Consumer Finance Monitor (Season 6, Episode 15): Performance-Based Regulation: A New Approach to Consumer Financial Regulation, with Special Guest Lauren Willis, Professor of Law and Associate Dean for Research, LMU Loyola Law School

Speakers: Alan Kaplinsky and Lauren Willis

Alan Kaplinsky:

Welcome to the award-winning Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer finance and what they mean for your business, your customers, and the industry. This is a weekly show brought to you by the Consumer Financial Services Group at the Ballard Spahr law firm. I'm your host, Alan Kaplinsky, the former practice group leader for 25 years, and now senior counsel of the Consumer Financial Services Group at Ballard Spahr. And I'll be moderating today's program.

For those of you who want even more information about consumer finance, don't forget about our blog, ConsumerFinanceMonitor.com. We've hosted the blog since 2011, so there is a lot of relevant content there. We also regularly host webinars on subjects of interest to those in the industry. So to subscribe to our blog or to get on the list for our webinars, please visit us at BallardSpahr.com.

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It's my very special pleasure to invite to our show today Lauren Willis. And in a moment, I will tell you what we're going to talk about. But first of all, let me tell you a little bit about Lauren. She's aprofessor of law and the associate dean for research at LMU Loyola Law School in Los Angeles, and has held visiting appointments at Harvard, Cornell, and Penn Law School. She's a leading critic of the use of financial education, disclosures, and, quote, "nudges," or that's another way of saying behavioral economics, I believe, for regulating consumer transactions. She's developed a groundbreaking performance-based approach to consumer law that unites the interests of firms with their customers and enables regulators to keep pace with rapid marketplace change. More recently, she has identified how law must evolve to address a new threat to fair competition and consumer protection, namely the business use of artificial intelligence to design and target online communications and interfaces.

Before academia, Professor Willis worked at the U.S. Department of Justice and with the Federal Trade Commission. She co-founded the Consumer Law Scholars Conference and was an advisor to the American Law Institute's Consumer Contracts Restatement project. And very recently, she was admitted to be a fellow in the American College of Consumer Financial Services.

So, before we go any further, a very warm welcome to Lauren.

Lauren Willis:

Thank you so much, Alan. It's a pleasure to be here.

Alan Kaplinsky:

Great. Let me just say a little bit about what we're going to be talking about. And if I get anything wrong, let me know about it. So, performance-based regulation is an approach that requires firms to meet certain outcome benchmarks. For example, factories have their emissions monitored for pollutants, and are required to emit no more than a certain amount. Or if they do, the firm will be sanctioned. In the consumer-law context, the outcome could be consumer understanding. A firm would need to demonstrate that its customers generally are not confused about key facts about the product or service they bought from the firm. Or the outcome could be substantive. A firm would need to demonstrate that its customers generally are not suffering from poor consequences as a result of the product or service they bought from the firm.

This truly is groundbreaking. And I must admit, until I started reading, I guess you would say the law review article that broke the ground, a University of Chicago law review article called Performance-Based Consumer Law, published in 2015, I didn't know anything about it. What I did know is that the current system we're using right now, which is generally based on disclosures or it's regulations that are prohibited, thou shalt do this, thou shalt not do that, I guess referred to sometimes as design-based regulations, that they're not working. So, I definitely share that view with Lauren.

But, Lauren, let me ask you some questions, because we're going to dig a little deeper into this article that you've written. Why did you develop this new approach to consumer law?

Lauren Willis:

Well, as you said, Alan, traditional disclosure and what I call design regulation, requiring products to have certain design features, really has not done a good job of creating the kind of marketplace for consumers that we want, right? A marketplace where consumers actually exercise autonomy, know what they're getting and get what they believe they're getting, where consumers can consistently engage in welfare-enhancing transactions and make good choices. And one thing that I kept seeing over and over again was that firms really are able to run circles around consumers and regulators, and AI is only going to make this move more quickly. So I was looking for something else.

Alan Kaplinsky:

Yeah, okay. Was this idea something that had been percolating in your mind before you wrote that article in the University of Chicago in 2015?

