consistently use set sources of information, nor were their information-gathering processes linear (even among the most experienced in the sample). Rather, the process was more like a matrix in which various sources were used to obtain information, and the consumer pieced together a 'story' about the IPO that they considered to be sufficient to enable them to decide if they wanted to invest.[69]

For a representation of the different sources of information and advice IPO investors used, see Figure 7.

[69] WhereTo Research, *Factors that influence retail investors in IPOs* (Attachment to REP 540), August 2017.

Figure 7: Different sources of information and advice for IPO investors



Sample: Qualitative research with a sample of 52 Australian investors in Victoria, New South Wales, Queensland, Western Australia and South Australia. Research was conducted between December 2016 and February 2017.

Engagement with information

Finally, there is also high variation in how we engage with information.

Case study: Differences in engagement with disclosure **AUS**

Relevant research findings about **investor and superannuation engagement with PDSs** include that consumers:[70]

- engage with PDSs differently, depending on their level of interest and reading style
- varied not only in *how much* they were interested in a topic, but also in *what* they wanted to know.

Consumers also differed in how they used PDSs:

- 'visual' people said they thought more easily when information was presented in bar and pie charts
- 'numbers' people preferred to read actual numbers in table form

[70] Bell, S, *The provision of consumer research regarding financial product disclosure documents*, Financial Services Working Group, ASIC (unpublished material), December 2008, pp. 16–17.

- some people referred to the contents extensively to navigate the documents
- some people ignored the contents and instead used elements like headings, dot points and colour cues.[71]

Another component of this research found that:

- almost two thirds (64%) of research participants were not able to locate all relevant fees in the PDS for a managed investment
- less than half (47%) of participants were able to locate all fees in the PDS for a superannuation fund.

Relevant research findings about **investor engagement with prospectuses for IPOs**[72] include that investors used:

- various parts of prospectuses differently and to different extents
- prospectuses differently from investment to investment.

This is consistent with other ASIC research that has found that consumer preferences for information presentation varies significantly – there is no single, universal approach that suits everyone.

Context matters

The context in which we access disclosure also significantly affects how we engage with it, including:

- the **physical environment** – for example, our engagement with a disclosure document in a quiet, undisturbed office environment, without time pressures, is likely to vary significantly from how we might engage with one on a mobile device on a busy train, or in a financial adviser's office with time constraints and the adviser present
- the **distribution channel** – for example, online environments can vary, and time constraints, like a digital countdown timer, can be imposed to rush our decisions
- our **emotional mindset and physical state** – we may be more inclined to purchase or spend more on financial decisions that are inherently emotional (e.g. taking out a mortgage to purchase a home, or insurance to cover a new car). Our personal emotional mindset and physical state, as well as any competing demands on our attention, will affect how much time, attention and cognitive resources, if any, we dedicate to the disclosure, the way in which we process it and the extent, if any, to which we act on it.

[71] Bell, S, The provision of consumer research regarding financial product disclosure documents, Financial Services Working Group, ASIC (unpublished material), December 2008, p. 30.
[72] REP 540, paragraphs 137–142.

No universal approach to disclosure can meet the needs of all

Most disclosure is generalised. It is not designed to maximise a particular consumer's understanding of the product as it applies to them individually. It also fails to account for the fact that any one piece of information is used and understood differently from person to person and situation to situation.[73] While some forms of disclosure are undoubtedly useful for some consumers in some contexts, no one disclosure will suit the needs of all consumers.

[73] ASIC, *Submissions of the Australian Securities and Investments Commission – Round 6: Insurance* (PDF 247 KB), Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, October 2018, paragraph 29(a).

Disclosure can
backfire in
unexpected ways

In the real world, disclosure can backfire in unexpected ways

At worst, disclosure creates unintended detrimental outcomes for some consumers – in effect contributing to consumer harm (e.g. by increasing rather than decreasing trust in conflicted advisers, and decreasing rather than increasing credit card repayments). Ongoing monitoring of disclosure is needed because of these unexpected effects.

Disclosure, like some other forms of regulatory intervention, can backfire. Consumer outcomes can be negatively affected by disclosure – either directly, because we react to the disclosure in unexpected ways, or indirectly, because the disclosure permits market conduct that is not in our best interests.

As the case studies below highlight, we may react to disclosures in ways that are opposite to those intended by policy makers. For example disclosure of:

› advisers' conflicts of interest can *increase* the trust we place in them

› credit card minimum repayment amounts can *reduce* the repayments we make.

Case study: Conflicts of interest disclosure increase consumer trust in sales staff **US**

A common public policy response to conflicts of interest is to make them transparent to consumers through disclosure, on the assumption that 'sunlight disinfects' (i.e. that making the conflict known to consumers will empower them to apply an appropriate 'discount'). However, a large body of research now indicates that disclosing conflicts of interest may in fact have unintended negative effects on both consumers and salespeople.

Some **consumers** may place an even higher degree of trust in the salesperson (as a result of the salesperson's candidness). Other consumers may interpret the disclosure as intended and distrust the advice, but still feel pressured to take the advice in order to satisfy the salesperson's interests, or out of fear of signalling their distrust to the salesperson.[74]

Salespeople may feel that, having made the appropriate disclosure, they are now morally licensed to recommend biased choices to their customers.[75]

[74] D de Meza, B Irlenbusch & D Reyniers, *Disclosure, trust and persuasion in insurance markets* (PDF 425 KB), IZA Discussion Paper No. 5060, July 2010.
[75] DM Cain, G Loewenstein & DA Moore, 'When sunlight fails to disinfect: Understanding the perverse effects of disclosing conflicts of interest', *Journal of Consumer Research*, vol. 37(5), 2011, p. 836; S Sah, *Conflicts of interest and disclosure* (PDF 345 KB), research paper, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, November 2018.

