

Understanding and Overcoming Confusion in Consumer Financial Decision Making

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Outline

- Confusion definition/constructs within financial context
- The broader context, regulators and financial confusion:
 - Expectations about confusion have evolved and are reflected in various inquiries including
 - Financial Services Inquiry (I), Super System Review, Financial Services Inquiry (II), Royal Commission
- Test Structural Model of Financial Confusion Proneness & Financial Literacy (*WIP*)
 - Investigate mediators and moderators

Financial Confusion & Financial Literacy

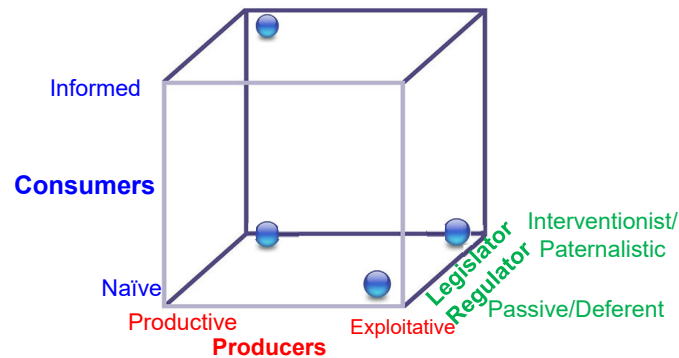
- How is financial confusion related to financial literacy?
 - Financial literacy as “a personal finance form of consumer expertise” (Ward and Lynch, 2019)
 - the understanding of, or at least the ability to understand, and apply/engage in short-term financial management as well as long-term financial planning (Remund 2010)

Confusion

- Confusion: Mature literature “burdened with incompatible definitions & conceptualisations, insufficient agreement even about the meaning of the most foundational term – **confusion**” (Kasabov, 2015)
- “Consumer confusion is a mental state characterised by a lack of clear and orderly thought and behaviour” (Leek & Kun 2006)
- “subjective consumer experiences of **mental discomfort** and **behavioural uncertainty** engendered by **misjudgements**, **information processing errors** and **inaccurate beliefs** relating to products or services” (Kasabov, 2015)

Financial Confusion and Context

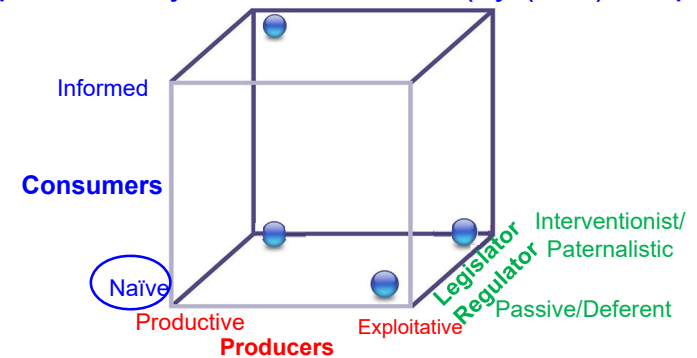
Financial Confusion emerges from the interaction of Consumers, Providers (Institutions), & Regulators in different markets and products – context is important



Financial Confusion and Context

Naïve Consumers can result from:

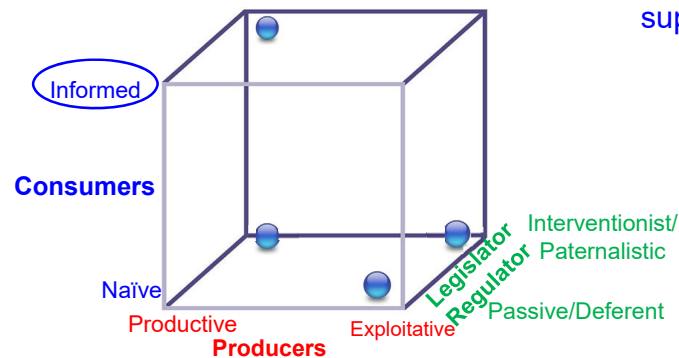
- Non-comprehension:
 - fundamental capacity (level of) financial literacy
 - constrained by time (application of) financial literacy
- Compounded by non-disclosure? (by (non)compliance)



Financial Confusion and Context

Informed:

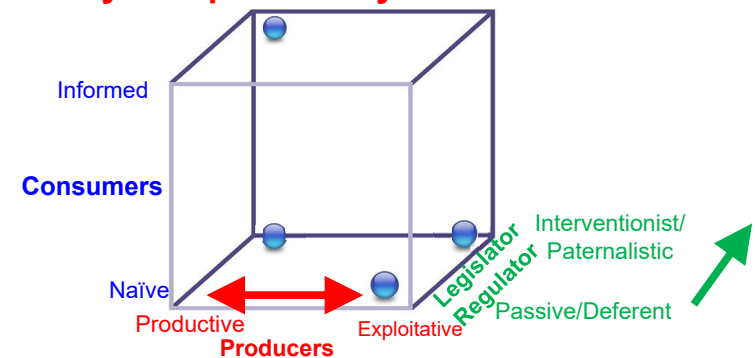
- Financially literate, capable consumer
- Via advice (paid/unpaid)
- But confusion is market specific (E.g. CFD vs Mortgage)
- Clouded by inducement? (e.g. CFDs, frequent flyer with super)