Lauren Willis:

Well, I had written a critique of disclosure regulation. I wrote it actually in my first law review article in 2006, before the mortgage meltdown, and had seen the ways in which disclosures... and I first witnessed this actually at the Federal Trade Commission working with consumers, the way that disclosures were really not connected to the way in which consumers were making decisions. You know?

Alan Kaplinsky:

Yeah. I mean, I know something about consumer-finance law, but I'll be the first one to tell you, I go in to buy a new car or lease a car or get a loan, I want to get out of there quickly. I want to know where do I sign. I understand that I'm going to be bound by everything that I've signed. I can't plead ignorance and try to get out of something in the contract that I later don't like. But it's certainly not working very well. Maybe it works a little bit better in the advertising requirements of the Truth in Lending Act. But when it comes to disclosures, particularly disclosures given to you when you're actually entering into the transaction or right before, yeah, they don't work.

Let me ask you another couple of other things. You also have criticized what I think I think what would be described as behavioral economics, the use of nudges. And at least to my way of thinking, the CFPB very much believes in the use of nudges. I mean, most of the economists that have been advising them over the years are behavioral economists. What's the problem that you have with that, Lauren?

Lauren Willis:

Well, again, firms are really able to run circles around mandated nudges. So it's not that I'm against behavioral economics as an analytical tool, but in terms of who's going to be the better nudger, it's going to be a firm that can experiment on customers, that can microtarget them in real time. So you design one nudge, if you're a regulator, and it's got to apply to everybody.

Maybe it works in the abstract, but then when you make a firm deploy the nudge, the firm can surround it with other types of information and can deploy it in a way that it's not going to be effective. The big example of this being the overdraft default, that firms were able to counteract that nudge quite effectively for those consumers who had been engaging in overdraft transactions.

And when consumers were interviewed, they said things like, "I opted out because when I said yes, I thought what that meant was that I wouldn't be charged overdraft." So consumers were completely confused. In addition, some of them said, "Hey, the reason I opted out is because every time I went into online banking, every time I had to click through a screen asking me, did I want overdraft or did I not want overdraft. And the only way to speed up my ability to do my transactions was to say, 'Yes, fine, I'll take the overdraft. I'll agree to it as a general matter and get out of the default that the regulation had put me in so that I can just get on with my life and get on with my banking.'" And of course, once you had agreed, banks would never ask you again because you'd switched to the position they wanted you to be in.

Alan Kaplinsky:

Right, right, right. We're going to get back in a little bit to the example that you gave of overdraft protection and, if we use performance-based regulation, how would it be applied in that context.

But before I get there, we've talked about disclosure regulation not working, the use of nudges not being effective. I assume that you have the same feeling about what you call design regulation. The regulations that say, thou shalt and thou shalt not. Am I right?

Lauren Willis:

Issues with design regulation are sort of on both ends. They're often over-inclusive and they're often under-inclusive. There's always some consumer for which some interesting and difficult-to-understand product is suitable. Because we're all different. We have different situations. So some design regulation cuts off innovation that could be good for consumers. Now, we might decide that's a price we want to pay, given how much welfare is actually really increased by getting that doctor into a home while they're in their residency versus making them wait two years to buy a house, or whatever it is. But we end up, often, then, being under-inclusive.

Firms can run circles around some of these rules, and payday lenders are really the masters of what I call shape-shifting, right? You make a loan that's just over the size or the maturity rule of the regulation, or you recast the transaction to appear to be check cashing or credit repair, or I think there's an infamous case where the lender was pretending that it was a computer rental. Not that these things aren't eventually caught, or at least some of them, but it just goes to show that the regulation itself is under-inclusive.

Alan Kaplinsky:

Yeah. You mentioned payday lending. And of course, the CFPB, long ago, under Richard Cordray as director, tried to promulgate a regulation, and half of it got thrown out dealing with the ability to repay. We're not going to get into the tortured history of that case. That would take our entire podcast show. But with respect to a requirement, that ability-to-repay is, you have to be able to demonstrate that to make a loan. That's a kind of performance-based regulation, isn't it? It's a suitability requirement.