Case study: Anchoring on minimum credit card repayment amounts reduces repayments **UK/US**

Credit card statements must include 'minimum repayment amounts' – that is, the minimum amount consumers must pay to stay current on their accounts and avoid late fees and other penalties. There is a large body of international research that has found that the amount consumers repay can be disproportionately influenced by this minimum repayment figure (an effect known as anchoring). This results in some consumers being *more likely to make minimum repayments* or repayments close to the minimum.[76] Researchers at the FCA (UK) have found that removing the minimum repayment amount from manual repayment screens (which is not part of mandatory disclosure) had a large positive effect in two online hypothetical experiments, significantly increasing the value of repayments made.[77]

In one experiment they found that removing the minimum payment amount increased the value of repayments made by nearly 20%.

Case study: Misunderstanding AFM approval **NL**

When the AFM approves a prospectus, it checks for consistency, comprehensiveness and clarity. This process does not include judging the trustworthiness of the issuer, or whether projected yields will be realised. However, the words 'approved prospectus' have been found to lead consumers to make unanticipated assumptions about products and issuers, and the way and extent to which the AFM had vetted them:[78]

- In 2012, one third of investors thought that 'approval' meant that the prospectus contained correct information, whereas in fact the AFM does not check whether the information is correct. In 2016, this misconception had increased to 43% of retail investors.
- Both in 2012 and 2016, 15% of Dutch retail investors assumed that an approved prospectus means that the AFM has approved the investment. About 3 out of 10 investors incorrectly thought that an approved prospectus also meant that the issuer is dependable.

[76] N Stewart, 'The cost of anchoring on credit card minimum repayments' (PDF 59 KB), *Psychological Science*, vol. 20, 2009, pp. 39–41; D Navarro-Martinez, L Salisbury, K Lemon, N Stewart, W Matthews & A Harris, 'Minimum required payment and supplemental information disclosure effects on consumer debt repayment decisions' (PDF 803 KB), *Journal of Marketing Research*, vol. 48, 2011, pp. S60–S77; S Jiang & L Dunn, 'New evidence on credit card borrowing and repayment patterns', *Economic Inquiry*, Western Economic Association International, vol. 51(1), January 2013, pp. 394–407; D Bartels & A Sussman, *Anchors, target values, and credit card payments* (PDF 3.14MB), Fed/GFLEC Financial Literacy Seminar, University of Chicago Booth School of Business, 5 May 2016.
[77] P Adams, B Guttman-Kenney, L Hayes & S Hunt, *Helping credit card users repay their debt: a summary of experimental research* (PDF 991 KB), research note, FCA, July 2018.
[78] AFM, *Many misunderstandings about the meaning of prospectus approval by AFM*, news article, 6 December 2012; AFM, *AFM consumer monitor 2016 Q1*, unpublished.

A warning
about warnings

A warning about warnings

> There is emerging evidence from financial services regulators about the limitations of the effectiveness of warnings that firms have to display about the risks and features of certain products and services. There is, for instance, some evidence of the effectiveness of warnings on our understanding of the risks associated with products, and in encouraging us to avoid unsuitable or harmful products.
>
> Warnings are not a cure-all for problems in financial services markets. Further research to evaluate their effectiveness is warranted.

Warnings do not always work as intended

Warnings are a specific form of disclosure designed to draw attention to the particular risks or features of a financial product or service. When financial firms are required to draw attention to specific risks or features, it is expected that we will properly factor them into our decision-making process and weigh up the risks identified against our own risk profile and preferences. As researchers at the FCA (UK) have identified, warnings have become a regulatory tool of choice for policy makers because they are easy to mandate firms to provide and are assumed to be effective in informing consumers and influencing our behaviour.[79]

In practice, we can ignore, overlook, misunderstand or misremember warnings. They can have no impact on our behaviour, or even backfire. The FCA researchers have suggested that 'warning fatigue' may be a relevant factor, given our finite attention, and the over-proliferation of warnings in relation to so many of the risks we encounter in our day-to-day lives.[80]

Gaining an understanding of the effectiveness of this tool is particularly important when the risks or features being warned about are significant and/or when policy makers place high reliance on warnings alone to offer consumer protection.

Case study: Credit warning has no impact on behaviour **NL**

Dutch credit providers must include the warning 'Caution! Borrowing money costs money' in advertisements for consumer credit. The warning was intended to:

- create awareness among consumers by pointing out the consequences of the credit
- counter the image presented in some of the credit advertisements that borrowing for consumer purchases is perfectly normal
- encourage consumers to carefully consider their choices.

---

[79] L Smart, 'Don't look here: Do risk warnings really work?', article, *Insight: Opinion and analysis from the FCA*, 13 December 2018.

[80] L Smart, 'Don't look here: Do risk warnings really work?', article, *Insight: Opinion and analysis from the FCA*, 13 December 2018. See also A Chesterfield & E Fradkin, Learning from experience in financial servicesv, article, *Insight: Opnion and analysis from the FCA*, 28 August 2019.

Empirical research[81] established that the credit warning had no short-term effects on the behaviour of consumers, or the way that they experienced the advertisements. The experiment did not show that the credit warning had any influence on the frequency with which consumers clicked on website banners, the way in which they browsed online, or the choices that they made when requesting a quote. This suggests that, at least in the short term, the warning was not influencing behaviour; however, long-term beneficial effects cannot be ruled out.