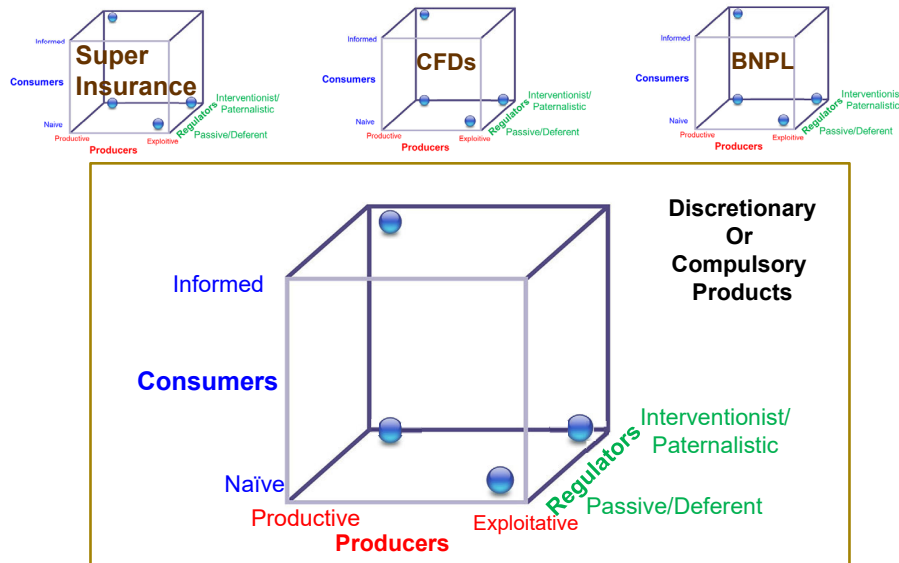
Financial Confusion and Context

Regulatory environment, philosophies, vary and change

Producers interact within the context, productively & exploitatively



Financial Confusion and Context



Changing regulatory philosophy

- Financial Regulation Philosophy has evolved largely reflecting changed assumptions about consumer behaviour
- **Financial Services Inquiry (I)** (1996) retains the optimism of the role of markets given the rational consumer agent model
- FSI (I) does refer to confusion and makes reflections which have been restated in subsequent reviews & inquiries
 - Confusion is not solely a description of consumers
 - exists within financial institutions and regulators
 - Confusion can be the inevitable outcome of institutional practice – it doesn't reflect a failing of the consumer
 - Confusion can be the objective

Changing regulatory philosophy

- FSI (I) reference to actual consumer confusion
 - “the risk of **consumer confusion** about risk and features is not limited to complex products ... case studies [show] ... **consumers** may also misunderstand less **complex products** and their core **features** and **risk**” (p.209)
 - Due to general proliferation of products from deregulation (p.595,651) and some (life) products (p.652)
- Reference to industry & regulatory confusion
 - The nature of what constitutes personal information (p.185)
 - As an outcome of regulatory design – multiple agencies (p.243)
 - Created by the nature of disclosure (p.261)
 - Confused nature of industry structure (p.329)
 - Regulatory structure (p.506, 544)

Changing regulatory philosophy

- **But, Financial Services Inquiry (I)** (1996) retains optimism of the rational consumer agent model
 - “consumers are assumed, for the most part, to be the best judges of their own interests. ... **disclosure requirements play an important role in assisting consumers to make informed judgments.** However, ... For many financial products, consumers lack (and cannot efficiently obtain) the knowledge, experience or judgment required to make informed decisions” ^{p.191}
 - “complexity of financial products increases the probability that financially unsophisticated consumers can **misunderstand** or **be misled** about the nature of financial promises, ... obligations & risks. This ... has led most countries to establish a **disclosure regime for financial products that is considerably more intense than disclosure rules for ... non-financial products**
- **Recommendation:** “the Inquiry believes that there would be both a philosophical justification and a practical need to wind back the more intense forms of prudential regulation **and to shift the focus of regulation more to conduct by market participants and disclosure of information.**” (p.14)

Changing regulatory philosophy



- Financial Regulation Philosophy (Financial Services Inquiry (I), 1996)
 - “consumers are assumed, for the most part, to be the best judges of their own interests. ... **disclosure requirements play an important role in assisting consumers to make informed judgments.** However, ... For many financial products, consumers lack (and cannot efficiently obtain) the knowledge, experience or judgment required to make informed decisions” p.191
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Super System Review



Source: <https://treasury.gov.au/review/super-system-review>

- Subsequent reviews become less optimistic, more critical
- “These [Wallis] settings assume that members have the tools at their disposal, ... the necessary regulatory protections in the market place, to enable them to make optimal decisions about their investment strategies, about when to enter and exit the market, and about what to do with their super on reaching retirement. In a compulsory system, it also assumes that members have the requisite degree of interest.”
- **“But, for many members, this is not the case**
 - **Literacy:** 46% would struggle to understand documentation such as job applications, maps and payroll forms
 - 53% reached just the second of five levels in a practical **numeracy** test
 - 70% managed only to progress to level 2 in **problem-solving**
 - Level 3 is regarded ... as the minimum required for individuals to meet the complex demands of everyday life and work ...”

Super System Review



Source: <https://treasury.gov.au/review/super-system-review>

- Notably the report refers more to confusion among the industry (trustees) in terms of
 - Their duties & obligations (p.46, 47)
 - What ESG requirements require them to do (p.181)
 - Complexity of the legislation (for SMSFs) (p.229)
 - Proposed changes (p.241)

Parliamentary Joint Committee on Corporations and Financial Services: Inquiry into financial products and services in Australia (2009, aka Ripoll)



- Also questions disclosure (rational model)
- Confusion evident among consumers
 - Vertical integration and role of advisers (p.50,67)
- But also among industry
 - Between institutions (e.g. banks, advisers) (p.38,50)
- And as a consequence of industry behaviour
 - Description of products, risk (p.67)
 - Lack of transparent fees (p.129)
- Raised by industry as a tactic/reason to avoid change (p.195)

Financial Services Inquiry (II)



- *Further move away from rational agent model, more highlighting of biased behaviour*
- *FSI (II) includes “Developments since Wallis Inquiry”* “Behavioural biases undermine the assumption that individuals are ‘rational’. They limit the efficacy of disclosure as a regulatory tool and can lead to sub-optimal outcomes for consumers”
- One reference to confusion relating to individuals
 - “the risk of **consumer confusion** about risk and features is not limited to complex products ... **consumers** may also misunderstand less **complex products** and their core **features** and **risk**” (p.209)
- If not confused – is there **misunderstanding**?
 - 4 references for consumer: product complexity, not recognising product attributes (insurance policy exclusions); basic (lack of) knowledge of risk
 - 41 references to (questioning) consumer understanding

