

The Vulnerable Consumer of Financial Services: Law, Policy and Regulation

Peter Cartwright*

Executive Summary

A common justification for the regulation of financial services is the need to protect the consumer. Economic and social explanations and justifications for regulation both focus in part on the consumer as the principal beneficiary of regulation. Consumers, however, are a heterogeneous rather than a homogeneous group. Some are affluent, some are not. Some are highly educated, others not. Protecting such a wide and diverse group presents the authorities with a range of challenges.

One challenge is to design policies which take appropriate account of the interests of those consumers who might be described as disadvantaged or, to use the language adopted by this paper, vulnerable. The concept of vulnerability has been examined by a number of commentators in a range of fora. That some consumers are more vulnerable than others has also been recognised by legislation. We know that vulnerable consumers exist, even if we may disagree about how to identify them, and about how their interests might best be addressed.

The principal purposes of this paper are twofold.

First, the paper considers how “the vulnerable consumer” should be understood. It does this first by looking at how vulnerability has been conceptualised by commentators and, secondly, by examining how the law currently takes account of the interests of consumers who might be described as vulnerable. This discussion reveals that we can conceive of “vulnerable consumers” in different ways, and that we may even disagree about whether the term “vulnerable” is the right label to describe those who are particularly susceptible to loss or harm. It also reveals that a range of legal provisions make reference to vulnerable consumers, and that a range of tools, or techniques, take account of the interests of such consumers.

Secondly, part three of the paper establishes a “taxonomy of vulnerability”. This is a novel framework consisting of a set of elements which, taken together, help to identify where vulnerability is liable to exist. The elements are classified by the paper as:

Information vulnerability

Pressure vulnerability

Supply vulnerability

Redress vulnerability; and

Impact vulnerability.

If the discussion ended there, then while the paper might be of academic interest, it would be limited practical utility. For that reason, the paper goes on to identify how key stakeholders (legislators and regulators in particular, but also firms and others) might use the taxonomy in practice to ensure that the interests of vulnerable consumers are appropriately addressed. A number of examples can be given by way of illustration.

To take a simple example, if vulnerability results from information gaps (what this paper calls information vulnerability) this might be tackled directly through information remedies such as disclosure. In some cases this will be an appropriate response. But the limitation of such action is also apparent. Vulnerable consumers may not be well placed to utilise the information provided, and a more nuanced approach may therefore be required. In particular, behavioural economics has demonstrated the difficulties presented by regimes that rely upon consumers to process and act upon information. In addition, if disclosure is deemed to be an appropriate response questions remain as to the basis upon which this should be achieved. Should the law mandate what has to be disclosed and how, or are firms allowed a degree of discretion? Regulatory changes, both organisational and substantive, should be considered in this context. The replacement of the FSA by new regulatory forms signal changes not only in structure but also in approach. Furthermore, the impact of the Retail Distribution Review is still uncertain, but a reduction in access to advice remains a possibility.

As a second example, if the cause of consumer vulnerability is a particular susceptibility to pressure (classified in this paper as pressure vulnerability) which tools are available to counteract that? Banning particular forms of supply? Providing additional remedies (such as cooling off periods) to

consumers? How, if at all, can we reduce the likelihood of salespeople straying from legitimate persuasive techniques to aggressive and illegitimate practices?

A final example concerns redress vulnerability. We might argue that consumers will sometimes only be appropriately protected where they are able to hold firms to account by obtaining redress. Obtaining that redress might require knowledge, confidence and resources, characteristics that will be in short supply among many vulnerable consumers. Again, what tools might be used to overcome this vulnerability? Should individual or collective litigation be further facilitated? Would it be better to rely on forms of alternative dispute resolution such as the Financial Ombudsman Service? Might there be greater scope for regulators to play in obtaining redress for consumers, or for ensuring that firms implement more responsive mechanisms for the handling of complaints? Changes to the regulatory landscape have already been noted, and we should also consider how the Coalition's approach to reorganising consumer redress and advice might impact upon consumer redress.

Such decisions require careful consideration and, ultimately, political judgement. It is not suggested that the answers will be easy. Nevertheless, it is argued that the taxonomy provides a useful tool through which the questions can be addressed. While these might be viewed as questions primarily for legislators and regulators, they have implications for others too. For example, firms concerned about whether their sales and marketing methods are fair to vulnerable consumers may decide to use the taxonomy to help answer this. Issues of vulnerability are relevant to marketing and sales training and not simply to compliance. Furthermore, as the Coalition Government further encourages individuals to take responsibility for financial well-being, and changes significantly the landscape under which consumer protection operates, it becomes imperative that the framework under which these changes occur pay appropriate regard to the interests of the vulnerable.

While it will not always provide a definitive answer, it should help both to clarify the questions to be asked, and to illuminate the responses. It is submitted, therefore, that the paper will be of interest to a wide range of parties concerned with the relationship between firms and consumers, including legislators, regulators, firms, consumers and their advisors.

Although the focus of this paper is on financial services, the arguments are also relevant to other sectors.

Contents

Introduction

1. Part One: Who are Vulnerable Consumers?

1.1. Introduction

1.2 Vulnerable Consumers: the Literature

2. Part Two: Vulnerable Consumers, Law and Financial Regulation

2.1 Introduction

2.2 Vulnerable Consumers and Unfair Commercial Practices

2.3 Vulnerable Consumers and Consumer Credit Law

2.4 Vulnerable Consumers and Unfair Terms

2.5 Vulnerable Consumers and the Financial Ombudsman Service

2.6 Treating (Vulnerable) Consumers Fairly and the FSA

2.7 Vulnerable Consumers and Private Law

2.7.1 *Duress*

2.7.2 *Undue Influence*

3. Part Three: Rethinking Vulnerability

3.1 Introduction

3.2 The Rationales for Regulation and the Taxonomy of Vulnerability

3.3 Informational Vulnerability

3.4 Addressing Informational Vulnerability

3.4.1 *Mandatory Disclosure*

3.4.2 *Weaknesses of Mandatory Disclosure*

3.4.3 *Addressing the Weaknesses*

3.4.4 *Controlling False and Misleading Information*

3.4.5 *The Relationship between Positive and Negative Informational Responses*

3.5 Pressure Vulnerability

3.6 Addressing Pressure Vulnerability

3.6.1 *Banning High-Pressure Modes of Supply*

3.6.2 Prohibiting Aggressive Commercial Practices through Broad Standards

3.6.3 Cooling Off Periods

3.6.4 Pressure Vulnerability and the Consumer as Defendant

3.7 Supply Vulnerability

3.8 Addressing Supply Vulnerability

3.8.1 Competition-Based Responses

3.8.2 Social Obligations

3.8.3 Governmental Supply

3.9 Redress Vulnerability

3.10 Addressing Redress Vulnerability

3.10.1 Facilitating Individual Litigation

3.10.2 Collective Redress

3.10.3 Alternative Dispute Resolution: the Financial Ombudsman Service

3.10.4 Regulatory Enforcement and Redress

3.11 Impact Vulnerability

3.12 Addressing Impact Vulnerability

3.12.1 Compensation Schemes

3.12.2 Social Force Majeure and Consumer Debt

4. Part Four: Conclusions

Introduction

A common justification for regulation of financial services is the need to protect the consumer.¹ The Financial Services Authority (FSA – soon to be replaced by the Consumer Protection and Markets Authority) has consumer protection as one of its statutory objectives and, along with the need to maintain financial stability, consumer protection is seen as perhaps the principal aim of financial regulation. Economic explanations for regulation (which focus on justifying intervention on the grounds of market failure) frequently identify information asymmetry between suppliers and consumers and externalities (particularly in the form of systemic risk) as rationales for financial regulation.² Social justice or non-economic explanations for regulation point to a range of possible justifications for regulation, including distributive justice, paternalism and community values.³ These explanations and justifications all focus in part on the consumer as the principal beneficiary of regulation.

Consumers are, however, a heterogeneous, rather than a homogeneous group. Some are reasonably well informed and reasonably observant and circumspect.⁴ Others may be ignorant, unthinking and credulous.⁵ Most probably fall somewhere between these two positions. Some will be relatively wealthy, others relatively poor. Some will have extensive experience of financial markets, others not so. Some will be confident and assertive, others more easily persuaded. Protecting such a wide range of individuals appropriately is a challenge.

The principal objectives of this paper are twofold. First, the paper considers how “the vulnerable consumer” should be understood. Secondly, the paper establishes a taxonomy of vulnerability which provides a framework for examining how vulnerable consumers can best be protected. The focus is on the protection of the financial services consumer, and therefore on financial services law,

*Professor of Consumer Protection Law, School of Law, University of Nottingham. The author gratefully acknowledges the assistance of the Financial Services Research Forum, and in particular Professors James Devlin and Nigel Waite, in producing this Paper.

¹ See e.g. P Cartwright *Banks Consumers and Regulation* (Hart, 2004); P Cartwright *Consumer Protection in Financial Services* (Kluwer, 1999); A Page and R Ferguson, *Investor Protection* (Weidenfeld and Nicolson, 1992); C Ford and J Kay ‘Why Regulate Financial Services?’ in F Oditah (ed) *The Future of the Global Securities Market* (Clarendon Press, 1996) 145.

² See e.g. D Llewellyn *The Economic Rationale for Financial Regulation* (FSA Occasional paper 1, April 1999); H Davies “Why Regulate?” Henry Thornton Lecture (City University Business School, 4 November 1998).

³ See A Ogus *Regulation: Legal Form and Economic Theory* (OUP, 1994) chap 3.

⁴ The test from Case C-210/96 *Gut Springenheide* [1998] ECR I-4657.

⁵ A term used in *Charles of the Ritz Distributors Corp. v FTC* 143 F. 2d. 676 (2d circuit, 1944).

regulation and policy, broadly understood. However, it is submitted that the lessons learned have relevance for other sectors.

The paper approaches its tasks as follows. First, it seeks to identify what might be meant by “vulnerable consumers”. Secondly, it examines how the law currently takes account of the particular interests of vulnerable consumers in the area of financial services. Thirdly, it suggests a new taxonomy of vulnerability which allows us to consider how such vulnerability might most appropriately be tackled using the tools available. Finally, conclusions are drawn.

The paper will be of interest to anyone who has to deal with consumer law and policy in the financial sector. For example, it contains ideas for firms to consider when they are advising consumers and drafting consumer-facing documents. In addition, it presents a taxonomy that legislators and regulators might take into account when considering what they expect of firms (and of consumers). Furthermore, consumers and their advisors might contemplate the implications of the findings for themselves and those whom they advise. While the regulatory landscape looks set to change, the challenges facing firms and consumers will remain.

1. Part One: Who are Vulnerable Consumers?

1.1. Introduction

This part considers what we might mean by “vulnerable” consumers with particular reference to the existing academic literature.

1.2 Vulnerable Consumers: the Literature

This paper views vulnerability as relative.⁶ Consumers as a group may be vulnerable compared with other players in the market (for example traders) or vulnerable compared with other consumers. The focus of the paper is on those consumers who are particularly vulnerable when compared with other consumers.

The paper is not concerned primarily with those consumers who are so vulnerable that they lack the capacity to look after their own interests, although it is important that any regime makes provision

⁶ For discussion see *What Do We Mean by Vulnerable and Disadvantaged Consumers?* (Consumer Affairs Victoria Discussion Paper, 2004) para 3.1. It is recognised that in one sense of the word, even generally sophisticated consumers may be vulnerable in relation to particular markets, but this paper is not using the word vulnerable in that sense.

for them.⁷ It concentrates instead on those consumers who have capacity, but who are nevertheless appropriately regarded as (relatively) vulnerable. Academic literature has constructed a number of possible definitions of consumer vulnerability which focus on different factors. Some studies focus on how individual characteristics make consumers vulnerable. For example, Ringold saw vulnerable consumers as those who have “diminished capacity to understand the role of advertising, product effects or both”.⁸ Smith and Cooper-Martin argued similarly that vulnerable consumers are those who are “more susceptible to economic, physical, or psychological harm in, or as a result of economic transactions because of characteristics that limit their ability to maximise their utility and well-being.”⁹ These studies focus on the difficulty that consumers have in playing the role traditionally expected of consumers by classical economics - that of “rational maximisers of their own utility” - because of their individual characteristics. Even if the term “characteristics” is taken to include personal states (such as grief) as well as more permanent characteristics (such as age or cognitive limitations) this focus on individual characteristics might be viewed as a little narrow. Vulnerability might also pertain to other personal circumstances (such as low income or indebtedness) and to lack of choice. In an important Discussion Paper, Consumer Affairs Victoria (hereafter CAV) emphasise the importance of this relationship, viewing consumer vulnerability as “the exposure to the risk of detriment in consumption due to the interaction of market, product, and supply characteristics and personal attributes and circumstances.”¹⁰ This broad explanation of vulnerability has particular strengths in that it reveals the context within which individual characteristics operate. It is also broadly consistent with the approach taken by the *Thoresen Review of Generic Financial Advice*.¹¹ The Review’s Final Report identified a series of “drivers of vulnerability”. Among the most financially vulnerable (that is, those who were most vulnerable to the consequences of poor decision-making), those drivers included supply side factors, such as lack of access to commercial advisors, personal economic circumstances, such as having limited savings or protection, and individual characteristics, such as having literacy problems or limited knowledge of products.

⁷ See for example the Mental Capacity Act 2005.

⁸ DJ Ringold “Social Criticisms of Target Marketing: Process or Product” (1995) 38 *American Behavioural Scientist* 578 at 584.

⁹ NC Smith and E Cooper-Martin “Ethics and Target Marketing: The Role of Product Harm and Consumer Vulnerability” (1997) 61 *Ethics and Target Marketing* 1 at 4. There is helpful discussion of various definitions in S Menzel Baker, JW Gentry and TL Rittenberg “Building Understanding of the Domain of Consumer Vulnerability” (2005) 25(2) *Journal of Macromarketing* 1 at 2.

¹⁰ Above n.4.

¹¹ O Thoresen *Thoresen Review of Generic Financial Advice: Final Report* (HMSO, 2008) p 26.

An alternative way of explaining vulnerability is set out by Burden.¹² He argued that consumers may be vulnerable for two main reasons: first, because they may find it more difficult to obtain or to deal with information needed to make appropriate purchasing decisions, and second, because they may suffer greater loss than other consumers by making inappropriate purchasing decisions.¹³ On this basis he identifies seven vulnerable groups: the elderly, the young, the unemployed, those with a limiting, longstanding illness, those in low-income households, members of ethnic minorities and those with no formal educational qualifications.¹⁴ While this is a useful starting point, it might be argued that it ignores other elements that contribute towards consumer vulnerability. This point is further developed below.