Similarly, the credit warning did not appear to affect the way in which consumers experienced advertisements and their general perception of borrowing money. In a laboratory study, there was also no effect on the steps consumers intended to take when taking out a loan. Showing a fictional advertisement that contained the existing warning, an alternative warning or no credit warning had hardly any effect on the attitudes to borrowing money.

This case also reflects important changes in emphasis by the regulator, from 2009, when the AFM declared the credit warning a success[82], because within half a year more than 80% of the Dutch population could recite the warning, to 2016, when it was found to be ineffective because it did not influence actual consumer behaviour[83].

Case study: High-cost small amount loan warnings – 'I don't think anyone reads that' **AUS**

In Australia, providers of high-cost small amount loans must provide a warning about the expense of borrowing small amounts of money, including messages about the availability of alternative sources of assistance and low/no cost sources of credit.[84]

Research commissioned by ASIC indicated that current warnings were unlikely to be effective in disrupting consumers' immediate transactions.[85] In general, research participants who had taken out small amount loans were sceptical about the impact of the existing message and many felt that it lacked relevance to them and their current needs. Many consumers who were interviewed for the research had difficulty remembering whether they had seen the existing warning message or recalling the content.

---

[81] AFM, Caution! Borrowing money costs money – A study of the effectiveness of a warning in credit advertisements (PDF 1 MB), report, December 2016.
[82] AFM, Let op! Geld lenen kost geld is succes *[Translated: Watch out! Borrowing money costs money is a success]*, report, December 2009.
[83] AFM, Let op! Geld lenen kost geld' geen onmiddellijk effect in verkoopomgeving *[Translated: 'Watch out! Borrowing money costs money' no immediate effect in sales environment]*, report, December 2016.
[84] There is a current proposal to introduce a similar warning statement for consumer leases of household goods, to help consumers make better decisions, including by informing of the availability of alternatives. ASIC will have the power to modify the requirements for the proposed warning statement for consumer leases and the current warning statement for small amount loans.
[85] C Stavros, R Russell, K Westburg & M Banks, *Development of consumer advice (warning) messages for SACC and consumer lease products*, research report for ASIC (publication forthcoming). The researchers undertook in-depth interviews with 30 consumers – 20 had taken out a small amount loan, and 10 had entered into a consumer lease for household goods.

"For a lot of people … they've got to get the money to pay a bill, put food on the table. School kids might need new shoes and they can't afford them right now. These people are desperate enough to go into these loans. Messages like that are neither here nor there."

Small amount loan customer, aged 35–49

A threshold reason why the warning was not effective was that information asymmetry is not a root cause of the problem. Consumers who participated in the research largely understood existing options and the high costs of small loans; and were aware of the potential for longer-term issues that could result from a cycle of small loans. Instead the key drivers for consumers decisions to take out small amount loans were urgent need; limited choice; and the ease and convenience.

"I'd be on the streets, homeless, if I didn't have this option."

Small amount loan customer, aged 35–49

Case study: General advice warning does not help most consumers to understand the limitations of general advice **AUS**

In Australia, there is an important distinction between 'personal advice' (which triggers a number of important consumer protection obligations) and 'general advice' (which affords minimal consumer protection to consumers). When general advice is provided to a retail client, the financial firm must give a warning that the advice does not take into account the consumer's personal circumstances and, therefore, that the consumer should consider whether the advice is appropriate for them before acting on it.

ASIC research[86] has found that:

- most consumers do not understand the limitations of general advice despite the general advice warning. Less than half (41%) of research participants understood the limitations and most did not indicate that they would take steps to check whether the advice was appropriate for them.
- more than one third (38%) of participants incorrectly thought that the adviser had a responsibily to consider the consumers' financial circumstances
- more than one third (38%) thought that the adviser was acting in the consumers' best interest and 26% thought they were prioritising the consumers' interests
- almost one third (31%) of participants incorrectly thought that the adviser had a responsibility to consider the consumer's financial goals.

[86] ASIC, Report 614 *Financial advice: Mind the gap* (REP 614), March 2019.

Some of the reasons suggested for why the warning was not effective include:

- viewing the warning simply as a means for advisers and companies to 'cover themselves'
- assuming that the adviser would flag any issues that need to be considered
- trusting the adviser not to recommend something that would make them worse off

"I'd kind of just gloss over it … I just know that disclaimers are thrown everywhere on everything …**"**

Case study: 'Strong' mutual fund warning had no impact on 'high knowledge' investors

US

Research conducted in the United States tested the impact of the inclusion of a 'past performance' warning in mutual fund advertisements.[87] The experiment assessed the impact of the warning on research participants' expectations of returns and attitudes towards the relevant mutual fund.

Among other things, the warning stated that 'mutual funds with a strong past performance revert to the market and underperform their peers' and warned investors not to 'project past performance in the future'.

Within each experimental group, participants were variously shown a typical mutual fund advertisement with no disclaimer (the control group); the current Securities and Exchange Commission (SEC) disclaimer which funds have to display; or the stronger 'past performance' warning drafted by the researchers.

The research found that the strongly worded warning did effectively impact investors assessed by the researchers as having 'low knowledge' but had no impact on investors assessed as having 'high knowledge'.

The researchers suggested that high-knowledge investors may hold stronger beliefs and/or be overconfident in relation to investments and their own abilities, and so may be more resistant to warnings that counter their beliefs.

The research also found that the current SEC disclaimer that firms are required to provide had no impact on return expectations, independent of the financial knowledge of investors.