Royal Commission into Misconduct in the Banking, Superannuation & Financial Services Industry



- Royal Commission mentions “confuse”, “confused”, “confusion” 5 times in its final report (Volume 1)
 - **none** of these relate to consumer confusion
 - “**confusion** of roles” (employees) (p.2)
 - “Advisers became sellers and sellers became advisers” (p.1)
 - assessment of trustee comments about limited applicability of “Best-Interests Duty” (p.227)
 - “such observations are more likely to **confuse** than to assist” (p.225)
 - Productivity Commission’s assessment “[c]onduct regulation arrangements for the super system are **confusing** and opaque
 - Effective governance of regulators: “having the effect of **confusing** and diluting accountabilities between the Minister, board and chief executive” (p.474)

Royal Commission into Misconduct in the Banking, Superannuation & Financial Services Industry (Vol 2) 15 uses of confus/e/ed/ion/ing



- Institutional
 - CBA argue **confusion** in interpretation of regulations by ASIC (p.76)
 - “Onepath custodians” engaging with IOOF too early could ‘**confuse** the very deliberate and careful considerations and the component parts of our decision.’” (p.176)
 - Deputy Chair of ASIC rejecting **confusion** about regulatory roles
- Institution as the source of confusion
 - Hostplus rejecting that letters they sent to members may have caused **confusion or misled** them their members that they would lose their balance to the ATO (p.216)
 - Deliberate policy of misselling “accidental death cover, combined with an accidental injury rider” where customer didn’t qualify for life insurance cover (p.308). It was the instructions given to agents to deliberately achieve a “**confused**” outcome of clients. **Confusion was desired outcome**
 - Acceptance by Commlnsure that their communication was a **source of confusion** to customer claiming on a heart attack insurance claim (p.319)

Royal Commission into Misconduct in the Banking, Superannuation & Financial Services Industry (Vol 2) 15 uses of confus/e/ed/ion/ing



- Institutional source, cont.
 - Acceptance by Commlnsure that lack of definition in their policy resulted in **confusion** in definition (radical breast surgery) (p.322)
- **Confusion** due to communications of AMP resulting in customers paying higher insurance fees (p.371)
- Claim by youi that it consciously did not provide information to clarify a term because it judged it would **confuse** customers whereas the commission considered that behaviour caused the **confusion** (p.432)
- AAI Limited (AAI) did not agree that its inclusion of a definition of reasonable cost into a supplementary PDS defined as “defined to mean the lesser amount of any quotes obtained by AAI” (p.440) was **confusing**.

- “Understanding” & variations referenced 136 times in RC Final report: majority relate to industry (regulators, funds, trustees, employees) **understanding** of legislation/regulation or roles (e.g. trustees)
- Minority refer to understanding of consumers & reflect on unsuitability and unreasonableness consumers’ task
 - E.g. “It is easy for consumers to **misunderstand** such questions” (insurer questions) p.299
 - “I just don’t how a customer in a phone call that lasts 20 minutes can come to a view of ... **understanding exactly** what they’ve bought in a fairly complex sort of area of financial services.” p.280

- One of the four major observations made by RC
 - [Exploitation of] “the asymmetry of power and information between financial services entities and their customers” p.1
- **Confusion as the objective**
 - Mandatory/default products, e.g. superannuation
 - Equilibrium level of confusion

Confusion and responsibility

- Confusion discussion linked with responsibility of “agents” for confusion & understanding
 - Regulator
 - Industry
 - Consumer
- FSI I consumer “incidental”, FSI II consumer more active agent with responsibilities
- PJJ (Storm), FSRC apportion blame/responsibility for confusion & bad behaviour
- SSR – in between

Behaviour Responsibility

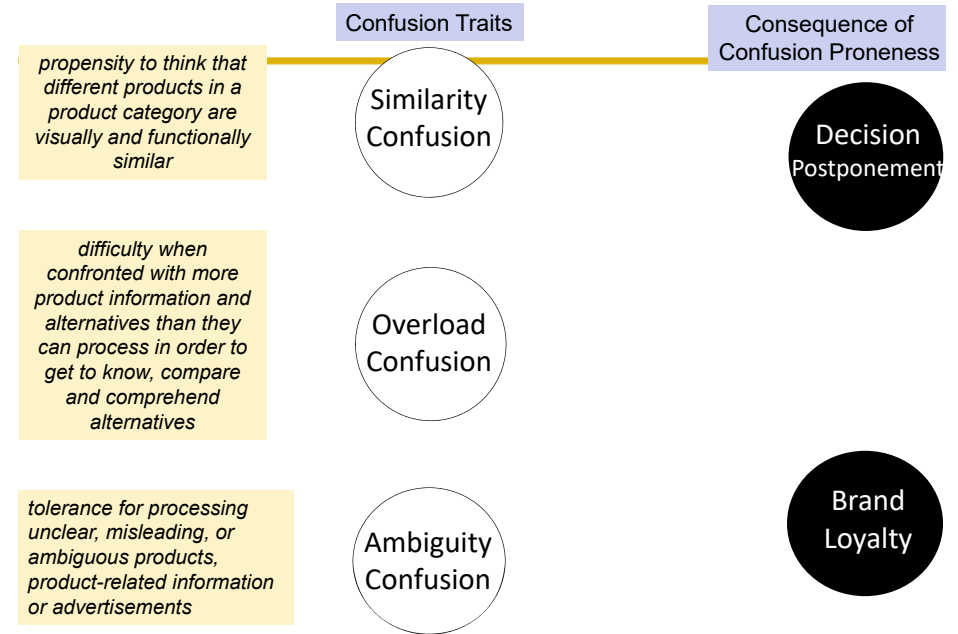
- FSI I discussion of responsibility primarily structural
 - Regulators (93 references)
 - e.g. “The main options appear to be either to vest responsibility in the RBA, or to establish a new stand-alone regulator” p.313
 - Industry (11 references)
 - Only 2 mentions of consumer responsibility
 - Related to increased responsibility from superannuation
- FSI II discussion – less discussion, more on consumer
 - Consumer (9 references)
 - “Fair treatment does not involve shielding consumers from responsibility for their financial decisions” p.6
 - Regulators (14 references)
 - “The Inquiry’s philosophy places great responsibility on policy makers, particularly regulators” p.11
 - Industry (8 references)
 - “Financial institutions have a responsibility to operate with integrity to build and protect trust and confidence in the financial system” p.38