A few words should be said here about terminology. Terms other than “vulnerable” could be used to describe the consumers who are the subject of this article. CAV suggest that where characteristics of vulnerability persist, the consumer may be described better as “disadvantaged”.¹⁵ Borrowing from the work of Andreasen, Menzel Baker *et al* also see a distinction between disadvantage and vulnerability. They argue that disadvantaged consumers are those who are “particularly handicapped in achieving adequate value for their consumer dollar”.¹⁶ By contrast, they see consumer vulnerability as being: “a state of powerlessness that arises from an imbalance in marketplace interactions or from the consumption of marketing messages and products.”¹⁷ Wilhelmsson uses alternative terms, distinguishing vulnerable consumers from “less privileged” consumers, and using the latter term to refer primarily to wealth and social status.¹⁸ He argues that it is misleading to think of particular groups of consumers as being vulnerable because “all consumers are vulnerable in some respect” and (as noted above) vulnerability can be situational. Wilhelmsson further argues that the notion of the vulnerable consumer, which he sees as stigmatic, “attempts to remedy inadequate abilities” while that of the less privileged consumer “looks at variations in needs.”¹⁹ There is a danger that using terms such as “vulnerable consumer” creates the impression of there being “them and us”. The term “vulnerable consumer” thus could be viewed as inadequate to reflect the broad range of factors that form the subject of this article. Nevertheless, it is suggested that it is useful as shorthand to reflect a particular susceptibility to detriment beyond

¹² R Burden *Vulnerable Consumer Groups: Quantification and Analysis* (OFT Research Paper 15, April 1998).

¹³ *Ibid* at p. 5.

¹⁴ *Ibid* at pp. 7-10.

¹⁵ As a result, disadvantaged consumers are vulnerable consumers, but vulnerable consumers are not necessarily disadvantaged consumers. Above n.4 at p 3.

¹⁶ Above n.7. See also A Andreasen *The Disadvantaged Consumer* (Free Press, 1975).

¹⁷ *Ibid* at 7.

¹⁸ T Wilhelmsson “The Informed Consumer v the Vulnerable Consumer in European Unfair Commercial Practices Law – A Comment” in G Howells, a Nordhausen, D Parry and C Twigg-Flesner (eds) *Yearbook of Consumer Law 2007* (Ashgate, 2007) 211 at p 213.

¹⁹ *Ibid* at p 213.

the norm faced by some consumers. The factors that give rise to that particular susceptibility are considered in more detail below. Before examining those, it is helpful to identify what the law says about vulnerable consumers of financial services.

2. Part two: Vulnerable Consumers, Law and Financial Regulation

2.1 Introduction

This part of the Paper examines how consumer law, broadly understood, currently takes account of the interests of vulnerable consumers. In large part, although not exclusively, the law has addressed the interests of such consumers through provisions which prevent unfair practices. Some of the provisions considered below have been examined in other work for the FSRF on fairness in financial services.²⁰

2.2 Vulnerable Consumers and Unfair Commercial Practices

The implementation of the Unfair Commercial Practices Directive by the CPRs is revolutionising consumer law in the UK and has important implications for financial services.²¹ At their core, the CPRs tackle unfair practices which distort the economic behaviour of consumers so that they take transactional decisions that they would not otherwise have taken. They are divided into four main parts. First, they list 31 commercial practices which are considered unfair in all circumstances. Secondly, they prohibit misleading commercial practices. Thirdly, they prohibit aggressive commercial practices. Finally, they include a “general prohibition” which attempts to future proof the law by acting as a form of safety net.²²

The provisions will be examined in more detail below in the light of the proposed conception of vulnerability. It should be noted initially that while the CPRs generally judge practices by the

²⁰ See in particular P Cartwright *Fairness, Financial Services and the Consumer in an Age of Principles-Based Regulation: Competing Visions for Competitive Markets* (FSRF) and P Cartwright “Conceptualising and Understanding Fairness: Lessons for and from Financial Services” chap 11 in M Kenny J Devenney and L Fox O’Mahoney *Unconscionability in European Private Financial Transactions* (Cambridge: Cambridge University Press, 2010).

²¹ There is a wide range of helpful literature on the Directive. See for example G. Howells, H-W. Micklitz and T. Wilhelmsson *European Fair Trading Law: The Unfair Commercial Practices Directive* (Aldershot: Ashgate, 2006); S. Weatherill and U. Bernitz (eds) *The Regulation of Unfair Commercial Practices under EC Directive 2005/29* (Oxford: Hart, 2007); H Collins (ed) *The Forthcoming EC Directive on Unfair Commercial Practices* (Dordrecht: Kluwer, 2004); H Collins “Harmonisation by Example: European Laws against Unfair Commercial Practices” (2010) 73(1) MLR 89.

²² See G Abbamonte “The Unfair Commercial Practices Directive and its General Prohibition” in S. Weatherill and U. Bernitz (*ibid*) p 11.

objective standard of the average consumer, this can be varied in certain cases. Distinctions are drawn on the bases of those to whom the practice is directed, and whether there are clearly identifiable groups who are particularly vulnerable to the practice. First, regulation 2(2) states that in determining the effect of a commercial practice on the average consumer where it reaches or is addressed to a consumer or consumers, account shall be taken of “the material characteristics of such an average consumer including his being well informed, reasonably observant and circumspect.” In most cases, this test will apply. Consumers are expected to live up to this (fairly high) standard. This test reflects that adopted by the European Court of Justice in cases on misleading advertising and trademarks.²³ The introduction of the average consumer test in the Directive was something of a trade off to reach agreement. Across Europe, different images of the consumer have been found. Germany, for example, has tended to judge practices etc from the perspective of the gullible consumer. The test in the CPRs seems broadly to reflect the approach previously taken in trade descriptions law in the UK. In *Burleigh v Van den Berghs and Jurgens Ltd* it was stated that to fall foul of the Trade Descriptions Act 1968 a description must be likely to mislead “the average member of the shopping public” and that “it is not enough that we should be sure that an unusually careless person might be misled...[or] a person who is dyslexic, short-sighted, or of less than average intelligence.”²⁴

However, there are two variations to this which are particularly significant for this paper. First, where the practice is directed at a particular group of consumers “a reference to the average consumer shall be read as referring to the average member of that group.”²⁵ So, where the practice is directed at a group who might not be expected to reach the standard of the “well informed, reasonably observant and circumspect” consumer, this will be taken into account. Second, where there is a clearly identifiable group of consumers who are particularly vulnerable to either the practice or the underlying product because of “mental or physical infirmity, age or credulity in a way which the trader could reasonably be expected to foresee” and the practice is “likely to materially distort the economic behaviour only of that group” then average consumer means an average member of that group.²⁶ It is through this provision that account can be taken of vulnerable consumers. This has implications for a variety of commercial practices, particularly those that might

²³ For further details see C Twigg Flesner, D Parry, G Howells and A Nordhausen *An Analysis of the Application and Scope of the Unfair Commercial Practices Directive* (DTI, 2005).

²⁴ [1987] BTLC 337. See RJ Bragg *Trade Descriptions* (OUP, 1990) p 43 for comment. The Trade Descriptions Act 1968 was replaced by the CPRs.

²⁵ Regulation 2(4).

²⁶ Regulation 2(5). According to paragraph 2(6) paragraph 5 is “without prejudice to the common and legitimate advertising practice of making exaggerated statements which are not meant to be taken literally.”

be misleading to some consumers, and those that might be aggressive for some consumers. This is further developed in the context of informational and pressure vulnerability below.

The relationship between the CPRs and financial services law requires some explanation. The Directive is viewed as imposing maximum harmonisation. In other words, member states are not permitted to impose restrictions additional to those contained in the Directive. They must provide the protection contemplated by the Directive, but no more. However, member states are permitted to impose more restrictive or more prescriptive requirements where financial services are concerned provided such measures are essential to ensure that consumers are adequately protected against unfair commercial practices, and provided they are proportionate to attaining that objective.²⁷ The FSA has argued that there is no need for additional rules in our Handbook because it already contains principles and rules which have the same effect as the Directive.²⁸

2.3 Vulnerable Consumers and Consumer Credit Law

The Consumer Credit Act 1974 is the principal piece of legislation to govern the relationship between lenders and consumer borrowers. While it might be argued that the whole of the Act is of interest to consumers, the part of particular relevance to vulnerable consumers is that dealing with unfair relationships (sections 140A to 140D). Under s.140A a court can make an order in relation to a credit agreement if it finds that the relationship between the creditor and the debtor is unfair because of one or more of the following:

- (a) any of the terms of the agreement or of any related agreement;
- (b) the way in which the creditor has exercised or enforced any of his rights under the agreement or any related agreement;
- (c) any other thing done (or not done) by, or on behalf of, the creditor (either before or after the making of the agreement or any related agreement)."

Subsection (2) then states that in deciding to make a determination under s.140A, the court shall have regard to "all matters it thinks relevant". The provisions have been criticised on the grounds that they "do not identify any badges of unfairness or, indeed, supply any meaningful criteria for identifying an unfair credit relationship."²⁹ The other side of this is that the test allows for maximum flexibility. In an attempt to aid clarity, the OFT has issued guidance on the exercise of its powers,

²⁷ Article 3(5).

²⁸ See *FSA Reforming Conduct of Business Regulation* (CP 06/9).

²⁹ House of Lords EU Committee 36th Report of Session 2005-6 *Consumer Credit in the EU* (HL 210-1) para 192.

while consciously not defining what is an unfair relationship.³⁰ It is clear that unfairness may involve both contract terms and business practices, and that account could be taken of, among other things: whether terms are unfair under the UTCCRs; whether costs are excessive; whether FSA rules, TCF outcomes or codes of practice have been breached; and whether adverse findings have been made by the Financial Ombudsman.³¹ The test was introduced by the Consumer Credit Act 2006 and it remains to be seen how it will be applied by the courts. However, it is worth noting that the European Consumer Credit Directive puts obligations on lenders to assess the consumer's creditworthiness and lend responsibly.³² There is thus a clear obligation to take account of the interests of those consumers who might be vulnerable because of (say) their overindebtedness.³³

2.4 Vulnerable Consumers and Unfair Terms

The Unfair Terms in Consumer Contracts Regulations 1999 (the Regulations)³⁴ allow for the challenging of unfair terms, which have not been individually negotiated, in contracts between suppliers (here "firms") and consumers.³⁵ The Regulations provide that "core provisions" cannot be challenged, so long as they are expressed in clear language. Provisions are core if they relate to the definition of the main subject matter of the contract, or to the adequacy of the price or remuneration. Schedule 2 of the Regulations provides a "grey list" of terms which may be regarded as unfair, although this list is not exhaustive.

The test of unfairness is whether the term contrary to the requirement of good faith "causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer." In *Director General of Fair Trading v First National Bank plc*, Lord Bingham argued that openness required "that the terms should be expressed fully, clearly and legibly, containing no concealed pitfalls or traps" and that the requirement of significant imbalance is met if a term "is so weighted in favour of the supplier as to tilt the parties' rights and obligations under the contract significantly in his favour".³⁶ The Regulations may potentially be unfair if they adversely affect a specific group of consumers. It is therefore important for firms to consider whether there may be certain consumers who are vulnerable to the effect of a particular type of term.

³⁰ OFT *Unfair Relationships* (OFT Guidance, May 2008).

³¹ *Ibid* chap 4.

³² 2008/48/EC Art 8.1.

³³ See F Philpott *et al The Law of Consumer Credit and Hire* (OUP, 2009) chap 13.

³⁴ SI 1999 no.2083, implementing Directive 93/13/EEC.

³⁵ Regulation 5(1).

³⁶ [2001] 3 WLR 1297 at 1308.

2.5 Vulnerable Consumers and the Financial Ombudsman Service

Ombudsman schemes were originally conceived as voluntary schemes for the resolution of consumer disputes outside the courts. Schemes were set up in a number of different areas, including banking, insurance and pensions. FSMA led to the creation of a statutory scheme – the Financial Ombudsman Service – which now covers a wide range of firms and products.

The FOS has now replaced the courts as the primary forum for the resolution of disputes between consumers and firms. It is particularly well-suited to resolution of disputes between firms and vulnerable consumers for a number of reasons. First, it is free for the consumers to use. Second, it adopts an inquisitorial rather than adversarial approach to fact finding. The use of lawyers is positively discouraged. Third, and perhaps most crucially, the FOS has significant discretion in decision-making. James and Morris argue that:

“[o]ne of the key advantages of the Ombudsman technique as a consumer redress mechanism is the capacity to transcend strict legal rules and draw upon a range of extra-legal standards in a manner which usually operates to the benefit of the consumer”.

The FSA Handbook states that: “[t]he Ombudsman will determine a complaint by reference to what is, in his opinion, fair and reasonable in all the circumstances of the case”. It continues by saying that in considering what is fair and reasonable in all the circumstances of the case, the Ombudsman will: “take into account the relevant law, regulations, regulators’ rules and guidance and standards, relevant codes of practice and, where appropriate, what he considers to have been good industry practice at the relevant time”.³⁷ The former Chief Ombudsman has argued that the test “can encompass considerations of wider public policy or the general public good.”³⁸ This approach has a considerable number of supporters. However, it also has its critics. Lord Ackner said that the breadth of the test made the industry “the hostage to fortune of uncertain and therefore unpredictable liability...”³⁹ More recently Lord Hunt called for more transparency of and consistency in decision-making. The FOS has responded to this with a policy statement on its strategic approach to transparency.⁴⁰

³⁷ DISP 3.6.4.

³⁸ W Merricks “Lessons from Merging the Financial Ombudsman Schemes” Address to the British and Irish Ombudsman Association 25 May 2001.

³⁹ Lord Ackner *Report on a Unified Complaints Procedure* (PIA, 1993) para 93.

⁴⁰ Available at <http://www.financial-ombudsman.org.uk/publications/policy-statements/transparency.html> (accessed 21-4-10). See also PE Morris “The Financial Ombudsman Service and the Hunt Review: Continuing Evolution in Dispute Resolution” [2008] 8 JBL 785.

2.6 Treating (Vulnerable) Consumers Fairly and the FSA

The FSA requires firms to treat their customers fairly. What amounts to “fairness” is a moot point. The FSA’s “Principles for Businesses”, for example, are designed to encapsulate what the Authority expects. Principle six states that “[a] firm must pay due regard to the interests of its customers and treat them fairly”) and principle seven states that “a firm must pay due regard to the information needs of its customers and communicate information to them in a way which is clear, fair and not misleading.” This obligation relates to how a firm deals with all its customers. However, it is clear that a firm’s conduct may be unfair if it impacts adversely on particular groups of vulnerable consumers. This has to be viewed alongside the CPRs.

2.7 Vulnerable Consumers and Private Law

A number of legal doctrines have emerged over the centuries which provide a degree of protection for individuals, including financial services consumers.⁴¹ They are introduced briefly here.