[87] A Hüsser, 'The role of investors' objective financial knowledge on the assessment of risk disclosures in mutual fund advertisements', *Journal of Financial Services Marketing*, vol. 20(1), pp. 5–22, March 2015.

Warnings can backfire

It is not just that policy makers can overestimate the effectiveness of warnings. Some mandatory warnings might even be counterproductive. The case studies below show that warnings can backfire in unexpected ways, consistent with other forms of disclosure. This evidence suggests a need for caution in the use of warnings, particularly in the absence of evidence that they will work as intended by policy makers.

Case study: Minimum repayment warnings reduce repayments of some customers — US

Minimum payment warnings on credit card statements were introduced with the aim of challenging consumers' present-bias and encouraging them to pay off debts faster. In the US, the warning credit card providers must include is a printed table comparing the difference in total interest paid if the customer pays only the minimum amount each month or were to pay off the total balance amount in three years.

Different combinations of disclosure have been provided to different subsets of consumers based on specific eligibility rules.

Using data available from the Consumer Financial Protection Bureau (CFPB), researchers found that these different combinations of disclosure had very different impacts on repayment behaviours and some caused borrowers to pay **less** than they had without the warning:[88]

- accounts receiving the three year payment calculation and standard minimum repayment warning saw a 0.6% overall reduction in the fraction of balances paid and a 1.4% decline in the account months paid in full
- accounts receiving the three year payment calculation without the more strongly worded warning caused some borrowers who had been paying their monthly balances in full to pay less

In contrast:

- accounts receiving a non-amortisation warning and the three year calculation saw payments increase by US$24 per month and had a small but insignificant increase in the average fraction paid
- accounts receiving the minimum repayment warning and three year calculation increased payments by only US$4 per month.

[88] J Wang & BJ Keys B J, 'Perverse nudges: Minimum payments and debt paydown in consumer credit cards' (PDF 509 KB), *Penn Wharton Public Policy Initiative*, Book 25, 2014. Note on data: The CFPB credit card database (CCDB) contains credit card accounts from large US credit card issuers, covering a large fraction of total outstanding balances in the market between 2008 and 2012. The statistics presented in this case study are derived from a subsample of issuers.

Case study: Social media risk warning reduce consumer understanding of risk **UK**

In a series of behavioural experiments in simulated social media environments, the FCA (UK) investigated the impact of the timing and design of risk warnings in advertising tweets by firms on the attractiveness of the tweets to consumers, as well as consumer searches and understanding.

The FCA found that, for character-limited social media, standalone compliance (the inclusion of a mandatory risk warning alongside positive information provided by firms in tweets about products) correlated with a reduction in the number of consumers who searched for information and in their understanding of risks. It also correlated with an increase in consumers choosing less suitable products.[89] The FCA researchers concluded that the warning had backfired.[90]

---

[89] This research is consistent with Monash Universtity research (see the case study on p. 10) and AFM research (see the case study on p. 11). All are examples of lab experiments where there is an unambiguous best choice (dominating other choices on all aspects).

[90] LT Mullet, L Smart & N Stewart, *Blackbird's alarm call or nightingale's lullaby? The effect of tweet risk warnings on attractiveness, search, and understanding* (PDF 4.02 MB), Occasional Paper 47, FCA, December 2018.

Conclusion

Policy makers have heavily relied on mandated firm disclosure and warnings in consumer protection, and used them to drive competition in many financial services markets around the world – arguably becoming default responses to problems that are diagnosed as information asymmetry market failures.

Regulation has traditionally required firms to provide us (as consumers) with specific information because it has been assumed that, with this information, we will be:

- able to protect ourselves from harmful products and services
- equipped to buy products that are fit for purpose and offer the best value for money.

ASIC, the AFM and other regulators have, however, identified limitations to disclosure over a number of years. This report has described how:

- disclosure does not solve the complexity in financial services
- disclosure must compete with firms for consumer attention
- firms can work around and undermine disclosure requirements
- one size does not fit all – the effects of disclosure are different from person to person, and situation to situation.

Further, the report has identified that these limitations are not only contained to longer forms of disclosure but also apply to warnings and 'simplified' and 'enhanced' disclosures. Real-world testing and monitoring is required to assess their effectiveness before concluding such disclosures are necessarily 'smarter' or better at achieving good outcomes for consumers.

Disclosure is not then the silver bullet it was once believed to be. It places a heavy burden on consumers to, for example, overcome complexity and sophisticated sales strategies. Some research suggests that disclosure may be used more often by those of us who are already more informed and engaged.[91] And it can be less effective than intended or ineffective in solving regulatory problems – or even backfire, creating new, unanticipated risks for consumers.

This raises both opportunities and challenges for policy makers, regulators and industry to progress public policy discussions *beyond* disclosure, and understand and address consumer harms on a case-by-case basis.

---

[91] On the related topic of financial advice, Bhattacharya et al. found that investors who most need the financial advice are least likely to obtain it. U Bhattacharya, A Hackethal, S Kaesler, B Loos, & S Meyer, 'Is unbiased financial advice to retail investors sufficient? Answers from a large field study', *The Review of Financial Studies*, vol. 25(4), pp. 975–1032, April 2012. Calcagno & Monticone's model shows that advisers disclose their superior information only to the most knowledgeable investors. They also cite experimental evidence from Mexico that less-informed consumers indeed receive less information from financial institutions about saving and credit products than more experienced customers: see R Calcagno & C Monticone, 'Financial literacy and the demand for financial advice', *Journal of Banking & Finance*, vol. 50, pp. 363–380, January 2015.