Behaviour Responsibility

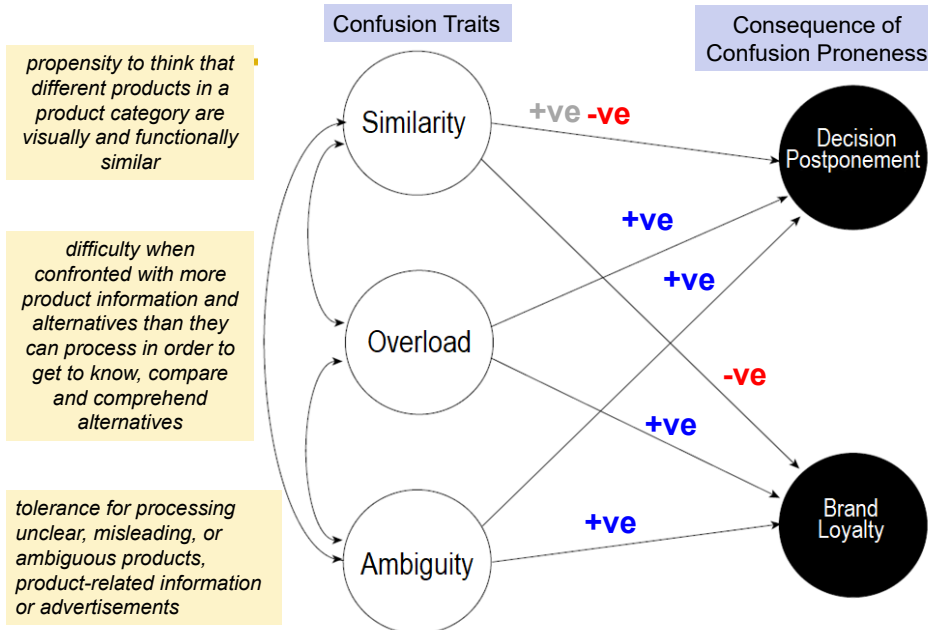


- PJCCFS: primarily (understandably) industry/advisers
 - Industry (28 references)
 - “There seems to have been an unacceptable degree of confusion and abdication of responsibility” p.38
 - CBA (Norris) sharing responsibility: “In truth, a degree of responsibility rests on the shoulders of banks, individuals and the regulator to a greater or lesser degree, and primarily on Storm Financial” p.49
 - Consumer (6 references)
 - “There is a need to better inform consumers about the products signed up for, so that consumers can take a higher degree of responsibility for financial decisions and only buy products that entail a comfortable level of risk” p.30
 - Regulator (4 references)

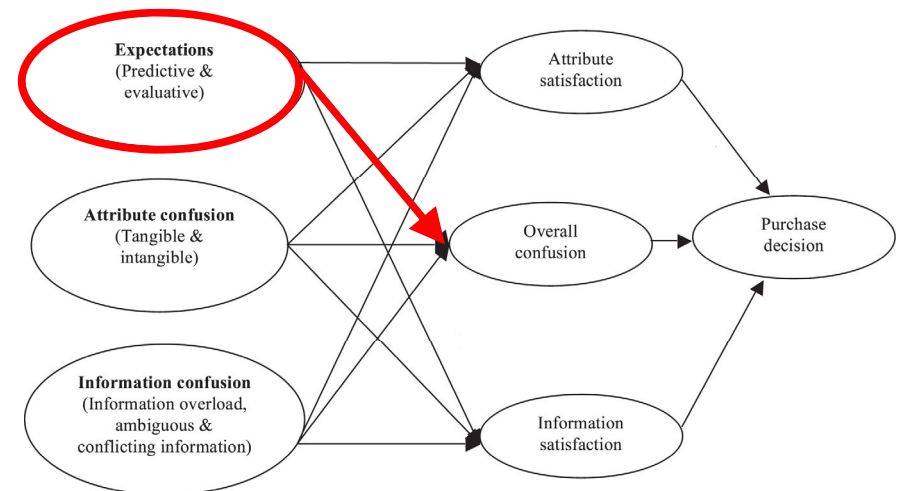
Walsh, G., Hennig-Thurau, T. & Mitchell, V-W. (2007) Consumer confusion proneness: scale development, validation, and application. *Journal of Marketing Management*, 23:7-8, 697-721