2.7.1 Duress

Where a firm induces a contract by unlawful or other illegitimate pressure or intimidation, the contract will be voidable on the basis of duress. In extreme cases the duress may be physical (for example, a threat to a person). These are the easiest to classify and resolve. In other cases duress may be economic. This is more difficult to identify, as legitimate transactions may involve a degree of pressure. It has been stated that duress involves “a coercion of the will so as to vitiate consent” and that “commercial pressure is not enough.”⁴² This means that duress “must be distinguished from commercial pressure, which on any view is not alone enough to vitiate consent.”⁴³

The close relationship between duress (which provides consumers with rights under private law) and unfair commercial practices (which allow enforcement authorities and regulators to take enforcement action against a firm) has been noted. Indeed, attempts are being made to see how the regimes might be co-ordinated.⁴⁴

2.7.2 Undue Influence

The doctrine of undue influence will be relevant where there is a close relationship of trust and confidence between two parties that is capable of being abused. Although it was traditional for

⁴¹ See P Cartwright *Banks Consumers and Regulation* (Hart 2004) chap 6.

⁴² *Pao On v Lau Yiu Long* [1980] AC 614 per Lord Scarman at 635.

⁴³ *Atlas Express Ltd v Kafco (Importers and Distributors Ltd)* [1989] QB 833 per Tucker J at 839.

⁴⁴ See HM Government *A Better Deal for Consumers* (Cm 7669) July 2009 para 4.3

undue influence to be divided into separate categories, the House of Lords has held that it represents a single doctrine that can be reached by separate paths.⁴⁵

Taking the first path, a claimant can argue that there has been actual undue influence. This occurs where “one party exercised such domination over the mind and will of the other that the latter’s independence of decision was substantially undermined, and this domination brought about the transaction”.⁴⁶ It bears much similarity to, and appears to overlap with, the doctrine of duress, considered above. It may be particularly relevant where vulnerable consumers are concerned. Secondly, the law has recognised what has become known as presumed undue influence. According to Lord Nicholls in *Royal Bank of Scotland v Etridge (no.2)*, where seeking to rely on this, the person needs to establish two factors. First he must show that he placed trust and confidence in the other party in relation to the management of his affairs, and secondly, that there followed a transaction which “calls for an explanation”.⁴⁷ In the absence of satisfactory evidence from the defendant to the contrary, this will be sufficient to discharge the burden of proof.

The cases on undue influence have frequently concerned financial transactions, and raise significant questions about the relationship between private law and unfair commercial practices legislation. Undue influence is an example of aggressive commercial practices, but it is unclear to what extent the public and private law regimes align. This is another area upon which more research is needed.

3. Part Three: Rethinking Vulnerability

3.1 Introduction

The discussion above reveals the following:

1. We can conceive of vulnerable consumers in different ways, and may even disagree about whether “vulnerable” is the right label for the consumers in question. Nevertheless “vulnerable consumer” is a helpful shorthand term to describe those consumers who are particularly susceptible to loss or harm.
2. A range of legal provisions make reference to vulnerable consumers, and a range of tools, or techniques is available to take account of the interests of such consumers. Most of these focus on fairness.

⁴⁵ *Royal Bank of Scotland v Etridge (no.2)* [2002] 2 AC 773

⁴⁶ J Beatson, *Anson’s Law of Contract* (28th ed) (OUP, 2002) at p 286.

⁴⁷ Above n 43 at p 796.

Part three forms the heart of the paper. It establishes what I refer to as a taxonomy of vulnerability. This is a novel framework consisting of a set of elements which, taken together, help to identify where vulnerability is liable to exist. The elements are classified by the paper as:

- Information vulnerability;
- Pressure vulnerability;
- Supply vulnerability;
- Redress vulnerability; and
- Impact vulnerability.

If the discussion ended there then the paper might be of academic interest, but would be of limited practical utility. That is why the paper goes on to identify how key stakeholders (legislators, regulators, firms and others) might use the taxonomy in practice to ensure that the interests of vulnerable consumers are appropriately addressed. For example, if the cause of consumer vulnerability is a particular susceptibility to pressure, what tools are available to counteract that? Banning particular forms of supply? Providing additional remedies (such as cooling off periods) to consumers? Such decisions require political judgement, and it is not suggested that the answers will be easy. Nevertheless, it is argued that the taxonomy provides a useful tool through which the questions can be addressed. Although the focus of this paper is on financial services, the arguments are largely also relevant to other sectors.

3.2 The Rationales for Regulation and the Taxonomy of Vulnerability

Before setting out the taxonomy, it is helpful to consider how it relates to our understanding of how markets operate (or are thought to operate in classical economics). There can be little doubt that the idea of the perfect market has been powerful one in discourse on consumer protection, financial regulation and policy. In the perfect market the rational, perfectly informed consumer makes consistent decisions in accordance with his or her preferences. Much consumer law scholarship focuses on the information asymmetry that exists between firms and consumers, sees this as a classic example of market failure, and views law as an appropriate tool to correct this.⁴⁸ This has

⁴⁸ There is a large quantity of literature here. See, for example, H Beales, R Craswell and S Salop 'The efficient regulation of consumer information' (1981) 24 *Journal of Law and Economics* 491; WC Whitford 'The Functions of Disclosure Regulation in Consumer Transactions' (1973) *Wisconsin Law Review* 400; G Hadfield, R Howse and M Trebilcock 'Information-Based Principles for Rethinking Consumer Protection Policy' (1998) 21 *Journal of Consumer Policy* 131. OFT, *Consumer Detriment Under Conditions of Imperfect Information* (OFT Research Paper 11 – prepared by London Economics, August 1997).

influenced some thinking on vulnerability and financial regulation. For example, and as noted above, Burden argued that consumers may be vulnerable for two main reasons, the first of which is that they may find it more difficult to obtain or to deal with information needed to make appropriate purchasing decisions. While we might argue that many consumers suffer from information asymmetry in relation to many products, we might also conclude that (a) this asymmetry is particularly great where financial services are concerned and (b) those consumers for whom the asymmetry is greatest are particularly vulnerable, and therefore particularly deserve our attention.⁴⁹ If we interpret the concept of information deficits broadly, as it is suggested that we should, it is apparent that such deficits permeate, at least to some extent, all the aspects of vulnerability examined here. CAV argued that vulnerability and disadvantage are the result of the interaction of characteristics that “create information problems” and make it clear that their study “emphasises information issues.”⁵⁰ I refer to this form of vulnerability as informational vulnerability.

Burden’s second element of vulnerability is that some consumers suffer greater loss than other consumers by making inappropriate purchasing decisions.⁵¹ This is also pertinent to our discussion. Where loss or harm disproportionately impacts upon certain consumers it seems appropriate to describe them as vulnerable. I describe this as impact vulnerability. This is perhaps the most challenging aspect of vulnerability for the law to deal with, particularly as it raises issues of (re) distributive justice, and not just market failure. For this reason, it is dealt with at the end of the taxonomy.

It is submitted that we may identify further characteristics of vulnerability of relevance to this discussion. For example, consumers may be vulnerable as a result of their greater susceptibility to pressure. In the perfect market, choices are made voluntarily, whereas in practice they may be subject to significant pressure. I describe this as pressure vulnerability. Next, consumers may be vulnerable as a result of lack of choice. In the perfect market there are numerous buyers and sellers, but in practice a smaller number of firms may be dominant. This is described here as supply vulnerability. In addition, consumers may be vulnerable because of the greater difficulty they face in achieving redress. The perfect market is underpinned by the private law, which allows consumers

⁴⁹ Although not all commentators see financial services as a special case. See e.g. G Benston *Regulating Financial Markets* (London, IEA, 1998).

⁵⁰ Above n 4.

⁵¹ R Burden *Vulnerable Consumer Groups: Quantification and Analysis* (OFT Research Paper 15, April 1998). CVA takes a similar approach, arguing that vulnerability is influenced by (a) the ability to protect or defend against the chance of injury or loss (which while broader than Burden’s first factor may result from problems in accessing or dealing with information) and (b) ability to cope with the negative consequences of injury or loss when it occurs, which is close to Burden’s second factor of liability to suffer greater loss. Above n 6 para 3.1.

(and others) to hold the market to account for breaches. However, the availability of such remedies may be more apparent than real. Some consumers will find it particularly difficult to obtain satisfaction, and I refer to this phenomenon as redress vulnerability.

It must be emphasised that while this categorisation is described as a taxonomy of vulnerability, it is not claimed to be perfect. It is possible to conceive of and explain vulnerability in different ways and, no doubt, to identify alternative or additional forms of vulnerability. However, it is submitted that the categories proposed capture appropriately the principal forms of vulnerability relevant to this work. The chief purposes of setting out these factors are twofold. First, it provides a framework for examining how vulnerability may manifest itself. Second, it aids the identification of effective responses for tackling this vulnerability, particularly through consumer law. The factors are now considered in more detail.

3.3 Informational Vulnerability

It was suggested above that some consumers may be particularly vulnerable as a result of the greater difficulties they face in obtaining and processing the information necessary to make informed purchasing decisions (hereafter, informational vulnerability).⁵² Much consumer law scholarship has focused on the role of the law in correcting market failure.⁵³

In practice, we know that many consumers will lack the information necessary to make fully informed decisions. The information asymmetry suffered by the most vulnerable is a particular cause for concern. It is clear that some consumers may find it more difficult to access information than others. For example, if they are restricted physically, such as by being housebound, they may find it difficult to access the information necessary to make an informed choice.⁵⁴ Furthermore, some consumers will lack the ability to use information seeking tools, such as the internet. It should also be noted that such consumers are likely to be subject to what has been termed “marketing exclusion”. Because they are not seen as profitable, they may find that they are not targeted by suppliers with information that they might have found useful.⁵⁵

⁵² For an examination of the role of information in consumer decision-making see London Economics *Consumer Detriment under Conditions of Imperfect Information* (OFT Research Paper 11, August 1997). The difficulties may relate not only to consumers’ ability and capacity, but also in inclination. See DP p 9.

⁵³ Hadfield, Howse and Trebilcock argue that rectifying information asymmetry was the “key analytical basis of for early consumer protection law”. See G Hadfield R Howse and MJ Trebilcock “Information-Based Principles for Rethinking Consumer Protection Policy” (1998) JCP 131 at 134.

⁵⁴ This is related to supply vulnerability, considered below.

⁵⁵ E Kempson and C Whyley *Kept Out or Opted Out? Understanding and Combating Financial Exclusion* (Policy Press, 1999).

As important as access is the ability of the consumer to process and act upon information when it is supplied. Consumers will differ greatly in the extent to which they can understand and use information. Simon famously recognised that many consumers suffer from “bounded rationality”. This means that their ability to receive, store and process information is limited.⁵⁶ Bounded rationality potentially affects all consumers but is of particular concern for those whose personal characteristics may make processing information especially difficult.

While information asymmetry exists in many markets, there is evidence to suggest that it might be particularly pronounced where financial services are concerned. This argument has been made in a number of sectors of the financial services industry. Davies has argued that two forms of information asymmetry are particularly apparent in financial services: complexity of contracts and difficulties in judging the soundness of firms.⁵⁷ The issue of complexity is itself complex but it can be brought down to the simple truth that many financial products are hard for consumers to understand. The Sandler Report argued that “[r]etail savings products are inherently more complex than almost all other consumer goods.”⁵⁸ While there is room for disagreement here (and commentators such as Benston have argued forcefully that financial products are typically not more complicated, or more difficult for consumers to understand than other products such as white goods) most commentators see this information asymmetry as a key rationale for regulation.⁵⁹ Davies’s second element of information asymmetry in financial markets focuses on the difficulties consumers face in judging the soundness of firms. This is a matter which may be very important to them (particularly in the absence of 100% insurance) but impossible to judge. With both forms of information asymmetry some consumers will be at a particular informational disadvantage. These are vulnerable consumers.

Related to this is the concern that some consumers may be vulnerable because they are at a particular risk of being misled. A consumer who is less knowledgeable, less linguistically proficient, or more credulous than most, is at particular risk from potentially misleading information. As noted above, this is recognised by the CPRs, which allow information to be judged by the standard of the average member of a group characterised by “mental or physical infirmity, age or credulity” in certain cases. There is no doubt that such characteristics are liable to make consumers vulnerable.

⁵⁶ H Simon *Models of Bounded Rationality* (Cambridge, MIT Press, 1982).

⁵⁷ H Davies “Why Regulate?” Henry Thornton Lecture (City University Business School, 4 November 1998).

⁵⁸ Sandler Report above n ?? para 15.

⁵⁹ See G Benston *Regulating Financial Markets* (London, IEA, 1998).

3.4 Addressing Informational Vulnerability

3.4.1 Mandatory Disclosure

If the concern is that consumers are not receiving the information they need to make informed choices, then the most direct response is to use informational tools such as mandatory disclosure. As well as providing consumers with the information they would otherwise lack, disclosure may assist the functioning of the market. According to Breyer, disclosure regulation works by “augmenting the preconditions of a competitive marketplace rather than substituting regulation for competition.”⁶⁰ As well as its (relative) cheapness, and its role in helping competitive markets to function more effectively, disclosure can also be seen as attractive because it respects, rather than restricts, consumer choice. Disclosure also encourages consumers to take responsibility for their decisions. This can be important in guarding against moral hazard – the risk that if they are not put under incentives to take responsibility for their actions, consumers will not do so.

3.4.2 Weaknesses of Mandatory Disclosure

Despite these strengths, mandatory disclosure has its weaknesses. The first difficulty for policy makers is to decide what information should have to be disclosed. Research by London Economics for the Office of Fair Trading has suggested that there are three types of information that consumers need to make informed choices: information on price; on quality, and on the terms of trade.⁶¹ Some of this information (for example about price) can be communicated relatively easily for most products.⁶² Other information (for example, about quality) is more difficult to communicate. Even where it is possible to communicate the information, it may not be possible to do it in a way that consumers find helpful. This has certain dangers. For example, it might lead to “focal point competition”, where suppliers focus on one aspect of a product at the expense of others. In addition, there is a danger of bad products driving good products out of the market, with suppliers under less incentive to provide high quality high price goods than low quality low price goods, because of the difficulties consumers face in judging quality. Furthermore, a key element of quality will be value for money, but this is notoriously difficult (and sometimes impossible) to communicate, particularly where the return from a product will not be known until the future (i.e. where the product can be classed as credence goods).

A second problem is the risk of information overload. Because consumers differ in the information they would find useful, and to avoid there being disclosure gaps, there is a danger that too much

⁶⁰ S Beyer, *Regulation and its Reform* (Cambridge, Harvard University Press, 1982) at 151.

⁶¹ Above n 49 at p 5.