Lauren Willis:

Not exactly. No. An ability-to-pay rule is a rule that's applied prior to entering the transaction. So it is potentially effective, potentially not effective. But the way in which we would approach it from a performance-based angle is to look at the outcome. I like this language that the payday lender association uses, that a payday loan is supposed to be a financial taxi. It's supposed to get you from one paycheck to another when you're faced with a small, short-term cash need. So the question is whether you're actually using it for a small, short-term cash need or for a long-term deficiency in your budget.

Originally, actually, in the proposal for that payday regulation, there was one performance-based piece of it. And that was for some of the longer, 6-12 months loans, so not your traditional payday, but a bit longer that community banks were making, so small loans. And part of that originally was that a bank could demonstrate, based on the pool of these loans, that it had no more than a 5% portfolio default rate after the fact. And if they exceeded that performance benchmark, they would have to disgorge and refund to consumers the fees that were charged over the prior year. And it was tested on an annual basis. Now, that never made it into the regulation in the end, but that's the idea.

Alan Kaplinsky:

But there's a real risk element here, isn't there, for a company because going into it, the company can say they're being as studious as they can and it's important to them that they treat consumers right, fairly, and that consumers understand what they're doing. They still may make a mistake in developing this product or whatever it is. And if they're going to be measured on whether they did it right or made a mistake after the fact down the road, and get hit with a requirement of disgorgement or an enforcement action by a federal or state agency, that strikes me as being unfair to the company, that the company is going to have to make guesses as to what's down the road going to be found to meet a certain benchmark.

Lauren Willis:

Well, it can be and it might not be. You might tie the portfolio default rate in that particular example to some economic indicators. So rather than having it as a set 5% rate, it might be tied to economic indicators that are local to the payday lender. But the other thing that the payday lenders' associations, in addition to this financial taxi test for payday loans, the purpose of payday loans, they also talk about workouts. And it's certainly possible for a firm to do a workout with a consumer on a payday loan and then not end up with a default. Obviously, every situation will be unique, but the payday lender association does suggest that payday lenders should be engaging in workouts if a loan has been already been flipped once, that then at that point, the lender should step in and do a workout.

Alan Kaplinsky:

Okay. Well, we've sort of danced around the subject of your article, but let's delve right into it. I mean, I tried to define performance-based consumer law as I was introducing our subject today. Did I do that right, or is there anything more that you'd like to add to that?

Lauren Willis:

Well, you did an excellent job, Alan, of course. And you're certainly right that the idea is to be something rather similar to an emissions standards. The idea is that we don't care how the firm gets to the outcome. We're going to let the firm -- that is, the expert on what's the most cost-effective way to produce the outcomes that we're seeking -- decide how to get there. So, for an emissions situation, they can change the fuel source, they can add scrubbers, they can restrict their operations, whatever they want to do to get to that point.

In the consumer context, obviously, what we're seeking at the end of the day is that a firm's customers are not confused by the transactions they've engaged in, or where it's not a matter so much of understanding, instead that the products are suitable so that the products are channeled to customers who do not suffer ill consequences from using the product. So we might call them confusion and consequences caps. And these would have to be demonstrated through field audits of a firm's actual customers. So we're not thinking about this in the abstract, what do we think a reasonable consumer would do, yada, yada. And instead, we are actually looking at the firm's actual customers.

So then firms would be incentivized not to try to cross the T and dot the I on the disclosure rule that may or may not even work or meet the design regulation that may be under- or over-inclusive, but instead are really incentivized to get to that competitive marketplace, where consumers understand transactions and, therefore, are able to select those that are best for them, and a fair marketplace, one where consumers are engaging in transactions that do not result in bad consequences. And firms can use whatever means they want to get there, right? They can use-

Alan Kaplinsky:

No, no. You say that, but yet, in your article, you do go out of your way to point out that you're not advocating that performance-based regulation replace disclosures and design-based regulation. So, you want to keep the system that we have now and then layer this on top. I think you might have developed more support in the industry if you said, "Let's get rid of disclosures. Let's get rid of design-based regulation. It's not working. This is the way the new system is going to work." So, why is it that you decided "We got to keep all these bad systems and then layer this on top"?