While it is clear that disclosure still has a role to play in retail financial services markets – for instance, in contributing to market transparency, integrity and efficiency – no one regulatory tool can be a cure-all for all regulatory problems. Which tool, or combinations of tools, will be fit for purpose in any particular case requires:

- a deep understanding of the underlying problem
- regard to behaviourally informed insights, such as those set out in this paper – for instance, by increasing regulatory focus on complexity, choice architecture and how (financial) decisions are framed and made.

While the limits of generalised, mandatory 'one size fits all' disclosure are clear, there is promise in the opportunities available to firms to deliver good consumer outcomes. For example, firms can tailor and improve their product information and give it to consumers 'just in time'.

Alternative regulatory tools that may improve consumer outcomes in some contexts include product design, governance and distribution.

Regardless of the type of intervention, regulators should continue to contribute to the evidence base of what works by monitoring the effect of interventions over time.

It is also incumbent on industry not to hide behind technical compliance with disclosure obligations. Firms that are proactive in aligning their product design, distribution and communications with consumer needs, capabilities and expectations will build customer trust and minimise regulatory costs.

Appendix: Accessible versions of figures and notes

Accessible versions of figures

This section of the appendix is for people with visual or other impairments. It provides the underlying information for the figures presented in this report.

Table 3: Complexity of ubiquitous financial services and products – Credit cards and insurance

Credit cards: Some of the features	Insurance: Some of the features
Fees: › reward programs › dishonour fees › late fees › annual account-keeping fees › fees for exceeding credit limit › international transaction fees › cash advance fees Direct debits Balance transfer Credit limit increases and decreases Reward and loyalty programs, discounts, and cashback Discounts and promotional offers Additional services: › concierge services Insurance: › travel insurance › credit card insurance Interest rates: › purchase and cash advance › promotional interest rate › balance transfer Interest-free periods and no interest-free periods Charges: › monthly › merchant surcharge Card usage: › dual network – credit and debit › contactless terminal – PayPass and payWave › personal identification number Repayment amounts	Types of insurance: › car › consumer credit › funeral › health › home and contents › life › mobile phone, tablet and laptop › pet › travel Policy inclusions and exclusions Type of coverage – accidental damage versus listed events Level of coverage and exclusions Eligibility Excess amounts Premium costs Fees Assessment of risks requiring insurance Preparations and conduct required to ensure eligibility to make a claim Policy options for contents – new for old versus total value cover Policy options for building – total replacement versus sum insured Extended cover Cooling-off periods Cover note Derogations from standard cover

Note: This is the information shown in Figure 1.

Table 4: Insurance purchase choices using key facts sheets and PDSs

Consumer purchasing choice	Key facts sheet (summary tool)	PDS (detailed tool)
Okay	35%	20%
Bad	11%	10%
Good	41%	41%
No insurance	13%	29%

Note: This is the data shown in Figure 2.

Table 5: Investment decisions of consumers using a summary prospectus, KID and a combination of both

Consumer investment decision	Summary prospectus	Combination	KID
All (€10,000) in best bond	24%	31%	34%
€5,000 to €9,999 in best bond	16%	26%	33%
€3,333 to €5,000 in best bond	29%	18%	9%
€0 to €3,333 in best bond	21%	13%	12%
€0 in best bond	11%	12%	13%

Note: This is the data shown in Figure 3.

Table 6: Decision-making process for purchasing home insurance

Process step	Few people	Some people	Most people
Start the process	› Start thinking and planning	N/A	› Start looking
Immerse and educate themselves	N/A	› Immerse in the world › Seek out trusted sources › Educate themselves on the features and benefits	N/A
Compare the various options	› Develop criteria	› Compare	N/A
Prioritise and decide	› Negotiate on terms	› Prioritise options	› Final check and decide
Justify choice	› Post-decision follow up	N/A	N/A
Key finding	The only two stages shared by most consumers were **Starting to look** and **Deciding**		

Note: This is the information shown in Figure 6.

Notes for Figure 5

The diagram is based on six separate quantitative research studies of consumers who read or used mandated disclosure and/or information. Research findings included products and services from various sectors delivered by a range of channels. Sources include:

- ASIC, Report 416 *Insuring your home: Consumers' experiences buying home insurance* (REP 416), October 2014: 20% of consumers who took out a new home and building insurance policy or considered switching their policy reported that they read the PDS.
- ASIC and EY Sweeney, Report 481 *Australian Financial Attitudes and Behaviour Tracker: Key findings report: Wave 6* March 2018: 16–18% of consumers who purchased and/or made changes to a product – that is, a credit card, home loan, investments (excluding superannuation), personal loan, bank account – in the last six months reported that they had read the PDS; 24% of consumers who had changed jobs in the last six months and compared superannuation funds (to decide where to put their superannuation) reported that they had read the PDS.
- B Custers, S van der Hof & BW Schermer, 'Privacy expectations of social media users: the role of informed consent in privacy policies', *Policy & Internet*, vol. 6, pp. 269–295, October 2017: 17% of consumers who created an account with a website (any) they had not used before always or often read the privacy policy.
- ICA, *Consumer research on general insurance product disclosures*, report, February 2017: 19% of consumers with car insurance and 26% of consumers with travel insurance reported that they used the PDS as an information source pre-purchase (but that it was not the main source of information). Among consumers with home building insurance, 22% reported that they used the PDS, and 23% used the key facts sheet as an information source pre-purchase (but it was not the main source). Among consumers with home contents insurance, 22% reported that they used the PDS, and 19% used the key facts sheet as an information source pre-purchase (but it was not the main source).
- P Nguyen & L Solomon, *Consumer data and the digital economy: Emerging issues in data collection, use and sharing*, Consumer Policy Research Centre, July 2018: 18% of consumers who signed up to a product or service in the last 12 months (channel not specified) reported that they read all or most of the privacy policy or terms and conditions.
- Office of the Australian Information Commissioner (OAIC), *Australian Community Attitudes to Privacy Survey 2017 report*, May 2017: 18% of consumers reported they always read the privacy policy before providing personal information for any product or service (channel not specified); 29% of consumers reported they read the privacy policy when going to any internet site.