⁶² Although there are exceptions, such as the price of credit.

information will be supplied. The effect of this may be either to confuse consumers, or to lead to consumers ignoring all the information. Sunstein suggests that “the recent enthusiasm for disclosure requirements is at least in some settings a mistake, for the simple reason that such requirements may defeat their own purpose.”⁶³

A third problem is that informational responses such as disclosure require consumers to respond to them. This may be more difficult for some consumers than others. It has been suggested that “the major problem with disclosure regulation is not in securing business compliance, but rather that consumers are unaware of the information disclosed, do not appreciate its significance, or simply do not employ the information provided in the marketplace”.⁶⁴ Wilhelmsson argues that the emphasis policy makers have placed on consumer information acts to reproduce injustice, because vulnerable consumers derive the least benefit from the protection offered. In short, they are least likely to make use of the information.⁶⁵

A final point is that mandatory disclosure is to a large extent based on assumptions founded upon classical economics about how consumers operate in the market. In particular consumers are assumed to be rational. However, many recent studies in behavioural economics have challenged these assumptions.⁶⁶ It is not possible to do full justice to the findings of behavioural economics here. Suffice it to say that consumers typically display certain characteristics at odds with their image as rational maximisers of their own utility. For example: their preferences vary over time (usually with a preference for the short term); they tend to be over-optimistic; they respond very differently depending upon how questions are presented, and they tend to use heuristics (rules of thumb) to assess factors such as risk.⁶⁷ It seems reasonable to assume that while these biases tendencies may affect a large proportion of consumers, there are likely to be some for whom they are particularly problematic. For example, those with less experience, or poor literacy or numeracy skills, may be particularly susceptible.

⁶³ C Sunstein *Free Markets and Social Justice* (OUP, 1997) p 284.

⁶⁴ C Scott and J Black *Cranston's Consumers and the Law* (Butterworths, 2000) p 372.

⁶⁵ T Wilhelmsson *Twelve Essays on Consumer Law and Policy* (University of Helsinki, 1996)

⁶⁶ The literature is voluminous. See for example C Jolls, CR Sunstein and R Thaler “A Behavioural Approach to Law and Economics” (1998) *Stanford Law Review* 1470; J Hansen and D Kysar “Taking Behaviouralism seriously: The Problem of Market Manipulation” (1999) 74 *New York University Law Review* 630. The literature is skilfully summarised and discussed in G Howells “The Potential and Limits of Consumer Empowerment by Information” (2005) 32(3) *Journal of Law and Society* 349.

⁶⁷ For an excellent summary of these issues see I Ramsay *Consumer Law and Policy* (2nd ed) (Hart, 2007) at 71-84.

Where consumers have the capability and inclination to act upon information, disclosure provides the benefits outlined above. Where they may not there is greater concern, although some commentators still see benefits. Cayne and Trebilcock champion disclosure laws for some vulnerable consumers, arguing that they “can be an effective means of protecting the poor...because they enhance the operation of free market forces”. However, they recognise its limitations. In particular, they argue that “they can only be of value if the consumer is intellectually and psychologically equipped to apply the information which disclosure regulation entitles him to have”.⁶⁸ Recent research in behavioural economics suggests that few consumers are intellectually and psychologically equipped to make well-informed choices.

3.4.3 Addressing the Weaknesses

Despite the concerns raised above, informational tools such as disclosure may still play an important role in a consumer protection regime designed to help vulnerable consumers.

First, there should be a greater focus on providing the information that is of particular importance to vulnerable consumers. In some cases, this will be information that might be obvious to many other consumers. This might, for example, include warnings about matters that would be obvious to many consumers, but not to the most vulnerable. Where there is a product that is particularly likely to be used by vulnerable consumers, then there is an argument that the key warnings should be (a) phrased very simply and directly; and (b) especially prominent. In some cases, the message might be effectively conveyed by images. In *Warning! Regulated Information: a Guide for Policy Makers*, it is suggested that information is most likely to achieve its goals in changing behaviour where: it is clear who the information is aimed at; language is accessible to the lowest ability group likely to access it; volume is minimised to maximise impact; the sources of competition for attention are identified and overcome; and visual tools are used to guide choices.⁶⁹ The second of these points perhaps demands particular attention. It is suggested that it is sensible for regulated information to be driven by the lowest common denominator in terms of reading age. Furthermore, it has also been argued that this will sometimes benefit those other than the defined vulnerable group. In their final report, the Better Regulation Executive and National Consumer Council suggested that “in designing information for the most vulnerable consumers all society will benefit from simple, concise messages.”⁷⁰ This also relates to the final point about the use of visual tools – in particular what

⁶⁸ D Cayne and MJ Trebilcock “Market Considerations in the Formulation of Consumer Protection Policy” (1973) 23 *University of Toronto Law Journal* 396 at p 406.

⁶⁹ *Warning! Regulated Information: a Guide for Policy Makers* (BRE/BERR/NCC (undated)) p 14.

⁷⁰ *Warning: Too Much information can harm* (Final Report) p 13.

might be called “image-based messaging”.⁷¹ There is evidence that this can sometimes be a particularly effectively way of communicating complex information, but that some such regimes have failed.⁷² The previous Government recognised the need for further research here and proposed examining various methods of labelling of financial products in more detail.⁷³

Second, there should be greater emphasis on improving the ability of consumers to recognise, and act upon, the importance of using this information. This requires a variety of responses, including advertising campaigns and efforts to improve consumer education.⁷⁴ The Financial Services and Markets Act (FSMA) is an interesting model here. Under FSMA, the FSA is charged with securing the “appropriate” degree of protection for consumers. In achieving this, the FSA is to have regard to a number of matters, including “the differing degrees of risk involved in different kinds of investment or other transaction...the differing degrees of experience and expertise that different consumers may have in relation to different kinds of regulated activity” and “the needs that consumers have for advice and accurate information”. These elements recognise that successful consumer protection requires consumers to understand products, something that is particularly important where products are complex. However, FSMA also contained a “public awareness” objective, requiring the FSA to promote public understanding of the financial system. This included, in particular, promoting awareness of the benefits and risks associated with different kinds of investment or other financial dealing; and the provision of appropriate information and advice.⁷⁵ The FSA has argued that risks to this objective may come from inadequate general financial literacy on the part of the public, and inadequate understanding by consumers of specific products and services. Significant efforts to improve financial literacy have been undertaken and further developments are taking place. In particular, the Financial Services Act 2010 required the FSA to establish a new consumer financial education body which has the function of enhancing: the understanding and knowledge of members of the public of financial matters, and the ability of members of the public to manage their own financial affairs.⁷⁶

⁷¹ *Ibid.*

⁷² Contrast, for example, information on child trust funds with that on recycling. Vanilla Research *Consumer Information and Regulation* (Vanilla Research, July 2007).

⁷³ HM Treasury *Regulating Financial Markets: Summary of Responses* (Nov 2009) para 2.143.

⁷⁴ Research has found that consumers frequently see ulterior purposes for disclosed information. Recycling logos were seen as marketing; product safety guidelines as protection for the firm against litigation and information that calls to call centres might be recorded as a warning against verbal abuse. See Vanilla Research *ibid* p.4.

⁷⁵ Section 4(2).

⁷⁶ Section 6A(1). For details see www.cfebuk.org.uk.

Improving consumer education should help to tackle different aspects of vulnerability. First, it should help to tackle informational vulnerability by assisting consumers in understanding information supplied to them, and the significance of that information. This will, of course make poor decisions less likely, helping to minimise impact vulnerability. In addition, consumer education is likely to make consumers more assertive, helping them to minimise the effect of pressure vulnerability and to be more confident in pursuing redress, thus tackling redress vulnerability. Of course, using education to improve consumer awareness and competence is a long-term strategy, but it is a valuable one.

It is important to recognise that regulated information will not always be the best tool to use. In some cases it may be better to recognise its limitations and choose an alternative regulatory approach. Efforts to regulate and, in particular, to simplify products should be noted here. While the success of such initiative has been limited, the previous Government appeared in its Paper *Reforming Financial Markets* to retain some enthusiasm for product regulation.⁷⁷ Following the responses to the consultation the Government stated that it preferred to focus on labelling (as discussed above) rather than additional product regulation.⁷⁸

An important point to emphasise where financial products are concerned is that sales will frequently be based on advice. The availability of advice is an obvious way to address information asymmetry about products – the consumer relies on the expert rather than trying to assess the product. But this model presents difficulties. These are well-trodden and justice cannot fully be done to them here. The relationship between information and advice is a complicated one.⁷⁹ The Retail Distribution Review has caused a significant re-assessment of the nature of advice and, in particular, the way such advice is regulated.⁸⁰ But given the focus of this paper on the vulnerable consumer, it is important to recognise that few vulnerable consumers will be dealing with financial advisors. Furthermore, while the impact of the RDR is not yet fully known, an obvious danger is that it will lead to a reduction in access to advice. Against this background the Thoresen Review deserves particular note.⁸¹ The Review was established to examine the feasibility of delivering a national approach to generic financial advice, with the aim of ensuring greater access to high quality affordable financial advice for those most vulnerable to the consequences of poor financial decision-making. It recommended the establishment of a national money guidance service which would be

⁷⁷ HM Treasury *Regulating Financial Markets* (July 2009) para 8.25.

⁷⁸ Above n 69 para 2.150.

⁷⁹ McMeel and Virgo argue that “information and advice exist on a spectrum and the two concepts merge imperceptibly into one another” G Mc Meel and J Virgo *Financial Advice and Financial Products* (OUP, 2001) para 1.59.

⁸⁰ See FSA *Distribution of retail investment: Delivering the Retail Distribution Review* (CP09/18 (June 2009)).

⁸¹ Above n 11.

governed by the principles of: impartiality; supportiveness; crisis prevention; universality and being sales-free. Rather than recommend specific products, the service would focus on giving people information and guidance on matter such as budgeting, saving and borrowing, protection, retirement planning, tax and welfare. It would also have a “jargon-busting” function. While it was proposed that the service would be nationally directed, most of the delivery would be through partner organisations. The initiative was launched by the then Chancellor of the Exchequer in March 2010 as part of the Moneymadeclear service. The service includes a helpline, website and face-to-face advice services, and is delivered through a range of partners such as Citizens Advice Bureaux and Age Concern. The cost of the service is to be funded by a levy on the financial sector and from funds recovered from dormant bank accounts. The service is currently lead by the FSA. However, as noted above, the Financial Services Act 2010 requires the FSA to set up a new consumer financial education body, which will take forward the implementation of the Moneymadeclear service.

There is some evidence of how the initiative will operate because a pathfinder service million has been underway in the North West and North East since April 2009. By March 2010 around 20,000 had called the helpline and around 23,000 used the face-to-face service. The Treasury has stated that approximately half the users of the service were vulnerable to the consequences of poor financial decision making.⁸²

The discussion above reveals the difficult decisions that have to made about what information should be provided to consumers, how that information should be provided, and how we ensure that the needs of the most vulnerable are addressed appropriately. It is hard to disagree with the conclusion of Howells that “a more sophisticated and nuanced approach to information rules should be developed which enhances the effectiveness of the rules, whilst recognising their limitations.”⁸³ Perhaps above all, there is a need to recognise that informational responses will not always be appropriate, in particular by themselves.

3.4.4 Controlling False and Misleading Information

It is important not only to ensure that consumers receive helpful information, but also to ensure that they do not receive false or misleading information. It is widely accepted that false information should not be tolerated, particularly where it is known to be false. More difficult is how potentially misleading information is controlled.

⁸² HM Treasury “Chancellor launches new free money advice service” (Press Release 11-3-10).

⁸³ G Howells “The Potential and Limits of Consumer Empowerment by Information” (2005) 32(3) *Journal of Law and Society* 349 at 362.

A difficulty with misleading information is to decide upon the standard by which it is judged. For example, it is possible for information to be both true and misleading at the same time. There are several options which can broadly be stated as follows. First, information might only be deemed misleading if it would be liable to mislead a well-informed consumer. Second, it might only be misleading if it would be liable to mislead an average consumer. Third, it might be misleading if it would be liable to mislead only a credulous consumer. The first two options have attraction from the point of view of firms because they expect a reasonable standard of consumers. It might encourage consumers “to go shopping with their eyes open and their wits reasonably alert”.⁸⁴ There was some evidence that the Unfair Commercial Practices Directive would adopt a similar standard. Indeed, recital 18 states that the Directive takes as a benchmark “the average consumer, who is reasonably well informed and reasonably observant and circumspect, taking into account social, cultural and linguistic factors.” Nevertheless, the Directive (and the CPRs in implementing it) allows for departure from such an objective standard. More specifically, the CPRs allow misleading information to be judged by the standard of the average member of a clearly identifiable group of consumers:

“who are particularly vulnerable to the commercial practice or to the underlying product because of their mental or physical infirmity, age or credulity in a way which the trader could reasonably be expected to foresee; and...who are not particularly vulnerable to the commercial practice by reason only of that commercial practice being the common and legitimate advertising practice of making exaggerated statements which are not meant to be taken literally.”

A number of points should be noted here. First, the advertising practice of making exaggerated statements that are not to be taken literally is deemed legitimate. A particularly credulous consumer who is misled by such a statement will not receive the benefit of the vulnerable consumer test unless that consumer is vulnerable for other reasons too. Second, the reference to age is relevant both for younger and older consumers. Where traders should have realised that younger or older consumers are particularly vulnerable (perhaps because they are less likely to have experience of certain products) then the practice is judged accordingly. The third point is that the test makes reference to consumers made vulnerable by mental (as well as physical) infirmity and credulity. Credulity, in particular, is relevant where misleading information is concerned. The test envisages that there will be cases where a trader should realise that there is an identifiable class of consumers

⁸⁴ Cmnd 1781 para 813. The Trade Descriptions Act 1968 was largely based upon the Report’s recommendations.

who are particularly credulous and, as a result, particularly vulnerable. Where this is so, the practice is judged by the standard of an average member of such a group. While the aim behind this is admirable, there are legitimate concerns. First, who are these consumers? One possibility would be children, but they are catered for by the reference to age. Credulity must stand separately. Another might be consumers with a mental health condition, but the reference to mental infirmity would, it is presumed, better cover them. It seems that the provision may be of most use where the consumer belongs to a class who have a particular religious or spiritual belief which can lead to members of the class being easily led. A belief in astrology or spiritualism might be an example. However, this will be difficult to apply in practice, in anything other than the most blatant cases of trickery. Furthermore, where a trader preys upon a particularly susceptible consumer, a better description of the conduct might be undue influence, which is provided for elsewhere in the CPRs.

The approach which allows the standard to be varied might be justified on several different grounds. First, by encouraging traders to consider how potentially ambiguous statements might be understood, we improve the clarity and quality, of information. This has clear economic benefits. Second, the test reflects the reality that not all consumers can meet the standards a purely objective test would require of them. A test that allows flexibility is rooted in concepts of distributive justice. To the extent that greater scrutiny of advertising imposes additional costs they are borne by all consumers, benefiting only the naïve, credulous, or poorly educated. However, this might be justified on grounds of social justice. Third, it could be argued that the rationale for a credulous consumer test might not only be protection for the weak, but also the reinforcement of trust.⁸⁵ The private law increasingly recognises concepts such as good faith, and the financial services sector imposes very broad requirements to treat customers fairly.