Lauren Willis:

Well, partly, it's wanting to go step by step. I certainly would foresee in the long-term that some of the disclosure and design regulation would change. And particularly, we would think about disclosure regulation differently, right? For a firm to make sure that customers understand, are not confused about key facts, it helps if all of industry is disclosing those key facts in a standardized way. So the role of disclosure would not be you have to make it look the specific way because we have the goal that this alone will achieve what we want to achieve. Instead, it's more of a coordinating function. So you don't end up with some sort of competition violation by firms coordinating on their marketing or disclosures. So, the role of the disclosure changes... And it's something that the industry would certainly be very involved in trying to help government shape in a way that would lead to customers understanding those key facts, for example.

I also see this form of regulation as something that could be deployed in a variety of ways. So it doesn't have to necessarily be something where we start with making it a full-blown regulatory scheme. It's the sort of thing where we might use it in court orders or consent decrees when a firm has been found to have violated, say, the UDAAP rules. And then rather than the firm promising, or in the consent decree being ordered, to cease and desist from deceiving consumers, instead require the firm to actually hire independent expert auditors to demonstrate through random sample testing of their customers that their customers are no longer being deceived, for example.

Alan Kaplinsky:

Okay. As you were talking, it occurred to me that there is a very, I would say, an old issue in the consumer-finance regulatory world that still hasn't gone away. And that's something called insurance packing, where mostly, it was a problem in the consumer-finance industry, not really in the banking industry, where consumer-finance companies would make a lot of their profit based on the sale of credit insurance. Now, credit insurance, if somebody really wants it and doesn't have other life insurance, it can actually be a very valuable product. But very often... I mean, I've been involved over the years in class actions where I have defended cases that involved so-called insurance packing, and you would find penetration levels that were very, very high, like 95% or higher of the people have signed up for credit life, disability insurance, maybe a variety of other bells and whistles. The type of performance-based regulation that you're talking about, would you have something, a benchmark that would say, "No more than 50% of your people can buy this product"?

Lauren Willis:

I might not have that kind of a benchmark because that's not very responsive to different firms, customer pools, but one can imagine two performance-based approaches to this issue, or maybe three. So one is, doing some kind of consumer confusion audit. Do consumers know that they've purchased it? Do they know it's optional? Because this tends to be something consumers think they're required to get, at least interviews have shown that. And do they know what it actually covers? You might use an 85% understanding rate, no more than 15% of consumers being confused about these facts, just to borrow from Lanham Act and FTC Act cases.

You also might use an approach that is similar to what we actually use for over-the-counter drug regulation, which is a counter-indications kind of cap. This would be a form of consequences cap, that when we bring a drug over the counter, we require a sort of initial test phase where the drug is put out in a certain number of drugstores, and those who self-select the drug are then tracked to see whether they were the customers who had some kind of counter indication for the drug or not. So here, you might do something like that in testing to see, are these people who have already purchased this product, do they already have life insurance that's going to cover this, or do they already have a disability that disqualifies them from receiving compensation from this insurance product? So, that's a kind of consequences cap. And that would be done through auditing to determine whether that was happening.

Another thing that I've talked about with some regulators in another country is, looking at what the payout rates are. If the payout rates are just unreasonable for insurance, that there would be some sort of broader cap about what the payout rates were, how profitable this really was. I'm not saying the 50% rule is not the right way to go. Maybe it is, we could compare it. But it's not precisely what I had in mind with performance regulation.

Alan Kaplinsky:

Yeah, good. Actually, as you have articulated it, I like it better. I wouldn't like that kind of a benchmark. Maybe there are some people that really need the credit insurance. And if you've hit the quota for the month, then you can't offer it to them. So, as I was mentioning this, I was saying to myself, I don't think that works very well.

So, how are the performance outcomes or these benchmarks that we talk about that a firm or company must meet, how do they get determined to begin with?