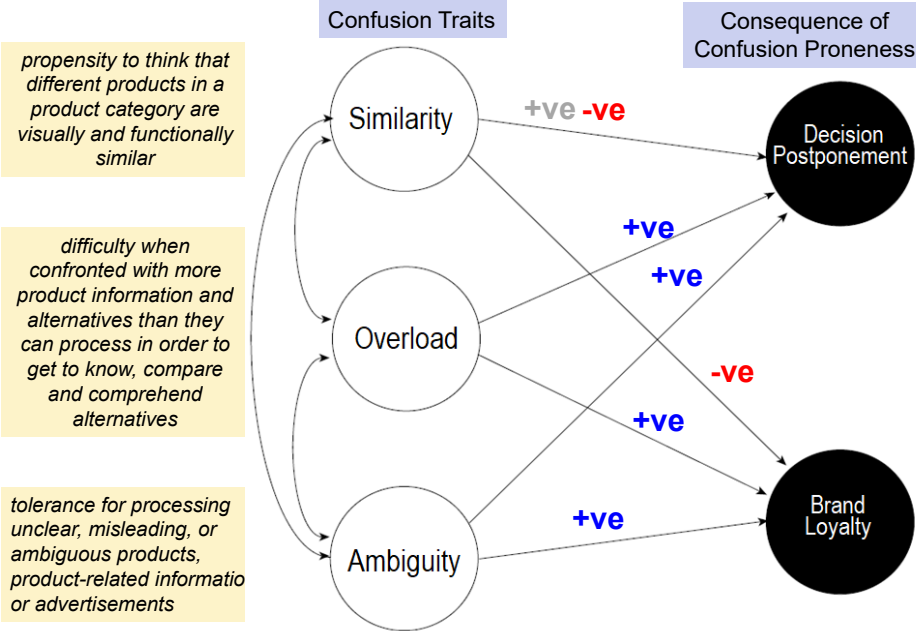


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Shukla, P., Banerjee, M., Adidam, P.T. (2010). Antecedents and Consequences of Consumer Confusion: Analysis of the Financial Services. *Advances in Consumer Research*, 37. 292-298.





Adaptation Walsh et al. (2007)

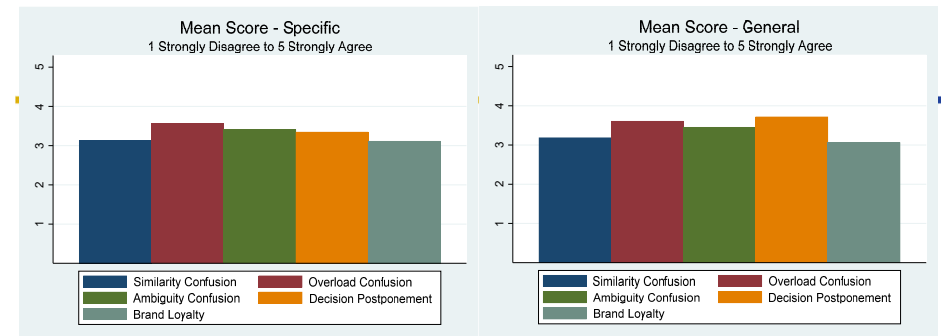
Confusion Traits	
Similarity Confusion	<p>Due to the great similarity of many financial products it is often difficult to detect new financial products</p> <p>Some financial companies brands look so similar that it is uncertain whether they are made by the same manufacturer or not</p> <p>Sometimes I want to use a financial product seen in an advertisement, but cannot identify it clearly between scores of similar financial products.</p>
Overload Confusion	<p>I do not always know exactly which financial product meets my needs best.</p> <p>There are so many financial companies brands to choose from that I sometime feel confused</p> <p>Due to the host of financial companies brands it is sometimes difficult to decide who to select from</p> <p>Most financial companies brands are very similar and are therefore hard to distinguish</p>
Ambiguity Confusion	<p>Financial products often have so many features that a comparison of different financial companies brands is barely possible.</p> <p>The information I get from advertising often is so vague that it is hard to know what a financial product can actually perform.</p> <p>When choosing a financial product I rarely feel sufficiently informed</p> <p>When choosing certain financial products I feel uncertain as to product features that are particularly important for me.</p> <p>When purchasing certain financial products, I need the help of sales personnel to understand differences between products.</p>

Confusion Consequences	
Decision Postponement	<p>Sometimes it is difficult to arrive at a decision when making a financial choice about financial products purchase</p> <p>Sometimes when making a choice about financial products purchase I delay the decision.</p> <p>Sometimes one postpones a planned choice about financial products purchase</p> <p>Sometimes the choice in a store of financial products from a company is so large that a decision purchase takes longer than expected</p>
Brand Loyalty	<p>Once I find a financial company brand I like, I stick with it</p> <p>I usually choose financial products from buy the same company brand</p> <p>I change financial company brands regularly</p>

Variation: savings accounts

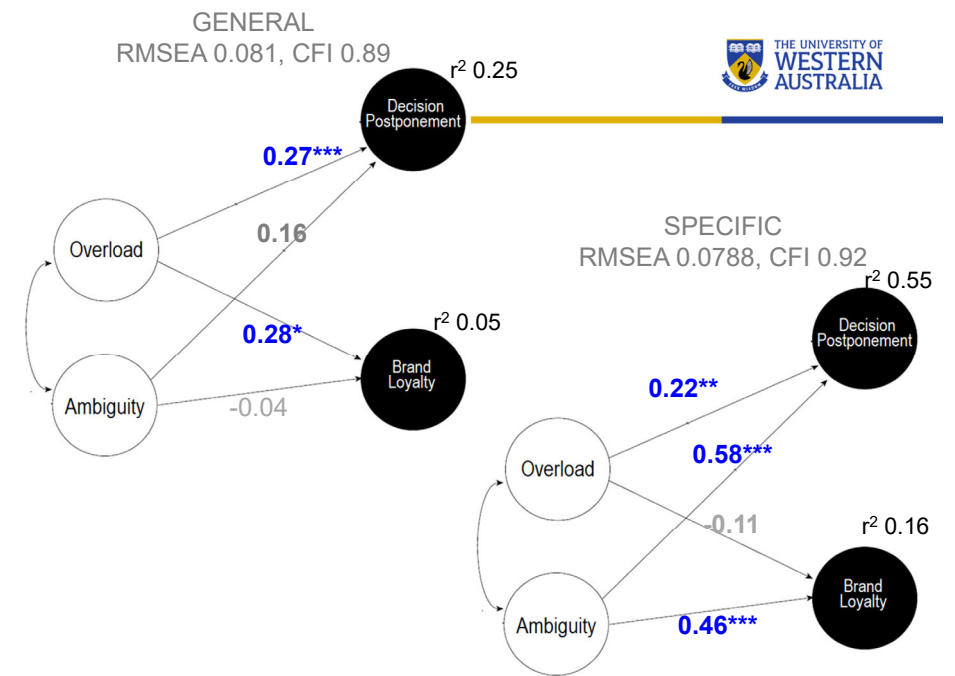
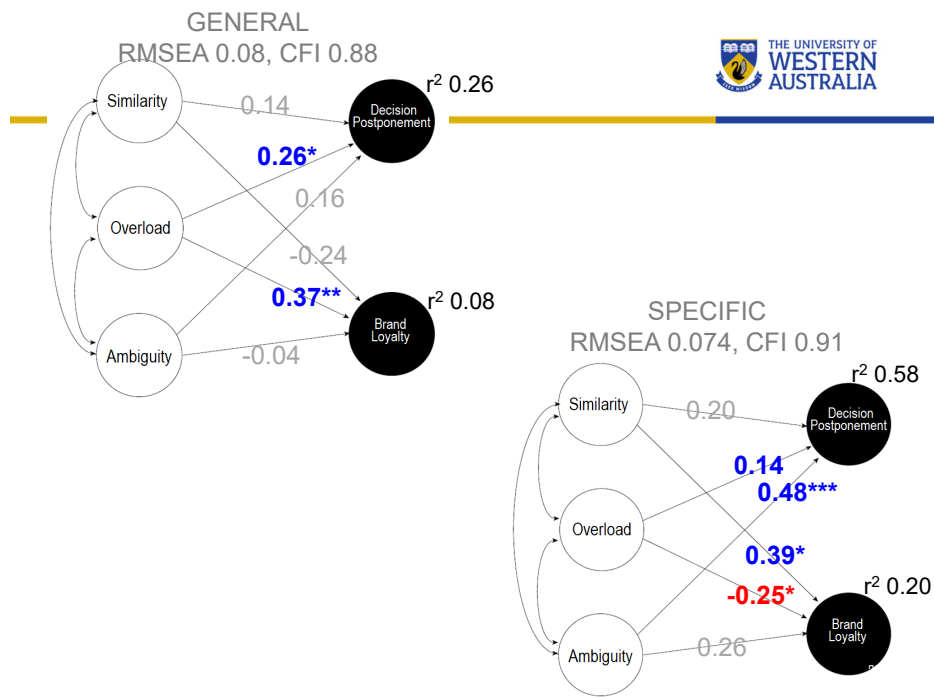
Sample