There is no doubt that the balancing act is a difficult one. Sunstein suggests that “almost all substantive advertisements will deceive at least some people in the light of the exceptional heterogeneity of listeners and viewers”.⁸⁶ Firms are likely to balk at a test which requires them to consider how the average consumer with a mental infirmity might have understood a marketing campaign. Furthermore, such a provision would not operate in isolation from other responses. Consumer education should again be beneficial here. The better educated consumers are, the better equipped they will be to appreciate potentially misleading information (and to identify false

⁸⁵ Ramsay *Advertising Culture and the Law* (Sweet and Maxwell, 1996) p 85.

⁸⁶ C Sustain *Free Markets and Social Justice* (New York, Oxford University Press, 1997) p 284.

information). The ability to depart from a purely objective test is one valuable way in which consumer protection law can protect the most vulnerable consumers.

3.4.5 *The Relationship between Positive and Negative Informational Responses*

It should be noted that the CPRs deal with two types of misleading commercial practices. First are misleading actions. A commercial practice is a misleading action if it contains false information and is therefore untruthful in relation to particular matters. It is also a misleading action if its overall presentation deceives or is likely to deceive the average consumers in relation to certain matters even if it is factually correct. There is also a second type of misleading commercial practice: misleading omissions. Regulation 6(1) states that a commercial practice is a misleading omission if, in its factual context, taking account of a series of matters it *inter alia* “omits” or “hides” material information. In most cases, material information is “the information which the average consumer needs, according to the context, to take an informed transactional decision.” The provisions on misleading omissions blur the distinction between positive informational responses (where information is required to be provided, such as through disclosure) and negative informational responses (where providing misleading information is prohibited). Rather than specify in detail the information which must be disclosed (as mandatory disclosure regimes do) the obligation is not to omit information which average consumers need to make informed decisions. This is a significant step forward for consumer protection. Collins identifies this as a “major innovation” for UK law, and points out that it also goes beyond the previous requirements of most Member States.⁸⁷ Questions remain about how the provision will be interpreted. For example, the courts will have to consider the “factual context” of the transaction as well as “the limitations of the medium” used to communicate the practice. There is also the question of when the consumer “needs” rather than simply “would benefit from” particular information.⁸⁸ Nevertheless, the provision reveals an increasing willingness to require firms to inform consumers about matters that are likely to be of interest to them, even where they are not under specific disclosure obligations. The test of the vulnerable consumer again becomes relevant here. It was noted above that where a consumer is particularly vulnerable to either the practice or the underlying product because of “mental or physical infirmity, age or credulity in a way which the trader could reasonably be expected to foresee” and the practice is “likely to materially distort the economic behaviour only of that group” then average consumer means an average member of that group. Information may be material to

⁸⁷ H Collins “Harmonisation by Example: European Laws against Unfair Commercial Practices” (2010) 73(1) MLR 89 at pp 104-105.

⁸⁸ *Ibid* at p 105.

some consumers that would not be to others and this places an obligation on traders to ensure that vulnerable consumers are given the information that they need to make an informed choice in the circumstances identified.

3.5 Pressure Vulnerability

In the perfect market, the consumer's actions are fully voluntary. In practice, consumers frequently make decisions when subjected to pressure. This section looks at vulnerability through consumers' susceptibility to pressure.⁸⁹ There may be overlap with other aspects of vulnerability; for example, consumers may be more easily pressurised into making a decision if they lack relevant information. But there will also be cases where information asymmetry is not the essence of the vulnerability, but power asymmetry is. An often-quoted rationale for intervention in the market place in the heyday of consumer protection was inequality of bargaining power, and it has been suggested that all consumer problems result from one or more of a disparity of bargaining power, knowledge and resources.⁹⁰ The three clearly are connected. For example, the inability to bargain effectively may arise from factors such as lack of knowledge and lack of choice. However, it may also result from a feeling of inferiority or susceptibility. The pressure felt by consumers may arise from individual characteristics (such as age, lack of confidence or knowledge) temporary individual circumstances (such as the loss of a loved one or similar life event) or physical situation (such as the presence of the seller in the buyer's home). It may also stem from the behaviour of the seller (for example if he or she acts in an intimidating manner). It is necessary for consumer law to find appropriate mechanisms which allow these to be addressed, taking account of the particular susceptibility some consumers may experience.

One problem is that transactions will frequently be concluded in situations where one party clearly is dominant, but where there is no question of vitiating the bargain in private law or allowing public enforcement action. The existence of power asymmetry is, to some extent, inevitable. The fundamental question, in the words of Kronman, may be "whether the promisee should be permitted to exploit his advantage to the detriment of the other party".⁹¹ Where physical intimidation is present we would doubtless have little hesitation in finding a remedy, such as by

⁸⁹ A study by the DTI in 2003 identified being subjected to high pressure sales techniques as one of the problems faced by vulnerable consumers across the various countries they studied (DTI *Comparative Report on Consumer Policy Regimes* (Oct 2003) p 9).

⁹⁰ J Ziegel "The Future of Canadian Consumerism" (1973) *Canadian Bar Review* 190 at p 193 (Cited in I Ramsay *Consumer Law and Policy* (Hart, 2007) p 53.

⁹¹ A Kronman "Contract Law and Distributive Justice" (1980) *Yale LJ* 472 at 480.

allowing the victim a private law right or allowing an enforcement authority to take action. Greater difficulties arise where psychological pressure is in issue. We might, for example, identify certain consumers as vulnerable because of their susceptibility to having their emotional weaknesses exploited.⁹² Where advertising is essentially aspirational, creating consumer desires and wants, we might find little reason for intervention. However, where advertisements exploit the concerns of parents they might be classed as unfair. This might be relevant in relation to financial matters. For example, it is possible to imagine advertisements putting pressure on parents to provide for their children's future, or to cover their own funeral expenses. It might be too much to identify parents as a vulnerable group, but if we believe some parents might be particularly susceptible to emotional pressure, there might be an argument for consumer law to address this. This is a difficult area, and one where the distinction between exploitative and persuasive advertising is important.

One group of consumers who are undoubtedly vulnerable to pressure are the mentally ill. The Government's White Paper *A Better Deal for Consumers* notes that "people with mental health problems are far more likely to fall into debt and difficulties with debt can lead to a worsening of mental health condition".⁹³ It further suggests that the mentally ill are a "particularly vulnerable group" during the economic downturn. Considerable efforts have been made to address the needs of mentally ill consumers and while the paper does not focus on those consumers who lack capacity, it is important to remember the need to take account of this particularly vulnerable group.

3.6 Addressing Pressure Vulnerability

3.6.1 Banning High-Pressure Modes of Supply

One response to pressure vulnerability is to ban forms of selling where such vulnerability is particularly likely to be found. An obvious candidate for such a ban is doorstep selling. In the 1960s the Molony Committee referred to doorstep selling as "a serious social evil; resulting in homes labouring under an excessive burden of debt and sometimes torn by consequential domestic disharmony."⁹⁴ Although the Committee recommended the introduction of cooling off periods rather than an outright ban on the practice, calls for more radical action have recently been heard. Citizen's Advice made a super-complaint to the Office of Fair Trading about doorstep selling in 2002 (which led to an OFT market study) and The Trading Standards Institute have called for a ban on the doorstep selling in certain sectors, including gas and electricity. Nevertheless, the practice remains

⁹² See I Ramsay above n 86 pp 423-424

⁹³ Above n 42 at p 24.

⁹⁴ Para 742.

lawful.⁹⁵ The CPRs list 31 commercial practices which are considered unfair in all circumstances and so are effectively bans on those practices. Several of these are unfair because of the pressure they involve. Examples of practices banned include creating the impression that the consumer cannot leave the premises until a contract is formed, and conducting personal visits to the consumer's home ignoring the consumer's request to leave or not to return (except in limited circumstances).

3.6.2 Prohibiting Aggressive Commercial Practices Through Broad Standards

Perhaps the main way that consumer protection law takes account of pressure vulnerability is by prohibiting aggressive commercial practices through broad "open texture" standards. Regulation 7(1) of the CPRs states that:

"A commercial practice is aggressive if in its factual context, taking account of all its features and circumstances-

- (a) it significantly impairs or is likely significantly to impair the average consumer's freedom of choice or conduct in relation to the product concerned through the use of harassment, coercion or undue influence; and
- (b) it thereby causes or is likely to cause the typical consumer to take a transactional decision he would not have taken otherwise."

Regulation 7(2) then explains that in determining whether a commercial practice uses harassment, coercion or undue influence account shall be taken of-

- (a) its timing, location, nature or persistence;
- (b) the use of threatening or abusive language or behaviour;
- (c) the exploitation by the trader of any specific misfortune or circumstance of such gravity as to impair the consumer's judgement, of which he is aware, to influence the consumer's decision with regard to the product;
- (d) any onerous or disproportionate non-contractual barrier imposed by the trader where a consumer wishes to exercise rights under the contract, including rights to terminate a contract or to switch to another product or another trader; and

⁹⁵ Indeed, it might be argued that some doorstep selling of financial products is to be applauded because of its role in addressing financial exclusion. Writing in 1994, Rowlinson commented that "legal moneylending, or weekly collected credit, provides a valuable service to a section of the population that most other creditors would not lend to. But there are specific practices that need addressing to reduce the risk of people being exploited by their lack of choice." K Rowlinson *Moneylenders and their Customers* (Policy Studies Institute, 1994) p 165.

(e) any threat to take any action which cannot legally be taken.

Finally, Regulation 7(3) provides that for the purposes of the regulation “coercion” includes the use of physical force, and “undue influence” means “exploiting a position of power in relation to the consumer so as to apply pressure, even without using or threatening to use physical force, in a way which significantly limits the consumer’s ability to make an informed decision.”

The provisions represent the first attempt in UK law to give broad powers to enforcement authorities to tackle excessive pressure applied by traders. According to the Government, the practices are largely those that “intimidate or exploit” consumers, and restrict their ability to “make free or informed choices”.⁹⁶ Therein lies one concern with the provisions. The aggressive practice must impair, or be likely significantly to impair, the average consumer’s freedom of choice or conduct, and must cause or be likely to cause him to take a transactional decision he would not have taken otherwise. Howells argues that the focus on impairment of choice is flawed, and that many aggressive practices concern protection of the consumer’s private sphere “rather than fears that they are forcing consumers into choices or conduct they would not normally make.”⁹⁷ He suggests that “practices that merely irritate or upset are not aggressive/unfair practices” for the purposes of the directive but that the harassment provision was intended to prevent objectionable behaviour that does not necessarily affect the consumer’s decision. While there are good reasons to tackle conduct which is harassing regardless of its economic effect, the Directive is concerned with unfair practices which impact upon individuals in their role as consumers. However, the need for “significant” impairment is questionable. The difficulty, as Howells points out, is “to find a measure against which to judge how significant an impairment of judgment is.”⁹⁸

A second difficulty concerns the definitions of the concepts. “Undue influence” is defined as “exploiting a position of power to apply pressure, even without using or threatening to use physical force, in a way which significantly limits the consumer’s ability to make an informed decision.” So there must be a position of power (which might arise through personal or economic relationship, etc) and the position must also be exploited. Sometimes the consumer will, almost inevitably, be in a temporary position of vulnerability, for example recently bereaved. The test, in particular the reference to “any specific misfortune or circumstance of such gravity as to impair the consumer’s

⁹⁶ Some of the most obviously aggressive practices are among the practices that are specifically banned.

⁹⁷ G. Howells, H-W. Micklitz and T. Wilhelmsson above n 18 p. 175.

⁹⁸ *Ibid* p. 176.

judgement” means that such circumstances will be taken into account when deciding if there has been exploitation.⁹⁹ A consumer’s financial position (for example overindebtedness) might well be a circumstance that would impair the consumer’s judgement in some cases. Harassment and coercion are not defined, but include both physical and other (e.g. psychological) forms of pressure.

The technique of adopting broad standards, and then requiring certain factors to be taken into account in deciding whether those standards are met is attractive from the perspective of consumer protection. It allows the courts to consider a range of matters relating to conduct (such as the use of threatening language, threats to take legal action that cannot be taken, or persistence) situation (such as location and timing) and terms (such as the use of disproportionate non-contractual barriers). This will be particularly relevant where vulnerable consumers are concerned. For example, an elderly consumer faced with a seller in her home at night may be particularly likely to give in to high pressure selling. It is interesting to note the extent to which the individual characteristics of a consumer will be a factor in deciding if the practice is aggressive. It has already been noted that “specific misfortunate or circumstance” is relevant where the trader is aware of that, and exploits it. It should also be noted that the vulnerable consumer test discussed above in relation to misleading practices is relevant to aggressive practices. This means that where there is an identifiable group of consumers who are “particularly vulnerable to the commercial practice or to the underlying product because of their mental or physical infirmity, age or credulity in a way which the trader could reasonably be expected to foresee” the practice is judged by the standard of an average member of that group. This will be particularly relevant where traders are dealing face to face with consumers and are thereby in a position to assess such matters, or where some characteristic of the consumer is known to the trader.

The flexibility of the provisions on aggressive commercial practices is both their strength and their weakness. Traders will, inevitably, want a clearer picture of how far they can go to persuade consumers to act in the way(s) they want. commercial practices are, after all, concerned with preference manipulation. Howells suggests that “it will be a challenge for the directive to ensure a common European understanding of which sales techniques aimed at manipulating the consumer’s will are permitted, and which are deemed illegitimate.”¹⁰⁰ Nevertheless, the provisions on aggressive practices are to be welcomed. Collins argues that “these provisions introduce a general offence that

⁹⁹ It should be noted that undue influence for the CPRs will not be the same as undue influence in private law. See Howells *Ibid* p.172.

¹⁰⁰ Howells *ibid* p. 184.

applies not only when the trader in an aggressive or threatening manner, but also when the trader deviously takes advantage of a special weakness or predicament of the consumer to induce entry into a contract.”¹⁰¹ It remains to be seen precisely how the provisions will be interpreted in practice.

3.6.3 Cooling Off Periods

Another response of particular relevance to pressure vulnerability is to use “cooling off periods”. It has been argued that cooling off periods have traditionally had two objectives. First, they protect individuals against high pressure sales, and are therefore of particular relevance to those sectors, or commercial practices, where high pressure is likely to be found. Second, they allow consumers time to access more information about a transaction, and can therefore be seen to have a role in improving competition.¹⁰² They have been incorporated into legislation in a number of areas, including doorstep selling and distance selling.