Lauren Willis:

Well, the benchmarks could be chosen in a variety of ways. One, as I mentioned, could be borrowing from the FTC Act cases on deception or the Lanham Act, a confusion standard, which generally, it's sort of maybe 10% in the FTC Act cases, but more like 15% in the Lanham Act cases. Okay, some people are going to be confused, but that's the cap. That's as much as should be reasonable.

Another possibility is, for the regulator, to have to do testing, broad testing in the market, and figure out what the median is. For different firms that are selling the same product, what are their customer confusion or poor consequences rates, understanding what proportion. And then require everybody to pull up to the median. So pull up the laggards, something like that. Or you could require people to pull up to the top 25%. That's what we actually do in the environmental area, using best available technology rules.

So, there's a variety of ways in which these benchmarks might be set. Implicitly, we are creating certain outcomes with existing disclosure regulation, existing design regulation. We just don't bother to figure out what the outcomes are currently. What the confusion rate is, even with these disclosures or what proportion of consumers experience poor consequences despite disclosures and design regulations And a performance based approach would make us be more explicit about the process and where we really want to go.

Alan Kaplinsky:

Right. A little earlier, you alluded to an auditing process that would be undertaken after the fact to see how the company has done in meeting these benchmarks. How does that auditing process work? Is that something that's done internally within the company, or did you contemplate there'd be a government agency, state or federal, that would be, in effect, the examination that would be done by an agency, or is it a combination of the two?

Lauren Willis:

Well, I could see an agency doing it internally just to figure out then which firms to monitor or look at more closely for UDAAP violations or something like this. But in terms of being part of a consent decree or court-ordered remedy, I would think you would need independent, third-party, neutral expert. So the same types of experts that testify in a Lanham Act case, for example.

And interestingly, in the Lending Club case [brought by] the Federal Trade Commission, Lending Club actually did this. They hired a third-party independent expert and academic at Penn, I believe, who went and, obviously had to use the firm's apparatus to do this, tested customers as they received their loans to determine whether or not customers understood that they were going to be paying fees, because the claim was that there had been deceptive advertising, this no-fee kind of advertising. And as it turned out, everybody understood they were actually paying fees. So, the third-party neutral expert demonstrated through random sample testing of customers, real customers in real time, that the customers were not deceived, and that was successful.

Or a long time ago, the Federal Trade Commission had this case against Hawaiian Punch, requiring them to demonstrate that customers understood that it wasn't really fruit juice, and required third-party neutral random testing of consumers. The flaw in that particular case was that they didn't have any real sanction built in when they didn't meet the benchmarks. So there wasn't an incentive to try to meet the benchmark quickly, and it went on for, I think, a decade or so.

Alan Kaplinsky:

Yeah. Let's now circle back to other use cases in the consumer-finance area. You reminded me of Hawaiian Punch used to be one of my favorite drinks as a kid. I don't think it exists anymore. But I used to love it. But anyway, let's talk about overdrafts and how it would work there, a performance-based regulation.

Lauren Willis:

Well, you might require banks to demonstrate that their account holders know, immediately before taking an action that's going to trigger an overdraft, that it is going to trigger an overdraft and somewhere close to the amount of the fee, because part of the issue here tends to be that consumers maybe think, "Oh, yeah, I'm going to have to pay a little overdraft fee," and don't realize that actually it's going to have some cascading effects such that they're going to pay quite a bit. To some extent, banks are already doing this. Some banks are actually sending text alerts to their customers. But by requiring demonstration that the customers know about it and choose to go ahead and buy that $35 cup of coffee or whatever it is, then all banks would have to do it, not just the few that have chosen to.

And there may be some consumers who don't have cell phones, who aren't getting texts, and then you might need to come up with a different way to inform them. So, the idea then is to incentivize the bank to make sure customers know when they're going to incur [a fee]. And so the customers have the choice, have the autonomy to choose, "I want to pay $35 for a cup of coffee or I don't." And banks could also either explain the details of the fee structure to the customer in real time, could choose to simplify the fee structure such that you don't end up with these sort of cascading fees, you end up with just a very clear, it's always going to be $35, it's never going to snowball into a hundred or whatever it is.