- ~650 undergraduate students
- As part of the survey random assignment to **General** "financial products" and **Specific** "savings products"



	Similarity	Overload	Ambiguity	Postpone	Loyalty
Similarity	1				
Overload	0.6060	1	non-significant in grey		
Ambiguity	0.5669	0.6852	1		
Postpone	0.5262	0.5996	0.6134	1	
Loyalty	0.4017	0.3057	0.3673	0.2814	1

	Similarity	Overload	Ambiguity	Postpone	Loyalty
Similarity	1				
Overload	0.5714	1	non-significant in grey		
Ambiguity	0.5244	0.6825	1		
Postpone	0.3419	0.4581	0.4201	1	
Loyalty	0.0131	0.1564	0.1503	0.1025	1



Sample

- ~650 undergraduate students
- As part of the survey random assignment to *General* “financial products” and *Specific* “savings products”
- Financial literacy (Fernandes, Lynch, Netemeyer, 2014)
 - Median score 7 Mean 6.8 SD 3.1 (/13)

Correlations

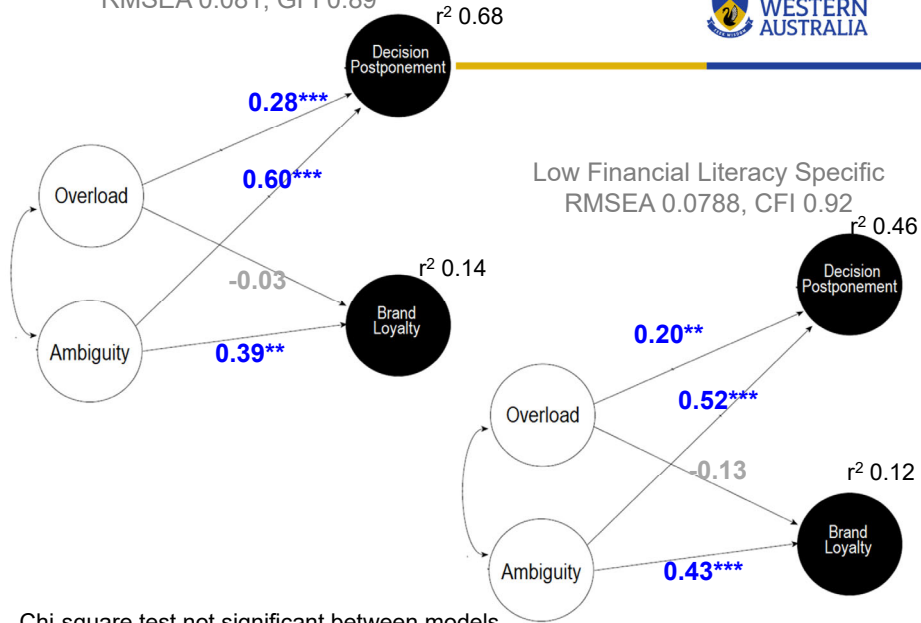
Specific

	Similarity	Overload	Ambiguity	Postpone	Loyalty
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Loyalty	0.4017	0.3057	0.3673	0.2814	1
Fin. Literacy	-0.1490	-0.1753	-0.2565	-0.1705	-0.2165

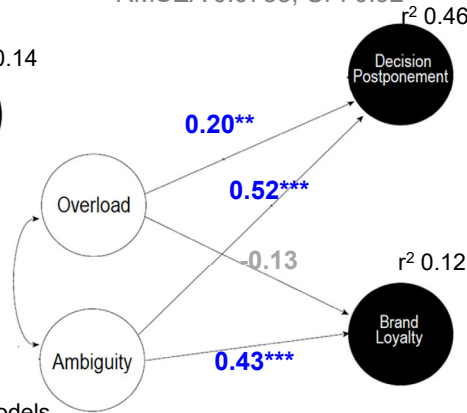
General

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Loyalty	0.0131	0.1564	0.1503	0.1025	1
Fin. Literacy	-0.1139	-0.0523	-0.1676	0.081	-0.0475