Cooling off periods have several strengths as a form of regulation. First, they are relatively market-friendly, as they make it easier for consumers to impose market discipline by making better informed decisions and, if desired, switching from one product to another.¹⁰³ Unfortunately, this argument can go only so far. In many cases, the cooling off period may be inadequate to allow the consumer to be fully informed. Because they respect consumer choice, and place few burdens on traders, cooling off periods can be supported by those who favour market-based solutions to consumer detriment. They are, perhaps, examples of “asymmetric paternalism” creating significant benefits for those who would otherwise make mistakes, but placing few burdens on other parties.¹⁰⁴ Second, and of particular relevance to this discussion, cooling off periods provide an avenue of escape from a consumer who makes a decision, not under information asymmetry, but power asymmetry. The cooling off period may be particularly important where the consumer is in a vulnerable situation (for example, in his or her own home) when entering a transaction. Unlike the provisions prohibiting aggressive commercial practices, cooling off periods provide a remedy without the need for investigation into the circumstances of the transaction.

The role of cooling off periods in protecting vulnerable consumers is interesting. They might be seen as particularly relevant for such consumers, who may be more likely than most to lack useful information, to make decisions rashly, or to feel under pressure. However, cooling off periods raise difficult distributional questions. First, because cooling off periods impose costs upon traders, that

¹⁰¹ Collins above n 83 p 109.

¹⁰² Ramsay above n. 86 p. 330.

¹⁰³ Howells sees cooling off periods as closely connected with information remedies. See Howells above n 79.

¹⁰⁴ C Camerer *et al* “Regulation for Conservatives: Behavioural Economics and the Case for Asymmetric Paternalism” (2003) *U Penn L Rev* 1211. Discussed in Ramsay above n 86 at p 346.

cost is likely to be passed on to all consumers. Like all regulatory costs, this affects most those who can least afford it. However, given that the cost is likely to be marginal this may not be a major concern. Second, and perhaps more significantly, it seems that cooling off periods will most commonly be used by relatively well informed consumers.¹⁰⁵ While they are available to all, the most vulnerable (who need them most) may be the least likely to take advantage of them. Wilhelmsson notes the operation of what he calls the “individual claims paradigm” in consumer law, where emphasis is placed on helping consumers to protect themselves and discipline the market through the action they take. He suggests that such measures operate to reproduce or even strengthen injustice as those most in need of protection (the vulnerable) are least able to take the required action.¹⁰⁶

3.6.4 Pressure Vulnerability and the Consumer as Defendant

One area where this is particularly apparent is where the consumer is not the claimant, but the defendant. It could be argued that the starkest pressure vulnerability that consumers face is when they are confronted with legal action, for example for recovery of a debt. The regulation of how consumers who find themselves in default are treated is an area of great complexity and importance. It is vital, of course, to minimise the likelihood of consumers finding themselves in default, something that can be achieved in a variety of ways, including by improving consumer education and requiring lenders to act responsibly. But it is also important to ensure that vulnerable consumers who are in default are protected from improper pressure from creditors. Some of these issues are examined below in the context of impact vulnerability.

3.7 Supply Vulnerability

A further element of vulnerability relates to the lack of choice faced by certain consumers. As noted above, although the most obvious elements of vulnerability relate to individual characteristics, it is the interaction of those characteristics with external or market factors that is liable to produce and exacerbate vulnerability. In an attempt to counter the assumptions made of consumers by classical economics and better-capture the nature of consumer decision-making, Wilhelmsson offers several visions of the consumer.¹⁰⁷ One of these is the “consumer without choices”; the consumer who has “a need which must be satisfied and there is little choice concerning the manner in which such

¹⁰⁵ See Citizen’s Advice “Can you cancel it?” CAB Evidence Briefing (Citizen’s Advice) p 4.

¹⁰⁶ T Wilhelmsson *Twelve Essays on Consumer Law and Policy* (University of Helsinki, 1996) p. 203.

¹⁰⁷ *Ibid* at pp 106-110.

satisfaction is obtained.”¹⁰⁸ Here the consumer’s vulnerability stems from a lack of options. In the context of financial services, the OFT’s former Head of Consumer Economics has recognised that “too often, attention has been focused on those who currently consume, and those who are excluded have been forgotten”¹⁰⁹ Access is likely to be of particular concern where those financial products are regarded as essential.¹¹⁰

There are several reasons why such a consumer might be vulnerable. First, there are some products which might be classed as essentials, basics or necessities. Indeed, Wilhelmsson’s point is made in the context of such products. There are difficulties in identifying when goods and services are essential. The NCC has recently argued that “energy for heating, nutritious food, clean water, healthcare, access to financial advice, are clearly basic needs, while recognising that definitions of what is basic or essential can change over time.”¹¹¹ Lack of access to some such products (such as basic financial services) might make consumers vulnerable because they exacerbate poverty. There is therefore a close link between supply vulnerability and impact vulnerability, considered below. Furthermore, lack of choice may also make consumers vulnerable because it places them at the mercy of those few suppliers with whom they are able to deal. There is therefore a close link with pressure vulnerability here, as those consumers with the fewest choices may be the most susceptible to improper pressure from those prepared to deal with them.¹¹² When Posner argues that “[t]he purchaser who is offered a printed contract on a take it or leave it basis does have a real choice; he can refuse to sign, knowing that if better terms are possible, another seller will offer them to him” he means that they will be offered if it is perceived sufficiently profitable to do so.¹¹³ Where it is only profitable to deal with a consumer at a price beyond that which the customer can comfortably afford, consumers will either be denied access, or risk putting themselves under great financial pressure by purchasing the product. A consumer is also likely to be particularly vulnerable when under pressure to make a decision quickly, for example for fear that an opportunity may be withdrawn.¹¹⁴ The Thoresen Report viewed lack of access to commercial advisors as a driver of financial vulnerability.¹¹⁵

¹⁰⁸ *Ibid* at p 110.

¹⁰⁹ Quoted in M Hewitt “Left Out in the Cold” 1999 22 *Fair Trading* 12 at 13-14.

¹¹⁰ For an early examination of some of these issues see F Williams (ed) *Why the Poor Pay More* (National Consumer Council, 1977).

¹¹¹ National Consumer Council *Paying More: Getting Less* (NCC, 2004)

¹¹² This is perhaps most stark in the area of consumer credit where loan sharks may be the only source of supply. See K Rowlinson above n. ??

¹¹³ R Posner *Economic Analysis of Law* (2nd ed, Little Brown) p 85

¹¹⁴ Note, for example, Wilhelmsson’s vision of the consumer as “snatcher” above n. 101 at p 109.

¹¹⁵ Above n.9.

3.8 Addressing Supply Vulnerability

This paper identifies three principal responses to supply vulnerability: competition-based responses; social obligations and governmental supply.

3.8.1 Competition-Based Responses

Supply vulnerability might, of course, be addressed directly by improving supply from the private sector. Governments can try to do this in market-friendly ways. Examples are reducing barriers to entry or using competition law to increase the number of suppliers.¹¹⁶ However, there are concerns with such an approach. First, it may improve supply for some consumers without improving access for the more vulnerable. Second, initiatives to improve supply such as the removal of legal barriers to entry may contribute to other forms of vulnerability.¹¹⁷ For example, the removal of licensing requirements for consumer credit firms may significantly increase the number of less reputable lenders.¹¹⁸ Increasing competition may bring advantages but should not be viewed as a panacea.

3.8.2 Social Obligations

Where products or services were traditionally provided by the public sector it is common to place social obligations (sometimes called public service or universal service obligations) on suppliers. According to Rott:¹¹⁹

“[u]niversal service means guaranteed access for everyone, whatever the economic, social or geographical situation, to a service of a specified quality at an affordable price.”

The EC Treaty recognises the existence of “services of general economic interest” which are subjected to public service obligations through a criterion of general interest.¹²⁰ Several Directives include public service obligations, including those on telecommunications, postal services, and

¹¹⁶ The OFT is currently reviewing barriers to entry in retail banking and the FSA is proposing to look at streamlining the authorisation process for new entrants. Furthermore, the Government hopes to improve competition through divestments from Lloyds Banking Group and Royal Bank of Scotland, which will mean over 900 branches will be available for purchase. See HM Treasury above n 69 chap 9.

¹¹⁷ For example, removing prior approval regimes may increase the supply of sub-standard products which put consumers at greater risk.

¹¹⁸ Note the effect of the introduction of prior approval for lenders. See Scott and Black above n 61 chap 12.

¹¹⁹ P Rott “Consumers and Services of General Interest: Is EC Consumer Law the Future?” (2007)(30)(1) *JCP* 49.

¹²⁰ See Commission Green Paper on Services of General Economic Interest COM (2003) 270 and Commission White Paper on services of General Economic Interest COM (2004) 374.

energy markets. Public service obligations found in the Directives include the right of access, the right to affordable services, and the right to identical service under comparable conditions.

The focus of these initiatives is on consumers who might not be able to access (or at least, access on what might be seen as affordable terms) services to which society considers them entitled. One challenge is to distinguish between those sectors where public service obligations can be justified, and those where they cannot. Although the principal area where these are found is that of privatised utilities, there have been suggestions that social obligations be introduced in other sectors. In his report *Vulnerable Consumers and Financial Services*, the then Director General of Fair Trading argued that there are four financial services that most consumers are likely to regard as essential: cash transmission and banking; insurance; short-term consumer credit and long-term savings.¹²¹ In April 2000 the Economic Secretary to the Treasury said she regarded banks as having “a responsibility to ensure that everyone has access to their services”.¹²² However, the Treasury’s Policy Action Team argued that “banks’ selection of which sections of the market to serve should be left to their commercial judgement.”¹²³ The case against imposing public service obligations on banks was made forcefully by Tim Sweeney, a former Director General of the British Bankers’ Association when he said: “banks are not public utilities, they are rational economic units, and can only be drawn seamlessly and easily into an approach which somehow meshes with their underlying business instincts.”¹²⁴ Banks are, of course, just one type of firm (although perhaps the most obvious) on whom such obligations might be placed.

Wilhelmsson argues that a service of general interest has the following characteristics: it fulfils a basic need of its users; there is no reasonable alternative to the service; there are few producers, and it is based on a long-term relationship. He concludes that some financial services therefore

¹²¹ *Vulnerable Consumers and Financial Services: The Report of the Director General’s Inquiry* (OFT January 1999). Domont-Naert suggested that essential financial services were: banks accounts; payment means; credit; insurance and protection against overindebtedness. It is difficult to see the final example as being a financial service, although protection is certainly important to consumers. F Domont-Naert “The Right to Basic Financial Services: Opening the Discussion” [2000] *Consum LJ* 63 at 67-69. A former President of the British Bankers Association suggested that mortgages might also be viewed as “essential requirements”. Andrew Buxton “Financial Services: Serving the Community?” speech to the Chartered Institute of Bankers 19 January 1999.

¹²² M Johnson “Speech by the Economic Secretary to the Treasury to the Conference on Tackling Financial Exclusion” 12 April 2000. See P Cartwright *Banks Consumers and Regulation* (Hart, 2004) chap 8 for discussion.

¹²³ PAT 14 para 4.2.

¹²⁴ *Ibid.*

qualify, and that a case can be made for the public service obligations on the bases of legitimate expectations and corporate responsibility. In relation to the former, he suggests that:¹²⁵

“the subjective element ‘expectations’ refers directly to the views among consumers, and the objective element ‘legitimate’ gives the courts the ability to screen those expectations by taking into account what enterprises can reasonably be expected to cope with.”

Whether consumers do expect to be offered a product or service on the same terms as others (or to be offered it at all) is an empirical question. Expectations may differ from one group to another. It seems doubtful that many consumers would believe that they are entitled to, say, a short term loan. It seems equally doubtful that they would believe they are entitled to one on the same terms as other, less risky borrowers. In either case, the courts are unlikely to regard such an expectation as legitimate. However, where banking services are concerned, it is plausible that consumers might expect to be able to open a basic bank account, and on terms that apply to all. This expectation may indeed be legitimate, particularly given the Government’s support of basic bank accounts. Those without a bank account are vulnerable in a number of ways. For example, holding cash puts them at risk of crime, and having to use cheque cashers is expensive.

In relation to corporate responsibility Wilhelmsson submits three arguments. First, he says that consumers have a special trust in (some) corporations, which justifies imposing enhanced responsibility. Second, he suggests that corporations can redistribute loss between consumers on the basis of the price mechanism. As he puts it: “[t]he losses caused by the responsibility to take into account the special needs of some consumers can be borne by the consumer collective through (usually modest) price increases.”¹²⁶ Returning to utilities, it should be noted that some of the social initiatives provided by suppliers, such as discounted tariffs, have been introduced under the concept of corporate social responsibility.¹²⁷ Third, Wilhelmsson argues that corporations should bear responsibility for problems they cause. Although there were several causes of the global financial crisis, it is common ground that banks’ lending practices were a factor. Against this background, (and the cost to taxpayers of resolving it) justifications can be found for expecting banks to take on some

¹²⁵ T Wilhelmsson, ‘Services of general interest and European private law’ in C Rickett and T Telfer (eds), *International Perspectives on Consumers’ Access to Justice* (Cambridge, Cambridge University Press, 2003) 149 at p 155. The concept was developed in particular by Hans Micklitz. See H-W Micklitz, ‘Principles of Justice Within the European Union’ in E Paasivirta and K Rissanen (eds), *Principles of Justice and the Law of the European Union* (Helsinki, Helsinki University Institute of International Economic Law, 1995).

¹²⁶ *Ibid* p 157.

¹²⁷ Research found that in 2004-5 energy suppliers spent around £100m on CSR activities.

social responsibilities. Putting obligations on banks to provide basic services is found in other jurisdictions. In the USA, the Community Reinvestment Act obliges financial institutions to show that their deposit facilities serve the convenience and needs of the community in which they are chartered to do business.¹²⁸ This includes the need for credit as well as the need for deposit services.¹²⁹ This is subject to the requirement that the bank's actions must be consistent with the sound and safe operation of the bank. Each institution's record is regularly evaluated, although the lack of sanctions for non-compliance is frequently viewed as something of a weakness. The Act is primarily an information-based measure, acting to shame the banks into action. It can also be used to highlight possible discrimination.¹³⁰

The 2010 Budget brought some of these issues into focus. The Government stated that it believes that "everyone should be able to access appropriate financial services in order to participate fully in modern day society and the economy."¹³¹ Where banking is concerned, the proposal is to introduce a universal service obligation which will give consumers the right to a basic bank account under certain conditions. The British Bankers Association remains unconvinced of the utility of this. It stated:¹³²

"It is already the case that everybody can have a bank account if they want one, unless (and this is rare) the law says they can't. Every month 40,000 more people open basic accounts. It is unclear whether a legal obligation to provide such accounts would make any difference to this steady trend."