Alan Kaplinsky:

In the consumer-finance area, are there other examples or other use cases that come to mind?

Lauren Willis:

Well, the sort of related area of data privacy, that's an area where people don't read these long privacy disclosures.

Alan Kaplinsky:

What a colossal waste of money, isn't it? I mean, it's ridiculous.

Lauren Willis:

Yeah, it's crazy. So, instead, you might test customers of a firm to ensure that customers know what personal data is being collected, who else is going to get that data besides the firm that's collecting it, and for what uses it will be put. And unless the firm is able to demonstrate that 85%, or whatever the percent is, of customers understand those things, the firm would not be allowed to retain this data. If you can't get people to understand it, you can't use it and share it. Obviously, you will have already collected it in the first place. But again, this would be sort of like the payday loans lookback period that you would use. So, that's another potential use.

And really anything with fees, customer understanding. In the investments area, you might require certain risk categories to be met that you could use more of a consequences cap for some of that. Is this a retiree who's investing? And we have these indicators that this is contraindicated for the individual's portfolio to take on this additional risk, sort of those kinds of things.

Alan Kaplinsky:

Let's say somebody, a Congressman, senator, takes an interest in this idea. Is this something that would require new legislation, either at the federal level or the state level, or is this something that within the existing legislative framework, your idea could be adopted?

Lauren Willis:

Well, to be adopted sort of wholesale would require a new regulation, if it was a whole-of-government kind of approach to consumer products and services. But there are some laws on the books that would allow for this. Dodd-Frank tasks the CFPB with rulemaking to ensure consumers understand the cost, benefits, and risks of the transactions, the financial products, as those will play out over the entire term of the consumer's use of the product, rather than requiring a particular disclosure. Or perhaps in somewhat of a dance with coordinating disclosures, the CFPB could pass regulations that required no more than a certain proportion of customers to be confused about cost benefits or risks of a product.

There's lots of places where the law requires something to be clear and conspicuous. So those may be places there where regulators would be able to use this as well. And there's lots of other areas outside of consumer finance that might allow for these things, like pesticides and customer understanding of pesticide uses, things that are more like the over-the-counter drug situation.

Alan Kaplinsky:

So, the auditing and the testing process, that sounds to me like it's going to cost a lot of money. You have to hire a third-party auditor, like law firms. They don't come cheaply. They probably charge by the hour. Isn't the net result of all this going to be that companies are going to end up raising prices so that consumers will actually be paying for this new level of protection, it won't be borne by the companies? Is that okay?

Lauren Willis:

Certainly, it's the type of regulation that, because it's sort of a new way of approaching things, we might not want to do wholesale to start with. So we might want to do it through consent decrees, firms that really have already hornswoggled consumers, and they ought to make it right.

Alan Kaplinsky:

Just on that point, Lauren, have you seen that happen yet in any either FTC, CFPB, or state attorney general consent orders?

Lauren Willis:

Yes and no. The Washington state case against one of these for-profit schools, part of a consent decree required them to put in place a computer system that monitored all of the phone calls between their, essentially, salespeople, I think they called them educational assistants or something like this, and that would detect any sort of false statements, false promises about whether the degree, for example, qualified someone to be a beautician or something.

Also, in the same area, we have the gainful employment rules, which are essentially sort of a lagging indicator of whether or not you've actually provided a real education to people. So, we've used that there. But it's also the type of thing we might start with larger players, although the difference between a large and a small player, of course, now is a little bit in dispute with SVB and all. We also might subsidize auditing for smaller players.

Alan Kaplinsky:

I was going to ask you... That was going to be my next question. In other words, yeah, maybe something like this wouldn't be exorbitantly expensive for a major financial institution to adopt. But what about the... We have thousands of banks and credit unions in the country. A lot of them don't have in-house lawyers. A lot of them are very unsophisticated. What do you do with them? Do you exempt them entirely, or-

Lauren Willis:

One possibility is do that, another possibility is subsidizing auditing. But honestly, when you look at their response to the overdraft default, what you notice is that these small banks and community banks hired third-party consultants who came in and developed marketing materials that essentially tricked people into changing the default, to opting out of the no-overdraft default. And it's the type of thing where certainly a third-party industry would grow up of consultants that would do this for so many small institutions. I mean, a small bank isn't going to do this by themselves. And so, like many other things, we would have specialization that would just naturally grow up.