Key terms

add-on insurance	General insurance policies that are 'added on' to the sale of a primary product, most commonly with the purchase of a motor vehicle
AFM	Dutch Authority for the Financial Markets
ASIC	Australian Securities and Investments Commission
ASIC research	Research ASIC has either conducted or commissioned
AUS	Australia
CCI	Consumer credit insurance
consumer	Has the meaning given to 'retail client' in s761G of the Corporations Act (AUS)
FCA	Financial Conduct Authority (UK)
ICA	Insurance Council of Australia
ICO	Initial coin offering
IPO	Initial public offering
KID	Key Information Document (NL)
NL	Netherlands
PDS	Product Disclosure Statement – A document that must be given to a retail client for the offer or issue of a financial product in accordance with Div 2 of Pt 7.9 of the Corporations Act 2001(AUS) **Note:** See s761A for the exact definition.
SOA	Statement of Advice – a document that must be given to a retail client for the provision of personal advice under Subdivs C and D of Div 3 of Pt 7.7 of the Corporations Act (AUS) **Note:** See s761A for the exact definition.
UK	United Kingdom
US	United States

Reference list

Adams, P, Guttman-Kenney, B, Hayes, L. & Hunt, S, *Helping credit card users repay their debt: a summary of experimental research* (PDF 990.9 KB), research note, Financial Conduct Authority, July 2018.

AFM, *A closer look at consumer borrowing: An analysis of decision-making behaviour and potential interventions in the consumer credit market* (PDF 428 KB), report, May 2019.

AFM, *A randomized controlled trial on the effectiveness of mandatory investment information*, article, 2019.

AFM, *AFM publiceert herziene beleidsregel Informatieverstrekking [Translation: AFM publishes revised policy provision for information]*, untranslated media release, 31 December 2018.

AFM, *Applying behavioural insights to promote better credit decisions: Impact of the choice architecture on decision-making* (PDF 368 KB), October 2016.

AFM, *Caution! Borrowing money costs money – A study of the effectiveness of a warning in credit advertisements* (PDF 1.01 MB), report, December 2016.

AFM, *Investing in cryptos in the Netherlands: Market survey under Dutch consumers* (PDF 372 KB), 26 June 2018.

AFM, *Let op! Geld lenen kost geld' geen onmiddellijk effect in verkoopomgeving [Translated: 'Watch out! Borrowing money costs money' no immediate effect in sales environment]*, report, 6 December 2016.

AFM, *Let op! Geld lenen kost geld is succes [Translated: Watch out! Borrowing money costs money is a success]*, report, 29 December 2009.

AFM, *Many misunderstandings about the meaning of prospectus approval by AFM*, news article, 6 December 2012.

AFM, *Prefilling income and expenditure has large and unwanted effects on telephone credit applications: a field experiment*, news article, March 2018.

AFM, *Rapport: Kennismaking met de financiële consument [Translation: Meet the financial consumer]*, untranslated report, April 2005.

AFM, *Wet op het financieel Toezicht* (Translation: Act on Financial Supervision), untranslated news article.

ASIC, Report 15 *Hook, line & sinker: Who takes the bait in cold calling scams?* (REP 15), June 2002.

ASIC, Report 126 *Understanding investors in unlisted unrated debenture (UUD) market* (REP 126), April 2008.

ASIC, Report 185 *Review of term deposits* (REP 185), February 2010.

ASIC, Report 279 *Shadow shopping study of retirement advice* (REP 279), March 2012.

ASIC, Report 292 *Paying for funeral, how consumers decide to meet the costs* (REP 292), July 2012.

ASIC, Report 341 *Retail investor research into structured capital protected and capital guaranteed investments* (REP 341), May 2013.

ASIC, Report 361 *Consumer credit insurance policies: Consumers' claims experiences* (REP 361), July 2013.

ASIC, Report 378 *Consumer testing of the MySuper product dashboard* (REP 378), December, 2013.

ASIC, Report 416 *Insuring your home: Consumers' experiences buying home insurance* (REP 416), October 2014.

ASIC, Report 426 *Payday lenders and the new small amount lending provisions* (REP 426), March 2015.

ASIC, Report 455 *Consumer testing of the Choice product dashboard* (REP 455), December 2015.

ASIC, Report 470 *Buying add-on insurance in car yards: Why it can be hard to say no* (REP 470), February 2016.

ASIC, Report 481 *Australian Financial Attitudes and Behaviour Tracker: Key findings report: Wave 6* (REP 481), March 2018.

ASIC, Report 540 *Investors in initial public offering* (REP 540), August 2017.

ASIC, Report 576 *Member experiences with self-managed superannuation funds* (REP 576), June 2018.

ASIC, Report 588 *Consumers' experiences with the sale of direct life insurance* (REP 588), August 2018.

ASIC, Report 614 *Financial advice: Mind the gap* (REP 614), March 2019.

ASIC, Report 622 Consumer credit insurance: Poor value products and harmful sales practices (REP 622), July 2019.