Where affordable credit is concerned, credit unions and community development finance associations are seen to be key players. It has stated that it will consult on options to "make sure banks make an appropriate contribution to community lenders, though regulatory action or a new community levy by retail banks."¹³³ In relation to insurance, the focus has been on improving access to contents insurance among what are described as "financially excluded tenants". The ABI for example, provides information about the advantages of contents insurance to landlords. There is still work to be done on encouraging savings. The 2010 Budget noted only one example of Government

¹²⁸ 1997 12 USC 2901. See I Ramsay and T Williams "Racial and Gender Equality in Markets for Financial Services" in P Cartwright (ed) *Consumer Protection in Financial Services* (Kluwer, 1999).

¹²⁹ See J Lee "The Poor in the Financial Market" (2002) *JCP* 203 at pp 207-208.

¹³⁰ Not that it is without criticism. See e.g G Benston *The Community Reinvestment Act: looking for discrimination that isn't there* (Cato Institute, 1999).

¹³¹ HM Government *Budget 2010* para 3.68.

¹³² *BBA Budget 2010 comment*. Available at <http://www.bba.org.uk/bba/jsp/polopoly.jsp?d=145&a=17470> (accessed 23-4-10).

¹³³ Above n 126 para 3.74.

efforts to support poorer households in building savings: that of the Office of Fair Trading's "Save Xmas" campaign.

It should also be noted that there is a danger that improving access by improving supply may sometimes be a cause of vulnerability. The origins of the global financial crisis illustrate this starkly. Consumers can easily become vulnerable as a result of being encouraged to access inappropriate products. This is why we should treat carefully the list of essential services identified by the Director General of Fair Trading. The problem is not that consumers lack access to loans, for example, it is that they lack access to appropriate loans. There is a case for tightening supply (for example through responsible lending provisions) as well as for expanding it.

3.8.3 Governmental Supply

The final solutions to supply vulnerability are for the State to provide basic goods and services, or to subsidise their provision, for example through the third sector. Simple examples of this include initiatives such as the social fund (to combat a lack of supply of cheap short-term credit) and the Moneymadeclear initiative discussed above (in relation to advice and guidance). This topic raises important questions about boundaries: between consumer law and social policy; between public and private; between the market and the state. These issues are demonstrated starkly when the response to the global financial crisis is considered. This topic deserves fuller examination in its own right and can only be introduced briefly here. The Government has committed enormous resources to addressing the global financial crisis, and intervention has taken a variety of forms. Where banks are taken into public ownership, it might be argued that the Government is *de facto*, providing essential services. However, the Government has been keen to emphasise the extent to which its relationship with the banks is at arms' length. In addition, the requirement for the Government to divest in LBG and RBS will reduce its role. It is clear from the illustrations above that the focus is likely to be upon relying on the private sector (including the third sector) to address issues of supply vulnerability.

3.9 Redress Vulnerability

Another way in which consumers may be vulnerable is through the greater difficulties they face in obtaining redress (redress vulnerability). Again, there will be a connection here with other aspects of vulnerability. For example, consumers may find it difficult to secure redress because they are unaware of their legal rights, or of the mechanisms under which they can seek a resolution of their

grievances.¹³⁴ Alternatively, they may feel unable to pursue a case because of pressure that has been applied to them.

If consumers are to exert the market discipline anticipated by classical economics (and desirable where possible) they need not only to be able to make voluntary informed decisions in an environment where they are offered choice, they also to be able to act where a product turns out to be unsatisfactory. In some cases that action will take the form of switching from one supplier to another. In other cases it will involve holding a supplier to account for breach of a legal obligation and receiving redress as a result. Whether switching or suing, consumers may face significant transaction costs, particularly in the form of enforcement costs. Obtaining redress is likely to require knowledge, confidence and resources. The absence of these contributes to consumer vulnerability. In addition, consumers need effective and affordable mechanisms under which they can enforce rights against suppliers. The courts provide the paradigm for obtaining redress, but many consumers will find this prohibitive.

The barriers to obtaining redress constitute a significant, and self-perpetuating source of vulnerability. Although reputable suppliers will be expected to make reparation on the basis of a justified complaint, where the supplier is less reputable redress is less likely to be forthcoming. This problem is particularly great where “fly by night” traders are concerned, as they cannot easily be located. This presents obvious difficulties for individual consumers, but is also of concern for the operation of the market more generally.¹³⁵ If traders know that they are unlikely to be held to account, then they will be under incentives to supply poor quality products and to engage in improper conduct. Less affluent consumers are particularly likely to deal with such traders.

3.10 Addressing Redress Vulnerability

Where vulnerability results from the greater difficulty that some consumers face in obtaining redress, there are different ways to address this. The first is to make it easier for individual consumers to obtain redress.¹³⁶

¹³⁴ In the words of Barr, know how includes “knowing your entitlements...knowing your legal rights; and...your social and professional contacts”. N Barr *The Economics of the Welfare State* (check latest ed and Ramsay p 50).

¹³⁵ See Anthony J Duggan “Consumer access to justice in common law countries: a survey of issues from a law and economics perspective” in Charles EF Rickett and Thomas GW Telfer (eds) *International Perspectives on Consumers’ Access to Justice* (Cambridge, CUP) 2003, 46.

¹³⁶ See for example I Ramsay “Consumer Redress Mechanisms for Poor Quality and Defective Products” (1981) 31 *University of Toronto Law Journal* 117; W Whitford “Structuring Consumer Protection Legislation to Maximise Effectiveness” (1981) *Wisconsin Law Review* 1018; W van Boon and M Loos (eds) *Collective Enforcement of Consumer Law* (Groningen, Europa Law Publishing, 2007)

3.10.1 Facilitating Individual Litigation

Individual redress can be facilitated in a number of ways. One is by simplifying civil procedures (for example by the introduction of small claims procedures in the county court). Despite the user-friendly small claims procedure envisaged by *Justice out of Reach* in 1970,¹³⁷ the reality has been a court which is used primarily by the “well healed and articulate”.¹³⁸ As Ramsay wryly observes: “when [the poor] do appear, it is primarily as a defendant.”¹³⁹ This experience appears to be shared across the globe.¹⁴⁰ It seems unlikely that the most vulnerable consumers will benefit where they are expected to take individual action before the courts, even where the process is simplified.

3.10.2 Collective Redress

If litigation is thought necessary, but individual action unsatisfactory (for example because a large number of consumers are affected) a pooling of claims, for example through some form of collective redress, might be appropriate. Much attention has been paid to the use of class or representative actions. The classic model is what is known as the private initiative model, where a case is brought by the consumers affected through representatives who have the same (or at least a common) interest. Although the UK does not make provision for class actions, the Group Litigation Order allows individuals with the same interest to “opt in” to an action. While this overcomes some of the concerns about transaction costs, concerns about the effectiveness of the procedure remain.¹⁴¹ It is not possible to do justice to the wide range of thinking that has permeated this area.¹⁴² Suffice it to say that a number of highly influential reports have led the then Government to rethink the provision of collective redress. Rather than introduce a generic right to take collective action, the Government decided to take a sector specific approach, introducing such procedures only where there is evidence that it is necessary. The Financial Services Bill contained provision for such an approach, but proposals were dropped and so do not appear in the Financial Services Act 2010.

¹³⁷ Consumer Council *Justice out of Reach* (HMSO, 1971)

¹³⁸ J Baldwin Small Claims in County Courts in England and Wales: the Bargain Basement of Civil Justice? (OUP, 1997) p 166. Cited in Ramsay above n 86 at p 233.

¹³⁹ Ramsay *ibid.*

¹⁴⁰ Anthony J Duggan “Consumer access to justice in common law countries: a survey of issues from a law and economics perspective” in Charles EF Rickett and Thomas GW Telfer (eds) *International Perspectives on Consumers’ Access to Justice* (Cambridge, CUP) 2003, 46 at p 60.

¹⁴¹ See R Mulheron “Some Difficulties with Group Litigation Orders – And Why a Class Action is Superior” (2005) 24 *Civil Justice Quarterly* 40.

¹⁴² See for example W van Boos and M Loos *Collective Enforcement of Consumer Law* (Europa Law, 2007) C Hodges *The Reform of Class and Representative Actions in European Legal Systems* (Hart, 2008); R Mulheron *The Class Action in Common Law Legal Systems: a Comparative Perspective* (Hart, 2004).

3.10.3 Alternative Dispute Resolution: the Financial Ombudsman Service

An alternative approach is to by-pass the courts and encourage the introduction of alternative dispute resolution (ADR) mechanisms. Although the experience of ADR has been mixed, one notable success is that of the Financial Ombudsman Service (FOS). The FOS is perhaps seen by consumers as the only effective means of redress when dealing with financial services firms.¹⁴³ The FOS is a statutory scheme which allows the ombudsman to determine a case “by reference to what is, in his opinion, fair and reasonable in all the circumstances of the case”.¹⁴⁴ In considering what is fair and reasonable in all the circumstances of the case, the Ombudsman will take into account “the relevant law, regulations, regulators’ rules and guidance and standards, relevant codes of practice and, where appropriate, what he considers to have been good industry practice at the relevant time”.¹⁴⁵ It is clear that this test is extremely broad and flexible. It has been suggested that the essence of the Ombudsman’s function is to ensure fairness; in the words of James “the requirement to do justice in the individual case, free from the constraints of formal precedent and taking a common sense approach.”¹⁴⁶

Despite such welcome initiatives, concerns remain about whether the interests of vulnerable consumers are appropriately protected. If the transaction costs involved in searching, bargaining and switching are perceived to be difficult, those of enforcing rights through the legal process are likely to be seen as even more troublesome. Consumers have been said sometimes to need “superspite” if they are hold suppliers to account for their wrongs.¹⁴⁷ Wilhelmsson argues that the emphasis placed upon corrective justice – the so-called “individual claims paradigm” – may have negative distributive effects, favouring the educated and affluent at the expense of less sophisticated and lower income consumers. Schemes such as the FOS provide a useful tool.

3.10.4 Regulatory Enforcement and Redress

There are alternative approaches, such as allowing regulators to take action on behalf of consumers, or creating new bodies such as the once proposed Consumer Advocate, to do the same. Research has found a number of concerns among enforcement authorities at taking representative actions on

¹⁴³ See R James ‘The Application of the EC Recommendations on the principles Applicable to Out of court Procedures to the New Arrangements for the settlement of Consumer Complaints in the UK Financial Sector’ [1999] Consumer Law Journal 443.

¹⁴⁴ FSA DISP 3.8.1.R

¹⁴⁵ *Ibid*

¹⁴⁶ R James *Private Ombudsmen and Public Law* p 206. This flexibility has come in for some criticism. Lord Ackner, when commenting on the private ombudsmen schemes that preceded the FOS suggested that such tests made the industry “the hostage to fortune of uncertain and therefore unpredictable liability.” (Lord Ackner, *Report on a Unified Complaints Procedure* (London, 1993, PIA) para 93. Cited in James and Morris “The New FOS” at 185). The FOS has recognised the need to be more open about the way it makes decisions.

¹⁴⁷ A Leff “Injury, Ignorance and Spite – the Dynamics of Coercive Collection” (1970) 80 *Yale LJ* 1.

behalf of consumers.¹⁴⁸ However, the Regulatory Enforcement and Sanctions Act 2008 does contain some new sanctioning tools that can be used to secure redress. One such power is to require a firm to restore the position as if the offence had not been committed. In the context of consumer law, this might mean providing redress for consumers in the form of compensation. However, the powers can only be used where an offence is committed. Moreover, the Financial Services and Markets Act 2000 contains powers for the FSA to apply to the court for a restitution order under s.382 and also gives the FSA administrative powers to require restitution under s.384. In deciding whether to use such powers, the FSA will consider a range of factors, such as: whether there are better ways in which redress could be obtained (for example through the FOS or, where the firm is insolvent, the Financial Services Compensation Scheme) and whether it is the best use of the FSA's resources. It is clear that the powers will be used only rarely but the FSA recognises that: "where a large number of persons have been affected or the losses are substantial, it may be more appropriate for the FSA to seek or require restitution from a firm."¹⁴⁹

It should not be thought that enforcement authorities will be a panacea for redress vulnerability. Ramsay suggests that:¹⁵⁰

"[t]he recognition that public authorities often have limited resources and that public enforcement waxes and wanes in response to political and public interest in consumer issues suggests that private actions may compensate for under-enforcement by public agencies."

One provision that deserves some attention is found in s.404 of FSMA (as amended by the Financial Services Act 2010).¹⁵¹ Where it appears to the FSA that there has been a widespread or regular failure by firms to comply with their requirements, consumers have suffered actionable loss or damage and it is desirable to make rules for the purpose of securing redress, the FSA may make rules requiring firms to establish and operate a consumer redress scheme. This would require each firm to investigate if it has failed to comply with its requirements, determine if that failure has caused loss or damage to consumers, and, if it has, determine what the redress should be and make that redress. When considering if it is desirable to make its powers, the FSA must consult with the FOS. The impact of this new Scheme remains to be seen. It is attractive from the perspective of the

¹⁴⁸ J Peysner and A Nurse Representative Actions and Restorative Justice (BERR, 2008) p 39.

¹⁴⁹ FSA *Enforcement Guide* para 11.3.

¹⁵⁰ Ramsay above n 86 p 264.

¹⁵¹ For discussion of the original s.404 see J Gray "The Legislative Basis of System Review and Compensation for the Misselling of Retail Financial Services and Products" (2004) 25(3) *Statute Law Review* 196.

vulnerable consumer, because the onus is upon the firm to investigate and, if appropriate, make redress to consumers. This gets around some of the difficulties presented by transaction costs which are likely otherwise to prevent vulnerable consumers obtaining redress. However, it is likely that the powers under s.404 will be used only sparingly, the Government having statute that it will be used “only in the most grievous cases.”¹⁵²

There is always likely to be a range of provisions under which consumers can potentially receive redress. A key is to ensure that within that range, there are measures that enable the most vulnerable consumers to obtain satisfaction. Public enforcement and the existence of a truly consumer-friendly ADR regime appear the most appropriate mechanisms for vulnerable consumers. However, a note of caution should be adopted here. The Coalition Government has signalled a fundamental change in the landscape of consumer protection with many responsibilities to be transferred to Citizens Advice. While it is too early to comment with any confidence what impact this will have, there is concern that consumer protection and consumer redress may suffer without considerable investment.

3.11 Impact Vulnerability

Impact vulnerability concerns the greater effect of loss, or harm, on certain consumers.¹⁵³ The operation of the theoretical perfect market has been emphasised. The responses identified above can all be justified, at least in part, as responses to market failure. They all help the market to function and might therefore be viewed as market correcting.