High Financial Literacy Specific
RMSEA 0.081, GFI 0.89

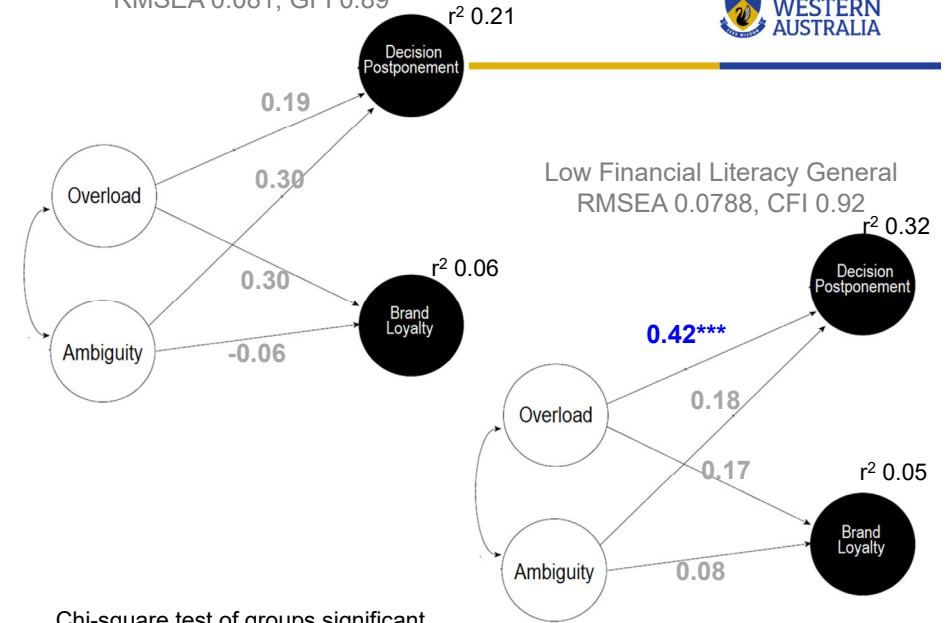


Low Financial Literacy Specific
RMSEA 0.0788, CFI 0.92

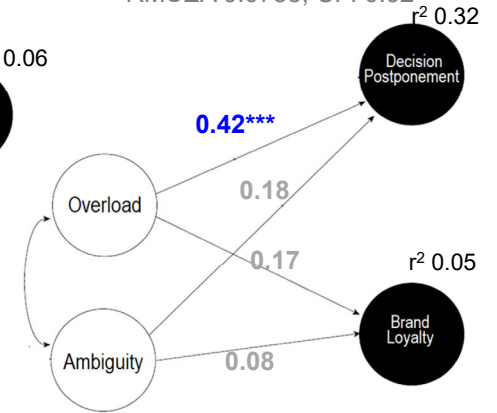


Chi-square test not significant between models

High Financial Literacy General
RMSEA 0.081, GFI 0.89



Low Financial Literacy General
RMSEA 0.0788, CFI 0.92

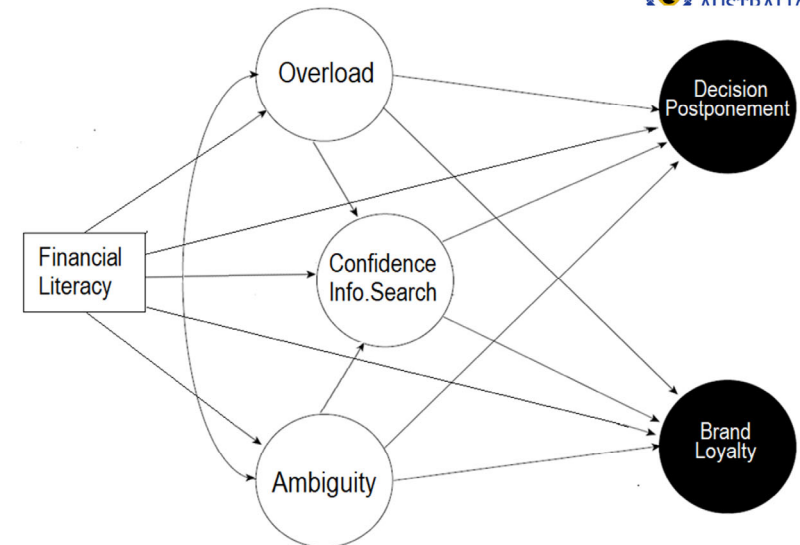


Chi-square test of groups significant

Sample



- ~650 undergraduate students
- As part of the survey random assignment to **General** “financial products” and **Specific** “savings products”
- Financial literacy (Fernandes, Lynch, Netemeyer, 2014)
- **Confidence in Information Search (CIS)** (Fernandes, Lynch, Netemeyer, 2014; Bearden, Hardesty, and Rose 2001)
 - “degree to which an individual feels capable and assured with respect to marketplace decisions and behaviour” (Fernandes, et al. 2014, p.1868)
 - (1 Strongly Disagree to 6 Strongly Agree: Mean Score 2.8 SD 1.2)
 - CIS is expected to:
 - Be predicted (+ve) by financial literacy
 - Mediate the effect of Overload and Ambiguity Confusion on Postponement and Loyalty