ASIC, *Submissions of the Australian Securities and Investments Commission – Round 6: Insurance* (PDF 247 KB), Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, October 2018.

ASIC, *Financial System Inquiry Interim Report: Submission by ASIC (PDF 961 KB)*, August 2014.

ASIC, *Financial System Inquiry: Submission by ASIC* (PDF 2 MB), April 2014.

Bar-Gill, O, *Seduction by contract: Law, economics, and psychology in consumer markets*, Oxford University Press, Oxford, 2012.

Bartels, D, & Sussman, A, *Anchors, target values, and credit card payments* (PDF 3.14 MB), financial literacy seminar, University of Chicago Booth School of Business, 5 May 2016.

Bateman, H, Dobrescu, LI, Newell, BR, Ortmann, A & Thorp, S, 'As easy as pie: How retirement savers use prescribed investment disclosures' (PDF 1.28 MB), *Journal of Economic Behavior & Organization*, vol. 121, 2015, pp. 60–76.

Bell, S, *The provision of consumer research regarding financial product disclosure documents*, Financial Services Working Group, ASIC (unpublished material), December 2008.

Benartzi, S, *The smarter screen: Surprising ways to influence and improve online behaviour*, Portfolio, New York, 2015.

Ben-Shahar, O & Schneider, CE, 'More than you wanted to know: The failure of mandated disclosure' (PDF 504 KB), *University of Pennsylvania Law Review*, vol. 159, 2011, pp. 647–749.

Bhattacharya, U., Hackethal, A., Kaesler, S., Loos, B., & Meyer, S, 'Is unbiased financial advice to retail investors sufficient? Answers from a large field study', *The Review of Financial Studies*, vol. 25(4), pp. 975–1032, April 2012.

Bossaerts, P & Murawski, C, 'Computational complexity and human decision-making', *Trends in Cognitive Sciences*, vol. 21(12), December 2017, pp. 917–929.

Cain, DM, Loewenstein, G & Moore, DA, 'When sunlight fails to disinfect: Understanding the perverse effects of disclosing conflicts of interest', *Journal of Consumer Research*, vol 37(5), 1 February 2011, pp. 836–85.

Calcagno, R & Monticone, C, 'Financial literacy and the demand for financial advice', *Journal of Banking & Finance*, vol. 50, pp. 363–380, January 2015.

Cialdini, RB, *Influence: The psychology of persuasion, Revised edition*, Collins Business, New York, 2007.

Chesterfield, A & Fradkin, E, 'Learning from experience in financial services', article, *Insight: Opinion and analysis from the FCA*, 28 August 2019

Consumer Action Law Centre, *What warning? Observations about mandated warnings on payday lender websites*(PDF 1.98 MB), report, August 2013.

Custers, B, van der Hof, S & Schermer, BW, 'Privacy expectations of social media users: the role of informed consent in privacy policies', *Policy & Internet*, vol. 6, pp. 269–295, October 2017.

de Meza, D, Irlenbusch, B & Reyniers, D, *Disclosure, trust and persuasion in insurance markets* (PDF 425 KB), IZA Discussion Paper No. 5060, July 2010.

Dubner, SJ, *People Aren't Dumb, The World is Hard* (Episode 340), podcast, Freakonomics, 11 July 2018.

Dunaway, J, *Mobile vs. computers: Implications for news audiences and outlets* (PDF 352 KB), Discussion Paper Series #D-103, Harvard Kennedy School: Shorenstein Center, August 2016.

Effective Disclosure Taskforce, *Too long; didn't read – Enhancing general insurance disclosure* (*Too long; didn't read*), report, Insurance Council of Australia (ICA), October 2015

Elsen, M, van Giesen, R, Elshout, M & Leenheer, J, *Consumenten en financieel advise. Consumentenonderzoek in het kader van de evaluatie van het provisieverbod* [Translation: Consumers and financial advice. Consumer research for the evaluation of the ban on commissions], Dutch only, CentER Data, November 2017.

Fletcher, A, *The role of demand-side remedies in driving effective competition*, Which?, 7 November 2016.

Gabaix, X & Laibson, D, 'Shrouded attributes, consumer myopia, and information suppression in competitive markets' (PDF 147 KB), *The Quarterly Journal of Economics*, vol. 121(2), 2006, pp. 505–540.

Hoekstra, WB, Minister of Finance, 'Uitkomsten onderzoek consumptiefkredietmarkt' ('Results of consumer credit market research', Dutch only), letter to parliament, September 2018.

Hüsser, A, 'The role of investors' objective financial knowledge on the assessment of risk disclosures in mutual fund advertisements', *Journal of Financial Services Marketing*, vol. 20(1), pp. 5–22, March 2015.

ICA, *Consumer research on general insurance product disclosures*, report, February 2017

Jiang, S, & Dunn, L, 'New Evidence on Credit Card Borrowing and Repayment Patterns', *Economic Inquiry*, Western Economic Association International, vol. 51(1), January 2013, pp. 394–407.

Jigsaw Research, *Consumer credit qualitative research: Credit cards and unauthorised overdrafts* (PDF 1.1 MB), report commissioned by the FCA (UK), April 2014.

Johnson, EJ, Shu, SB, Dellaert, BGC, Fox, C, Goldstein, DG, Haubl, G, Larrick, RP, Payne, JW, Peters, E, Schkade, D, Wansik, B & Weber, EU, 'Beyond nudges: Tools of choice architecture' (PDF 211 KB), *Marketing Letters*, vol. 23(2), May 2012, pp. 487–504.

Kahneman, D, *Why we contradict ourselves and confound each other*, interview transcript, 5 October 2017.