However, it should be noted that there are other possible justifications for intervention in the market place. We might refer to such interventions as “non-economic” or “social”. It is true that some of the solutions discussed above might be better classified as non-economic, in particular placing social obligations upon suppliers. But that is nevertheless a response to a market failure. Tackling informational, pressure, supply and redress vulnerability are all concerned, at least to some extent, with improving the working of the market for vulnerable consumers. They reduce the likelihood of consumers making adverse choices, and provide avenues of redress where breaches take place.

¹⁵² HM Treasury *Reforming Financial Markets: a Summary of Responses* Nov 2009 para 2.88.

¹⁵³ Again there are difficulties in terminology. The CAV Paper starts by using the word “injury” but then moves to “detriment”, stating that “detriment is used interchangeably with injury in this paper” (above n 4 at p 10). Detriment is capable of a number of meanings, as the paper.

Where impact vulnerability is concerned, the issues can be conceptualised slightly differently. We are concerned with the greater impact that choices have on certain consumers. Where there has been a breach of the law (such as a misrepresentation, breach of contract or deception) then, provided redress vulnerability can be addressed, the vulnerable consumer should be protected. But there will be cases where no such breach can be identified. The consumer has simply made a decision which has had a particularly deleterious impact upon him or her. Where financial services are concerned, this will relate chiefly to poverty. In its White Paper *Modern Markets, Confident Consumers* the UK Government emphasised how “the poorest in society are least able to afford the consequences of bad decisions.”¹⁵⁴ It has been argued that poverty is perhaps the most significant factor in vulnerability, as well as a constant justification for consumer law. As Ramsay has observed: “[a]lthough few consumer protection measures have specifically identified the poor consumer as the intended beneficiary of legislation, the alleviation of problems of poverty and the disadvantaged...has been a continuing undercurrent in consumer protection.”¹⁵⁵

The greater loss suffered by vulnerable consumers from making inappropriate decisions is likely to result from low income and/or low wealth. Cowell and Gardiner concluded that a detriment of £1 suffered by a consumer with half the national average income was as significant as detriment of £2.50 suffered by a consumer with average income.¹⁵⁶ Problems for low income consumers are compounded by the fact that they are likely to pay more than others for their goods and services. The best-known work to come to this conclusion is Caplowitz’s seminal *The Poor Pay More*, but other works reach similar conclusions.¹⁵⁷ More recently, the National Consumer Council identified a number of reasons for this: the need to pay by cash; the inability to buy in bulk; the difficulty in accessing a variety of suppliers; and the tendency for suppliers to charge more, for example for credit.¹⁵⁸ Low-income consumers are also likely to face particular problems where long-term financial products are concerned because they are more likely than average to suffer job insecurity and so be unable to maintain regular payments.¹⁵⁹ Impact vulnerability is particularly apparent where a consumer is in debt and faces action from creditors. Personal insolvencies grew by around 5% in 2008 to almost 130,000, and have continued to rise through 2009.¹⁶⁰ Consumer law has

¹⁵⁴ HM Government *Modern Markets: Confident Consumers* (HMSO 1999).

¹⁵⁵ I Ramsay above n 86 at p 88.

¹⁵⁶ OFT *Welfare Weights* (OFT 282, January 2000)

¹⁵⁷ See also A Andreasen *The Disadvantaged Consumer*, F Williams (ed) *Why the Poor Pay More* (NCC, 1977) and, most recently, National Consumer Council *Paying More: Getting Less* (NCC 2004).

¹⁵⁸ See e.g. National Consumer Council (*ibid*).

¹⁵⁹ OFT *Job Insecurity for the Vulnerable: Is it Increasing?* (OFT, January 1999).

¹⁶⁰ HM Government *A Better Deal for Consumers* Cm 7669 (July 2009) p 15.

traditionally focused primarily on the consumer as claimant or complainant, seeking redress for the wrongs of a supplier. But it is vital also to recognise the needs of consumers when they face action, particularly that from creditors.¹⁶¹

3.12 Addressing Impact Vulnerability

It was noted above that Burden saw the greater impact suffered by particular consumers as one of the two key aspects of vulnerability. Its importance should not be doubted; but nor should the difficulty of tackling it satisfactorily.

The ideal way of reducing impact vulnerability is to reduce the chance of the consumer making a decision that will have such an impact. A consumer who is well-informed, confident and capable, acting with choice and without pressure in circumstances where he has a remedy should it need to be used is unlikely to make such a decision. Impact vulnerability can, therefore, perhaps be best tackled by addressing the other forms of vulnerability identified and discussed above.

However, it is clear that some consumers will, even in a well-functioning market, make decisions which have significant negative impact upon them. In the free market, this might be classified as unfortunate. Schelling observed that freedom to make decisions means the freedom to make mistakes.¹⁶² But an environment which provides no form of relief for the consumer facing a significant burden is unlikely to be widely regarded as acceptable.

3.12.1 Compensation Schemes

Public policy provides a range of responses to impact vulnerability in the form of safety nets. Unemployment and sickness benefits are obvious examples.¹⁶³ But there may also be a role for consumer protection law. One example of particular note where financial services are concerned is that of the Financial Services Compensation Scheme (FSCS). The FSCS can be described as the UK's compensation fund of last resort for customers of authorised financial services firms. It provides compensation if a firm is unable, or likely to be unable, to pay claims against it, for example if the firm has stopped trading or has been declared to be in default. The FSCS now protects a range of

¹⁶¹ Such recognition is on the part of the Government is apparent. See *ibid.*

¹⁶² T Schelling *Choice and Consequence* (Harvard University Press, 1984) p 144.

¹⁶³ Barr draws a distinction between the "Piggy Bank" and the "Robin Hood" functions of the welfare state. It is the latter which seeks to relieve poverty and reduce social exclusion by redistributing income and wealth. See N Barr *The Welfare State as Piggy Bank* (2001, Oxford, OUP).

products, namely: deposits, insurance policies, and insurance broking; investment business, and home finance. There are limits to the protection provided, although for deposits, investments and home finance the limits are all now £50,000 per person per firm declared in default.

The rationale for financial compensation schemes may differ depending upon the product and sector concerned. For example, one of the rationales for deposit insurance is that by providing an incentive for depositors to leave their cash in an institution the danger of a run on the bank, and the systemic risk that might result, is minimised. However, perhaps the principal rationale for compensation schemes is consumer protection. It is possible to see the basis of compensation schemes as information asymmetry. For example, a consumer may be more concerned with the financial stability of the firm offering a product, than the different types of financial product available. Indeed, it has been argued that “[t]he public availability of meaningful information sufficient for people to make informed decisions about the likely standing of banks both individually and relatively is the keystone of market discipline”.¹⁶⁴ However, it is unrealistic in practice to expect consumers to make an informed judgement about a firm’s solvency. Attempts have been made to provide such information, but their success has been limited.¹⁶⁵ Compensation schemes do not correct information asymmetry. Instead, they make the choice of provider less significant than it would otherwise be. But there is another element to the consumer protection rationale for compensation schemes. Such schemes might be justified on the basis of the significant loss that would be suffered by consumers when a firm fails. Consumers frequently have a large proportion of their assets in the form of deposits, and this proportion is likely to be particularly high for the less sophisticated.¹⁶⁶ The need to provide some form of safety net for consumers therefore forms part of the justification for compensation schemes. Moreover, as well as standing to lose the highest proportion of their assets, vulnerable consumers are likely to be the least able to judge the soundness of an institution, making it particularly important to provide the safety net of compensation.

3.12.2 *Social Force Majeure and Consumer Debt*

Safety nets may benefit vulnerable consumers in other ways. There are techniques, for example, which allow the court to examine whether a bargain became unfair because of circumstances that did not exist at the time of formation. An illustration of this is the “social force majeure” scheme found in Nordic law.¹⁶⁷ Wilhelmsson identifies four characteristics of social force majeure: First of all,

¹⁶⁴ D Mayes, *A More Market Based Approach to Maintaining Market Stability* (FSA Occasional Paper 10, August 2000).

¹⁶⁵ *Ibid.*

¹⁶⁶ See R Cranston, *Principles of Banking Law* (2nd ed) (Clarendon Press, 2002) at 78-80.

¹⁶⁷ See T Wilhelmsson ““Social Force Majeure” – A New Concept in Nordic Consumer Law” (1990) 13 *JCP* 1; T Wilhelmsson above n 101.

the consumer is affected by some special occurrence. Wilhelmsson gives the examples of an unfavourable change to health, work, housing or family. Typical examples might be physical illness, unemployment, termination of a lease or divorce. Secondly, there has to be a causal link between the occurrence in question and the consumer's ability to meet his obligations. Thirdly, the consumer must not have foreseen the special occurrence at the time that the contract was concluded. Finally, the occurrence must not be attributable to any fault on the part of the consumer. The effects would depend on the particular case in point. For example, a supplier might have his remedies restricted or be prevented from avoiding the contract, and the consumer might be able to withdraw from, or terminate the contract.

An important point to emphasise here is that social force majeure takes effect where the consumer *becomes* (more) vulnerable after having entered the contract. It acts as a kind of safety net in the event of unanticipated events which affect the ability of consumers to meet their obligations.¹⁶⁸ This raises some difficulty for the law. Chief among these is indeterminacy. As will be seen later, there are a number of ways in which the courts can challenge a contract on the basis of its being unfair. Although the courts are likely to be influenced by the fairness of the outcome, their task is to consider whether the term is unfair of itself. The court is looking at the position of the parties at the time that they entered the contract. With social force majeure, the question is whether the provision is now unfair, bearing in mind what has happened. It is possible to make too much of this distinction.

Like compensation schemes, social force majeure operates as a form of compulsory insurance policy. From the perspective of reducing impact vulnerability, social force majeure schemes appear attractive. However, they raise concerns. First, there is an argument that they generate moral hazard. Knowing that they will be protected in the event of adverse circumstances, consumers may be more willing to take risks. However, this criticism can be over stated. As noted above, the circumstances must have been both unforeseen and have occurred without fault on the part of the consumer. Second, social force majeure may make it more difficult to construct markets. Traders will not be in a position to identify, when the contract is formed, the position s/he will be in should the consumer default. While this is a potential concern, the cost can be managed, for example through insurance. Third, there is a danger that social force majeure might be exclusionary, either by raising the cost of a transaction (to incorporate the price of default) or by reducing supply by disincentivising traders from entering (or continuing in) the market. These concerns should be

¹⁶⁸ It is therefore distinguishable from provisions such as the Unfair Terms in Consumer Contracts Regulations which allow the consumer to argue that the provision was unfair from the start.

taken seriously, but it is submitted that they do not present an insurmountable hurdle. Many of the objections apply similarly to tools such as cooling off periods.

In the UK, these issues are well known in the area of consumer credit and debt. It is well established that a high proportion of debtors will be unable rather than unwilling to meet their obligations. The relationship between controlling creditors' remedies and other aspects of consumer protection of the vulnerable has been noted. Ramsay suggests that "an enforcement system that does not protect debtors' rights may result in an over-extension of credit or create incentives for irresponsible or fraudulent marketing."¹⁶⁹ Regulation may operate in a variety of ways.¹⁷⁰ In some cases the focus will be on giving the consumer information. For example, the obligation to provide a debtor with an arrears information sheet is designed to help the parties to reach an agreement (often with the help of a third party), while the requirement for creditors to give debtors notice before they terminate an agreement, recover possession of goods or enforce a security gives the debtor time to respond. In other cases there will be requirements to obtain court orders before specific action is taken against the debtor. However, the most significant issues where impact vulnerability is concerned involve the restructuring (or writing down) of debt. Where a consumer is unable to repay debt then a number of actions are possible. These include individual voluntary agreements (IVAs); administration orders; bankruptcy and debt relief orders (DROs). While all consumers using these mechanisms might be regarded as vulnerable, it is DROs that are perhaps of most note here. They are aimed at people who do not own their own home, who have little surplus income and assets and who owe less than £15,000 of debt. A DRO lasts for 12 months, during which time creditors cannot take any action without a court's permission. After that time the debtor whose circumstances have not changed is freed from the debts that were included in the order. Rather than involve the courts, DROs are run by The Insolvency Service in partnership with "approved intermediaries" (debt advisers).

The examples above are not intended to constitute an exhaustive examination of the ways in which impact vulnerability might be addressed. In some cases more informal responses might be appropriate. For example, the Lending Code sets out procedures to follow where a consumer is in financial difficulty. But it is clear that substantive law plays a particularly important role.

¹⁶⁹ Ramsay above n 86 at p 580.

¹⁷⁰ See Ramsay above n 86 chap 10.

5. Part Four: Conclusions

A common justification for regulation of financial services is the need to protect the consumer, but consumers are a heterogeneous group. Protecting such a wide and diverse group presents the authorities with a range of challenges. One such challenge is to design policies which take appropriate account of the interests of those consumers who might be described as vulnerable. Consumer vulnerability has been examined by a number of commentators and has been recognised by legislation. But disagreement remains about how vulnerable consumers should be defined, and how their interests might best be addressed.

This paper has had two main objectives.

First, it has considered how “the vulnerable consumer” might be understood. It has done this first by looking at how vulnerability has been conceptualised by commentators, and secondly by examining how the law currently takes account of the interests of vulnerable consumers. This has demonstrated that we can conceive of “vulnerable consumers” in different ways. It has also revealed both that a range of legal provisions make reference to vulnerable consumers, and that a range of tools, or techniques, take account of their interests.

Secondly, and crucially, the paper has established a novel “taxonomy of vulnerability”. This consists of a range of elements which, taken together, help to identify where vulnerability is liable to exist. The elements are classified by the paper as: information vulnerability; pressure vulnerability; supply vulnerability; redress vulnerability; and impact vulnerability. In order to be of practical as well as academic relevance, the paper has identified how key stakeholders (legislators and regulators in particular, but also firms and others) might use the taxonomy in practice to ensure that the interests of vulnerable consumers are appropriately addressed.

Deciding on how, and by whom the interests of vulnerable consumers should be addressed requires careful consideration and political judgement. It is not suggested that the answers will be easy. Nevertheless, it is argued that the taxonomy provides a useful tool through which the questions can be addressed. While these might be viewed as questions primarily for legislators and regulators, they have implications for others too. For example, firms concerned about whether their sales and marketing methods are fair to vulnerable consumers may decide to use the taxonomy to help answer this. While it will not always provide a definitive answer, it should help both to clarify the questions to be asked, and to illuminate the responses. As a consequence, the paper has raised

issues of great interest and relevance to a wide range of parties concerned with the relationship between firms and consumers, including legislators, regulators, firms, consumers and their advisors. It is impossible to avoid the conclusion that an optimum system which encourages and respects consumer choice, but which also ensures that the most vulnerable and protected appropriately is difficult to design. Through the taxonomy of vulnerability, this paper offers some idea of the factors such a system might have to take into account. It also considers the role that other stakeholders, including firms themselves, might be expected to play. While the paper by no means provides the last word, it is hoped that it constitutes a helpful starting point.