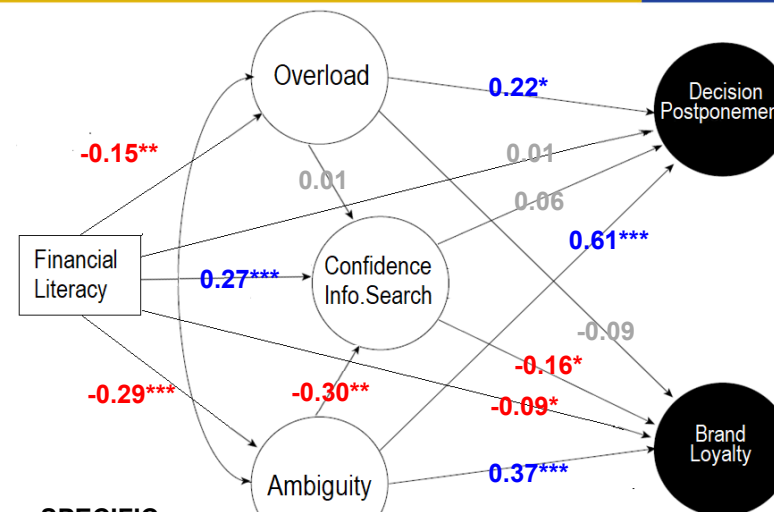


Specific

	Similarity	Overload	Ambiguity	Postpone	Loyalty	Fin. Literacy	Conf. Search
Similarity	1						
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Fin. Literacy	-0.1490	-0.1753	-0.2565	-0.1705	-0.2165	1	
Conf. Search	-0.2020	-0.2884	-0.3342	-0.2263	-0.1105	0.3562	1

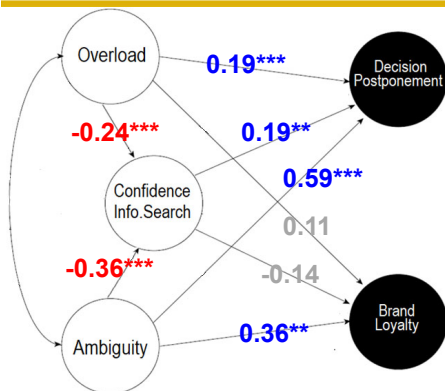
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Fin. Literacy	-0.1139	-0.0523	-0.1676	0.0810	-0.0475	1	
Conf. Search	-0.1754	-0.2807	-0.3037	-0.1320	-0.0522	0.3515	1

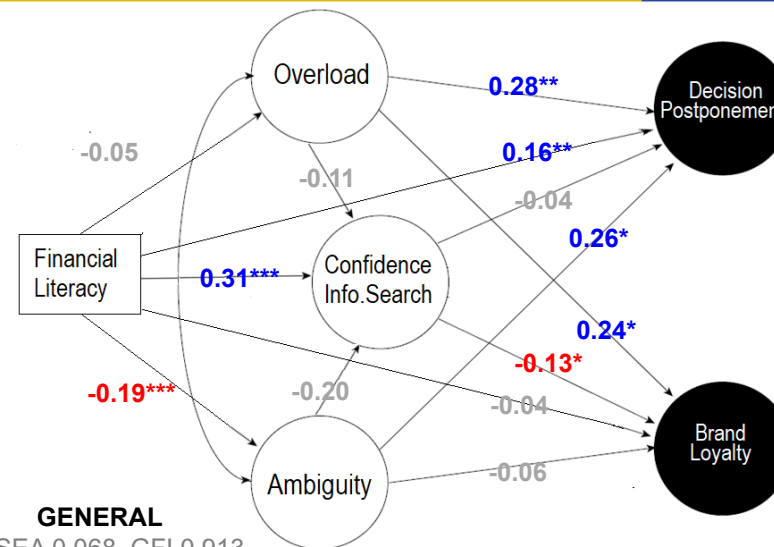
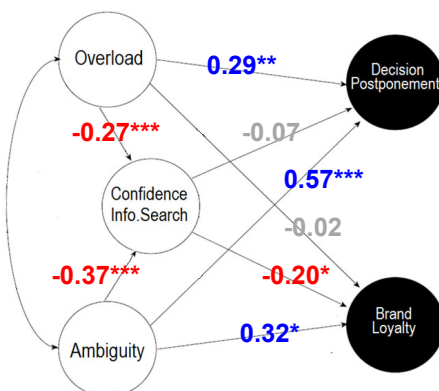


SPECIFIC
RMSEA 0.068, GFI 0.922

Low Financial Literacy Specific

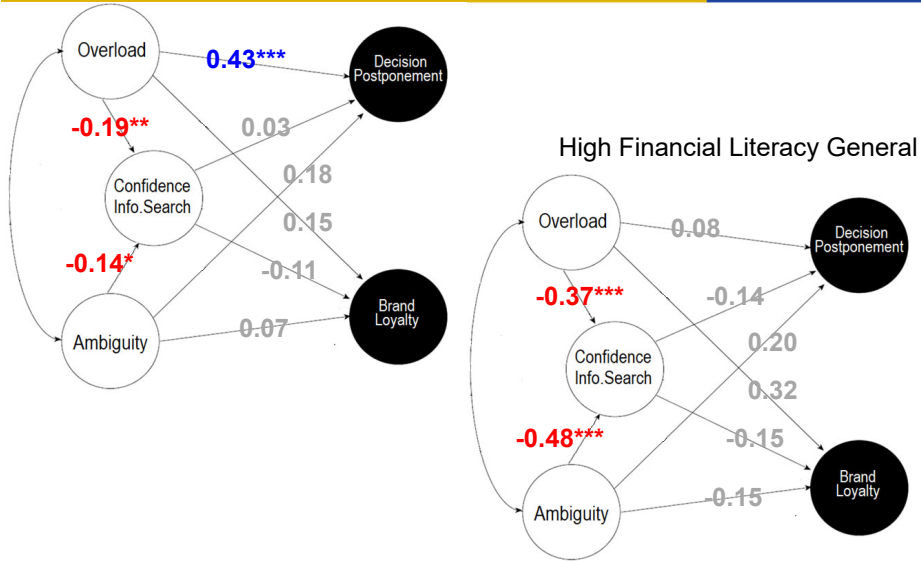


High Financial Literacy Specific



GENERAL
RMSEA 0.068, GFI 0.913

Low Financial Literacy General



Points for discussion

- Fit-for-purpose. Can tests be specified which puts burden of proof on legislator, regulator, producer, to provide evidence that proposed legislation, regulation, product meet minimum threshold of understanding or confusion?
- To what extent is a general trait (confusion proneness) useful across contexts/products