Kaptein, M, *Persuasion profiling: How the internet knows what makes you tick*, English edn, Business Contact Publishers, Amsterdam/Antwerp, May 2015.

Kell, P, ASIC Deputy Chairman, *ASIC and behavioural economics: Regulating for real people*, speech, Queensland University Behavioural Economics Group (QuBE) symposium, 18 October 2016.

Lunn, P, Bohacek, M, Somerville, J, Choisdealbha, AN & Mcgowan, F, *PRICE Lab: An investigation of consumers' capabilities with complex products*, report, Economic & Social Research Institute, May 2016.

Malbon, J & Oppewal, H, *(In)effective disclosure: An experimental study of consumers purchasing home contents insurance*, research report of a study commissioned by the Financial Rights Legal Centre, Monash University: Australian Centre for Financial Studies, 2018.

Mathur, A, Acar, G, Friedman, M, Lucherini, E, Mayer, J, Chetty, M & Narayanan, A, *Dark patterns at scale: Findings from a crawl of 11K shopping websites*, paper, July 2019.

Merritt, A, Effron, D A & Monin, B, *Moral self-licensing: When being good frees us to be bad. Social and Personality Psychology Compass*, 4/5, 344–357, May 2010.

Mons, M & Baelemans, C, *Value chain excellence in retail*, presentation slides (untranslated), IG&H Consulting, 14 July 2011.

Mullet, LT, Smart, L & Stewart, N, *Blackbird's alarm call or nightingale's lullaby? The effect of tweet risk warnings on attractiveness, search, and understanding* (PDF 4.02 MB), Occasional Paper 47, FCA, December 2018.

Navarro-Martinez, D, Salisbury, L, Lemon, K, Stewart, N, Matthews, W, & Harris, A, 'Minimum Required Payment and Supplemental Information Disclosure Effects on Consumer Debt Repayment Decisions' (PDF 803 KB), *Journal of Marketing Research*, vol. 48, March 2011, S60-S77.

Nguyen, P & Solomon, L, *Consumer data and the digital economy: Emerging issues in data collection, use and sharing*, Consumer Policy Research Centre, July 2018

North, G, 'Efficiency, fairness & irrationality: Incompatible or complementary?', *Banking & Finance Law Review*, vol. 24(2), February 2009, pp. 311–342.

Novio Research, *Onderzoek: Aflossingsvrije hypotheken* (PDF 1 MB) ('Research: Free of down-payment mortgages', Dutch only), report commissioned by the Dutch Banking Association (Nederlandse Vereniging van Banken), November 2018.

OAIC, *Australian Community Attitudes to Privacy Survey 2017 report*, May 2017.

Risseeuw, P, Kerste, M, Baarsma, B & Dosker, R, *Evaluatie provisieregels complexe producten* *[Translation: Evaluation provision rules complex products]* (PDF 710 KB) (SEO-rapport nr. 2010-44), untranslated report, SEO Economisch Onderzoek, September 2010.

Sah, S, *Conflicts of interest and disclosure* (PDF 345 KB), research paper, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, 1 November 2018.

Sedgwick, K, *Crowdfunding: 46% of last year's ICOs have failed already*, news article, Bitcoin.com, 23 February 2018.

Slovic, P, 'Perception of risk', *Science*, vol. 236(4799), 17 April 1987, pp. 280–285.

Smart, L, 'Don't look here: Do risk warnings really work?', article, *Insight: Opinion and Analysis from the FCA*, 13 December 2018.

Stavros, C, Russell, R, Westburg, K & Banks, M, *Development of consumer advice (warning) messages for SACC and consumer lease products*, research report for ASIC (publication forthcoming).

Stewart, N, 'The cost of anchoring on credit card minimum repayments' (PDF 59 KB), *Psychological Science*, vol. 20, 2009, pp. 39–41.

Sunstein, CR, *Sludge audits*, Harvard Public Law Working Paper No. 19-21, April 2019.

van Steen, R, Visser, J, Eecen, A, *De effectiviteit van de Financiële Bijsluiter* *[Translation: The effectiveness of the Financial Information Leaflet]*(PDF 382KB), untranslated report, TNS Nipo, 13 March 2009.

Wang, J, & Keys, BJ, 'Perverse nudges: Minimum payments and debt paydown in consumer credit cards' (PDF 509 KB), *Penn Wharton Public Policy Initiative*, Book 25, 2014.

WhereTo, *Factors that influence retail investors in IPOs* (Attachment to REP 540), August 2017.

Willis, LE, *Decision-making and the limits of disclosure: The problem of predatory lending*, Research Paper No. 2005-14, Loyola-LA Legal Studies, June 2005.

Willis, LE, Keynote speech at an ASIC Forum, *Regulating for results: Beyond disclosure* (unpublished), 2017.

Willis, LE, 'Performance-based remedies: Ordering firms to eradicate their own fraud' *Law and Contemporary Problems*, vol. 80(3), 2017, pp 7–42.

Willis, LE, 'When nudges fail: Slippery defaults' (PDF 656 KB), *The University of Chicago Law Review*, vol. 80, 2013, pp. 1154–1229.

Willis, LE, Hastak, M & King, J, 'Customer confusion audits: Lessons from the use of consumer confusion audits in the United States', research report for ASIC (publication forthcoming).

Zeisberger, S, Borsboom, C, Janssen, D-J, Strucks, M & Zijlstra, W, *Investor risk perception in the Netherlands* (PDF 807.3KB), research paper, AFM, 2018.

Agenda Item #5

Discuss Any Other Matters Brought Before the Committee