Alan Kaplinsky:

Right. I mean, to me, while you've given some examples of instances where it's being applied right now, I think you'd acknowledge this would be a major change in the law. This would be very impactful, very significant. Are there any regulators, let's say outside the US, that are using this type of regulation right now?

Lauren Willis:

Well, I've worked with Australia and a little bit with the UK over the past, I guess, seven years on adopting approaches like this for financial products. Australia is doing something that's a bit of a modified version of this. They have enacted what are called the design and distribution obligations. And they require firms, for a product, to define who is an appropriate customer for this product. Then, firms need to demonstrate that those are the customers that have purchased the product. So, the firm sets its own bar, essentially, sets its own performance benchmark in some sense.

I mean, obviously, it has to explain why it is suitable for this type of consumer and why it's unsuitable for other types of consumers. But then the firm has to test -- both the issuer of the product and if they have a third party that's doing the sales, the distributor -- has to demonstrate it's actually getting to the right customers and not being sold to those customers for whom it's inappropriate. Now, the implementation of that was delayed due to COVID. So, what's really happened so far is that firms have just started putting out their descriptions of what the appropriate market is for each product, but they haven't gotten quite to the testing stage yet.

The UK, the Financial Conduct Authority, has gone further, although that is a more recent legislation that hasn't come into effect yet. It's called the Consumer Duty, and it really places the duty on financial-services firms to ensure that their customers are experiencing good outcome from the products, the transactions they're engaging in. So, there, it's really quite broad. They talk about it both, not only at origination -- are the right customers buying the right products? -- but during the course of the relationship with the financial institution, that customers are being assisted adequately if they want to switch to a new provider, if they want to change products, if they want to end an account so that the servicing part of the relationship is also covered. Now, as I said, this is brand new. We don't know how it's working out in practice yet. I am hoping to go there and find out as it unfolds.

Alan Kaplinsky:

Yeah. I'd like to ask you what you think of something called principles-based regulation, which is something I thought the UK uses. Well, why don't you describe what that is for our listeners, and I'd like to get your thoughts on it.

Lauren Willis:

Well, they had the Treating Customers Fairly principle, the Financial Conduct Authority. And they found that that was not sufficient, which is why they've now adopted the Consumer Duty, which is more outcomes-focused as opposed to "Let's make sure we're treating people well in the process of obtaining something." And they just, I think, found that it was too vague of a principle to be able to really get firms to comply with and adequately monitor and enforce when you have something that's that vague. Here, by seeing more concretely what the outcomes are, the hope is that this will be more effective than the principles-based regulation for customer transactions with financial institutions.

Alan Kaplinsky:

Right, right. Okay, well, I think we've come to pretty much the end of our show for today, but before we sign off, Lauren, is there anything else, a question that I should have asked you, that I neglected to, that you think our listeners ought to be aware of when it comes to this topic?

Lauren Willis:

No, I think you asked a lot of good questions, Alan. I would say that the potential benefits here are really, I think, quite enormous in terms of just changing how we're thinking about regulation, and that we should be especially concerned in an era of AI when firms are able to have microtargeted marketing. Nobody can go out and check all that marketing to make sure it's not deceptive if you got thousands of ads, but you could do random sample testing of customers to see whether-- whatever marketing they received -- they understood what it was they were doing with the firm. So, I think this type of regulation is becoming more and more necessary as things move faster and faster.

Alan Kaplinsky:

Well, again, Lauren, thank you very much for being a guest on our program today and educating me greatly on this subject and, I'm sure, educating our listeners. I have to have you back in a couple of years and get an update on where things stand.

Lauren Willis:

Thank you, Alan. I would love to do that.

Alan Kaplinsky:

Yeah.

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